

MARSHALLS ENERGY COMPANY, INC.

**FINANCIAL STATEMENTS AND
ADDITIONAL INFORMATION AND
INDEPENDENT AUDITORS' REPORT**

YEARS ENDED SEPTEMBER 30, 2005 AND 2004

INDEPENDENT AUDITORS' REPORT

Board of Directors
Marshalls Energy Company, Inc.:

We have audited the accompanying statements of net assets of the Marshalls Energy Company, Inc. (MEC), a component unit of the Republic of the Marshall Islands, as of September 30, 2005 and 2004, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of MEC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

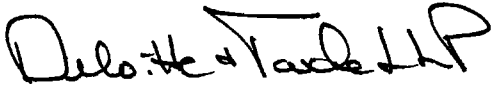
We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan 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 MEC'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, the financial statements referred to above present fairly, in all material respects, the financial position of MEC as of September 30, 2005 and 2004, 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 3 through 6 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 MEC'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.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements of MEC taken as a whole. The accompanying Schedule of Revenues, Expenses and Changes in Net Assets by Source for the year ended September 30, 2005 (page 18) is presented for purposes of additional analysis and is not a required part of the basic financial statements of MEC. This schedule is the responsibility of MEC's management. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 8, 2006, on our consideration of MEC's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

A handwritten signature in black ink, appearing to read "Deloitte & Touche LLP". The signature is stylized and cursive, with the letters "D" and "T" being particularly prominent.

May 8, 2006

MARSHALLS ENERGY COMPANY, INC.

Management's Discussion and Analysis Year Ended September 30, 2005

Marshalls Energy Company (MEC) herewith presents a discussion and analysis of the company's financial performance for the financial year ended 30th September, 2005. It is to be read in conjunction with the financial statements following this section.

FINANCIAL HIGHLIGHTS

MEC's net assets decreased by \$3,165,938 in 2005 compared to a decreased in net assets of \$1,841,431 in 2004. This decrease occurred largely as a result of difficulties experienced during the last quarter of the financial year in securing timely, reasonably priced fuel supplies, which are necessary to maintain normal fuel sales and consequent profits.

The decrease in net assets occurred despite an increase in utility revenue of 13% or \$1,092,519 and an increase in non-utility revenue of 22% or \$2,556,366. Total operating expenses for power generation increased by 37% or \$3,125,641. While the fuel and lube component of these operating costs increased by a massive 50% or \$2,962,664 compared to 2004. The total of all other operating expenses increased marginally by 7% or \$162,977.

FINANCIAL ANALYSIS

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

The Summary Statement of Net Assets for MEC is presented below:

	<u>2005</u>	<u>2004</u>
Current and other assets	\$ 4,719,675	\$ 5,379,672
Capital assets	<u>11,526,838</u>	<u>12,276,709</u>
Total assets	<u>\$16,246,513</u>	<u>\$17,656,381</u>
Current liabilities	\$ 6,549,877	\$ 4,405,685
Non-current liabilities	<u>8,903,917</u>	<u>9,292,039</u>
Total liabilities	<u>15,453,794</u>	<u>13,697,724</u>
Net assets:		
Invested in capital assets	2,110,951	2,495,689
Unrestricted	<u>(1,318,232)</u>	<u>1,462,968</u>
Total net assets	<u>\$ 792,719</u>	<u>\$ 3,958,657</u>

Total assets decreased by \$1,409,868 or 8% from \$17,656,381 in 2004 to \$16,246,513 in 2005. The majority of the decrease is shown as an increase in Accumulated Depreciation of \$1,129,753 from \$7,252,335 in 2004 to \$8,382,088 in 2005. Additionally accounts receivable have been reduced from \$5.2 million to \$4.5 million reflecting management's aggressive policy of debt collection. This has also allowed a reduction in the allowance for bad debts of 8%.

Non current liabilities continued to be reduced through the regular repayments against the power plant loan with the Rural Utilities Services. Current liabilities increased by 49% or \$2,144,192 primarily due to the loss of cash flow discussed earlier relating to uncertain fuel supplies.

MARSHALLS ENERGY COMPANY, INC.

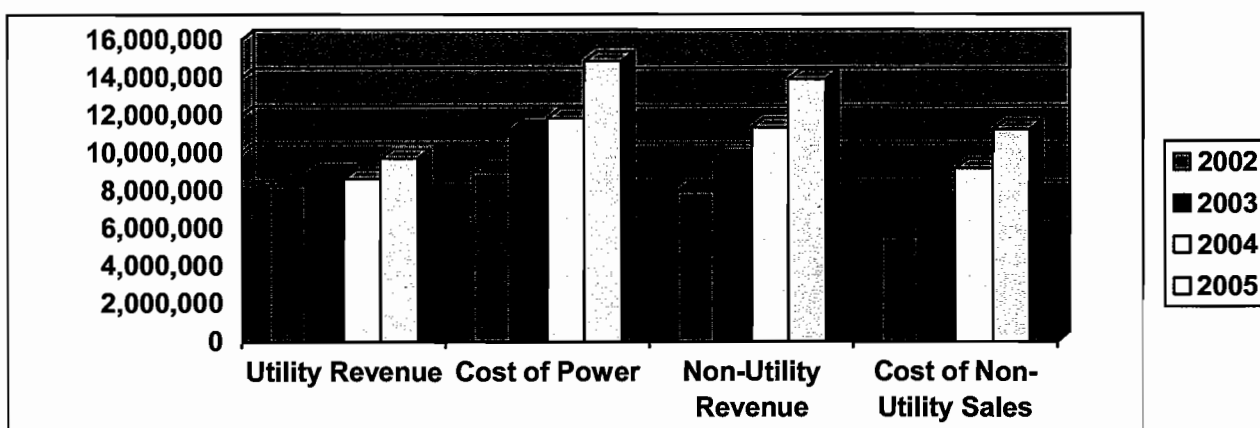
Management's Discussion and Analysis Year Ended September 30, 2005

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

	<u>2005</u>	<u>2004</u>
Revenues:		
Utility revenue	\$ 9,712,058	\$ 8,619,539
Non-utility revenue	<u>14,062,333</u>	<u>11,505,967</u>
Total operating revenue	<u>23,774,391</u>	<u>20,125,506</u>
Expenses:		
Utility expenses	14,869,874	11,848,489
Non-utility expenses	<u>11,864,242</u>	<u>9,655,826</u>
Total operating expenses	<u>26,734,116</u>	<u>21,504,315</u>
Interest expense	(606,213)	(686,616)
Capital contributions	<u>400,000</u>	<u>173,994</u>
Change in net assets	<u>\$ (3,165,938)</u>	<u>\$ (1,841,431)</u>

The Statement of Revenue, Expenses and Changes in Net Assets identifies the various revenue and expense items that contributed to the change in net assets. As indicated above, MEC's total revenues increased by \$3,648,885 or 18% to a total of \$23,774,391 compared to \$20,125,506 in 2004. Electricity billings increased by \$1,092,519 to \$9,712,058 or 13% compared to \$8,619,539 in 2004. Non-Utility revenue, which is basically fuel sales, increased by \$2,556,366 to \$14,062,333 or 22%, compared to \$11,505,967 in 2004. No compact funding was received in 2005. A capital contribution of \$400,000 was received in 2005 from RepMar for the installation of solar home systems in the outer islands.

The graphic below shows the major components of revenue for 2005 compared with 2002, 2003 and 2004:

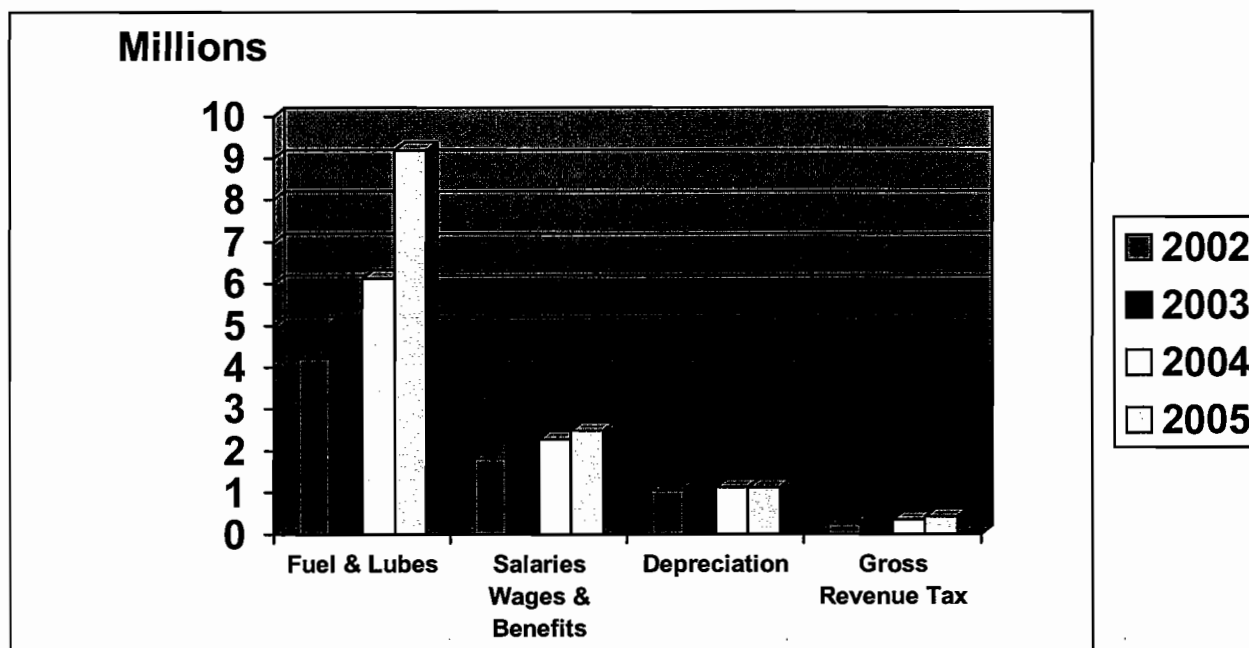


Total expenses increased by a massive \$5,229,801 or 24% from \$21,504,315 in 2004 to \$26,734,116 in 2005. The major contributing factor was the huge increase in the landed cost of fuel. The cost of fuel as a percentage of total generation operating costs has risen from 60% in 2002 to 77% in 2005. This alone represents an increase in fuel and lube costs of \$4.9 million for 2005 compared to 2002. The remaining expenses were relatively stable showing minor increases for the year. This reflects management's continuing commitment to maintain tight and effective control over both expenses and cash flow.

MARSHALLS ENERGY COMPANY, INC.

Management's Discussion and Analysis
Year Ended September 30, 2005

The following graphic shows the major components of operating expenses excluding the cost of fuel sold, for 2005 compared with 2002, 2003 and 2004:



CAPITAL ASSETS

Total Capital Assets before depreciation increased by \$149,769 through the acquisition of miscellaneous plant and equipment amounting to \$113,167, motor vehicles of \$34,700 and office equipment of \$1,902. The net Provision for Depreciation increased by \$1,129,753 in 2005. This, together with the abovementioned acquisitions and additions to capital construction in progress of \$230,113, now totaling \$284,871, gives a decrease in Net Capital Assets of \$749,871.

ECONOMIC FACTORS

MEC will continue to monitor operating expenses and maintain tight fiscal constraints and control over utility receivables in order to further improve cash collections and the net asset position. MEC, as a viable ongoing concern, will continue to depend on the financial support of RepMar in the form of:

- timely payment by RepMar for services provided,
- the collection of long outstanding utility receivables, and
- continuing improvements in operations.

Even though there were two tariff increases during the year in January 2005 and September 2005, a further increase was necessary in November 2005 due to the continuing escalation of world fuel prices. Despite these increases MEC has been able to maintain electricity tariffs at levels which are still among the lowest in the Pacific.

MARSHALLS ENERGY COMPANY, INC.

Management's Discussion and Analysis
Year Ended September 30, 2005

ADDITIONAL FINANCIAL INFORMATION

This discussion and analysis is designed to provide MEC's customers and other stake holders with an overview of the company's operations and financial condition as at 30th September 2005. Should the reader have questions regarding the information included in this report, or wish to request additional financial information, please contact the Marshalls Energy Company, Inc. General Manager at P.O. Box 1439, Majuro, Marshall Islands, MH96960.

MARSHALLS ENERGY COMPANY, INC.

Statements of Net Assets
September 30, 2005 and 2004

<u>ASSETS</u>	<u>2005</u>	<u>2004</u>
Utility plant:		
Electric plant in service	\$ 19,442,193	\$ 19,292,424
Construction work in progress	284,871	54,758
Total utility plant	<u>19,727,064</u>	<u>19,347,182</u>
Less accumulated depreciation and amortization	<u>(8,263,816)</u>	<u>(7,142,048)</u>
Net utility plant	<u>11,463,248</u>	<u>12,205,134</u>
Other assets:		
Nonutility property	181,862	181,862
Less accumulated depreciation	<u>(118,272)</u>	<u>(110,287)</u>
Nonutility property, net	<u>63,590</u>	<u>71,575</u>
Current assets:		
Cash and cash equivalents	<u>712,274</u>	<u>709,863</u>
Accounts receivable:		
Electricity	2,979,131	3,176,148
Affiliates	1,100,697	1,090,394
Other	<u>444,837</u>	<u>966,237</u>
Total accounts receivable	<u>4,524,665</u>	<u>5,232,779</u>
Less allowance for uncollectible accounts	<u>(2,113,583)</u>	<u>(2,292,530)</u>
Net accounts receivable	<u>2,411,082</u>	<u>2,940,249</u>
Materials and supplies	<u>1,585,628</u>	<u>1,707,048</u>
Prepayments	<u>10,691</u>	<u>22,512</u>
Total current assets	<u>4,719,675</u>	<u>5,379,672</u>
Total assets	<u>\$ 16,246,513</u>	<u>\$ 17,656,381</u>

See accompanying notes to financial statements.

MARSHALLS ENERGY COMPANY, INC.

Statements of Net Assets, Continued
September 30, 2005 and 2004

<u>LIABILITIES AND NET ASSETS</u>	<u>2005</u>	<u>2004</u>
Net assets:		
Investment in capital assets, net of related debt	\$ 2,110,951	\$ 2,495,689
Unrestricted	(1,318,232)	1,462,968
Total net assets	<u>792,719</u>	<u>3,958,657</u>
Commitment and contingencies		
Long-term debt:		
RUS mortgage notes less current maturities	<u>8,903,917</u>	<u>9,292,039</u>
Current liabilities:		
Current maturities of long-term debt	511,970	488,981
Accounts payable	5,526,789	3,412,436
Payable to affiliates	56,073	58,745
Accrued taxes	29,772	60,016
Other current and accrued liabilities	<u>425,273</u>	<u>385,507</u>
Total current liabilities	<u>6,549,877</u>	<u>4,405,685</u>
Total net assets and liabilities	<u>\$ 16,246,513</u>	<u>\$ 17,656,381</u>

See accompanying notes to financial statements.

MARSHALLS ENERGY COMPANY, INC.

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Utility operations:		
Operating revenues	\$ 9,712,058	\$ 8,619,539
Operating expenses:		
Cost of power	11,178,752	7,907,035
Administrative and general	1,461,846	1,259,536
Depreciation and amortization	1,089,242	1,084,201
Distribution operations	977,161	1,003,522
Taxes	240,290	226,151
Distribution maintenance	101,530	93,807
Consumer accounts	71,053	274,237
Total operating expenses	<u>15,119,874</u>	<u>11,848,489</u>
Operating loss from utility operations	<u>(5,407,816)</u>	<u>(3,228,950)</u>
Nonutility operations:		
Operating revenues:		
Fuel and gas sales	13,882,183	11,314,817
Other	180,150	191,150
Total operating revenues	<u>14,062,333</u>	<u>11,505,967</u>
Operating expenses:		
Cost of sales	11,231,959	9,168,423
Other	632,283	487,403
Total operating expenses	<u>11,864,242</u>	<u>9,655,826</u>
Operating income from nonutility operations	<u>2,198,091</u>	<u>1,850,141</u>
Operating loss	<u>(3,209,725)</u>	<u>(1,378,809)</u>
Nonoperating income (expense):		
Interest expense	(606,213)	(636,616)
Bad debt recovery	250,000	-
Total nonoperating (expense) income, net	<u>(356,213)</u>	<u>(636,616)</u>
Capital contributions	<u>400,000</u>	<u>173,994</u>
Change in net assets	<u>(3,165,938)</u>	<u>(1,841,431)</u>
Net assets at beginning of year	<u>3,958,657</u>	<u>5,800,088</u>
Net assets at end of year	\$ <u>792,719</u>	\$ <u>3,958,657</u>

See accompanying notes to financial statements.

MARSHALLS ENERGY COMPANY, INC.

Statements of Cash Flows
Years Ended September 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities:		
Cash received from customers	\$ 24,482,505	\$ 19,624,364
Cash payments to suppliers for goods and services	(21,569,939)	(16,457,423)
Cash payments to employees for services	(2,108,855)	(1,968,407)
Net cash provided by operating activities	<u>803,711</u>	<u>1,198,534</u>
Cash flows from capital and related financing activities:		
Capital contributions	400,000	173,994
Acquisition and construction of capital assets	(379,882)	(285,878)
Proceeds from disposal of capital assets	-	5,100
Principal paid on long-term debt	(365,133)	(458,581)
Interest paid on long-term debt	(456,285)	(636,616)
Net cash used for capital and related financing activities	<u>(801,300)</u>	<u>(1,201,981)</u>
Net increase (decrease) in cash and cash equivalents	2,411	(3,447)
Cash and cash equivalents at beginning of year	<u>709,863</u>	<u>713,310</u>
Cash and cash equivalents at end of year	<u>\$ 712,274</u>	<u>\$ 709,863</u>
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (3,209,725)	\$ (1,378,809)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization	1,129,753	1,125,029
Provision for uncollectible accounts receivable	71,053	274,237
(Increase) decrease in assets:		
Accounts receivable:		
Electricity	197,017	158,877
Affiliates	(10,303)	(47,558)
Other	521,400	(608,076)
Materials and supplies	121,420	127,620
Prepayments	11,821	7,869
Increase (decrease) in liabilities:		
Accounts payable	2,114,353	1,391,703
Payable to affiliates	(2,672)	(31,603)
Accrued taxes	(30,244)	(115,352)
Other current and accrued liabilities	(110,162)	294,597
Net cash provided by operating activities	<u>\$ 803,711</u>	<u>\$ 1,198,534</u>

See accompanying notes to financial statements.

MARSHALLS ENERGY COMPANY, INC.

Notes to Financial Statements
September 30, 2005 and 2004

(1) Organization

The Marshalls Energy Company, Inc. (MEC) was granted a corporate charter by the Cabinet of the Republic of the Marshall Islands (RepMar) on February 2, 1984. MEC's principal lines of business are predominantly the generation and transmission of electricity and the buying and selling of petroleum products. Other lines of business include the rental of equipment and accommodation facilities. The principal markets for the generation and transmission of electricity are government agencies, businesses and residential customers located on the atolls of Majuro, Jaluit and Wotje. Petroleum products are sold primarily to foreign and domestic fishing vessels.

MEC's articles of incorporation have authorized the issuance of 100,000 shares of \$1 par value common stock. RepMar owns 75,000 of these shares and MEC retains the remaining 25,000 shares in treasury. These amounts are included in unrestricted net assets in the accompanying statements of net assets.

An exclusive franchise to construct, maintain and operate a distribution system for furnishing electrical power within Majuro Atoll was granted to MEC by RepMar on March 8, 1983. Simultaneously, RepMar leased to MEC, for a nominal amount, a 12-megawatt power plant, a six million gallon capacity fuel storage facility, electrical transmission systems and related facilities on Majuro Atoll. The term of both the lease and the franchise is for a fifty year period commencing on December 1, 1996.

Pursuant to Cabinet Minute C.M. 162(93), RepMar leased to MEC, for a nominal amount, the right to operate and manage the power generating and distribution system in Jaluit Atoll effective November 1, 1993. The term of the lease is for a fifty year period commencing on December 1, 1996.

Through Cabinet action in October 2000, RepMar contracted MEC to develop, operate and maintain power generation systems on Wotje Atoll.

MEC's financial statements are incorporated into the general purpose financial statements of RepMar as a component unit.

(2) Summary of Significant Accounting Policies

The accounting policies of MEC 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. MEC has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

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

MARSHALLS ENERGY COMPANY, INC.

Notes to Financial Statements
September 30, 2005 and 2004

(2) Summary of Significant Accounting Policies, Continued

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

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

- Investment in capital assets; capital assets, net of accumulated depreciation and related debt, 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 total assets. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Cash and Cash Equivalents

For purposes of the statements of net assets and cash flows, cash and cash equivalents is defined as cash on hand, cash held in demand accounts, and time certificates of deposit maturing within ninety days. As of September 30, 2005 and 2004, cash and cash equivalents are \$712,274 and \$709,863, respectively, and the corresponding bank balances are \$389,697 and \$1,812,811, respectively. Of bank balances as of September 30, 2005 and 2004, \$387,105 and \$1,810,219, respectively, are maintained in one financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2005 and 2004, bank deposits in the amount of \$100,000 are FDIC insured. Accordingly, these deposits are exposed to custodial credit risk. MEC does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC coverage are uncollateralized.

MARSHALLS ENERGY COMPANY, INC.

Notes to Financial Statements
September 30, 2005 and 2004

(2) Summary of Significant Accounting Policies, Continued

Receivables

All receivables are due from government agencies, businesses and individuals located within the Republic of the Marshall Islands and are interest free and uncollateralized. The allowance for uncollectible 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.

Allowance for Uncollectible Accounts

Management determines the adequacy of the allowance for uncollectible accounts based upon review of the aged accounts receivable. Amounts determined uncollectible are charged to bad debts and added to the allowance.

Materials and Supplies

Fuel and supplies are valued at the lower of cost (first-in, first-out) or market (net realizable value). Bulk fuel inventories held on consignment for power plant use and for resale are not reflected in the accompanying statements of net assets.

Plant and Nonutility Property

Plant and nonutility property with a cost that equals or exceeds \$500 are capitalized. Such assets are stated at cost. Depreciation of plant and nonutility property and amortization of leasehold land and residences are calculated on the straight-line method based on the estimated useful lives of the respective assets. The estimated useful lives of these assets are as follows:

Power plant engines	20 years
Plant and machinery	3 - 10 years
Vehicles	2 - 4 years
Leasehold improvements	20 years
Residences	20 years
Fences and seawalls	10 years
Leasehold land	20 years
Furniture and fixtures	3 - 5 years

Costs pertaining to distribution and line supplies are expensed during the year of installation as MEC considers the estimated useful lives of these supplies to be less than one year.

New Accounting Standards

In fiscal year 2005, MEC implemented GASB Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB Statement No. 3) and GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. Implementation of GASB Statement Nos. 40 and 42 is reflected in the accompanying financial statements.

Reclassifications

Certain reclassifications have been made to the 2004 financial statements in order to conform with the 2005 presentation.

MARSHALLS ENERGY COMPANY, INC.

Notes to Financial Statements
September 30, 2005 and 2004

(3) Materials and Supplies

Materials and supplies at September 30, 2005 and 2004, consist of the following:

	<u>2005</u>	<u>2004</u>
Distribution and power plant supplies	\$ 1,513,312	\$ 1,576,046
Lubricants	54,629	73,777
Fuel	<u>17,687</u>	<u>57,225</u>
	<u>\$ 1,585,628</u>	<u>\$ 1,707,048</u>

(4) Capital Assets

Capital assets activity for the years ended September 30, 2005 and 2004, was as follows:

	2005			September 30, 2005
	October 1, 2004	Additions	Retirements	
Utility Plant:				
Power plant engines	\$ 14,720,739	\$ -	\$ -	\$ 14,720,739
Plant and machinery	1,674,494	113,167	-	1,787,661
Vehicles	833,721	34,700	-	868,421
Leasehold improvements	641,012	-	-	641,012
Residences	548,284	-	-	548,284
Fences and seawalls	371,702	-	-	371,702
Leasehold land	330,000	-	-	330,000
Furniture and fixtures	172,472	1,902	-	174,374
Nonutility Plant:				
LPG terminal	<u>181,862</u>	-	-	<u>181,862</u>
	<u>19,474,286</u>	<u>149,769</u>	-	<u>19,624,055</u>
Less accumulated depreciation	<u>(7,252,335)</u>	<u>(1,129,753)</u>	-	<u>(8,382,088)</u>
	<u>12,221,951</u>	<u>(979,984)</u>	-	<u>11,241,967</u>
Construction work-in-progress	<u>54,758</u>	<u>230,113</u>	-	<u>284,871</u>
	<u>\$ 12,276,709</u>	<u>\$ (749,871)</u>	<u>\$ -</u>	<u>\$ 11,526,838</u>
	2004			September 30, 2004
	October 1, 2003	Additions	Retirements	
Utility Plant:				
Power plant engines	\$ 14,720,739	\$ -	\$ -	\$ 14,720,739
Plant and machinery	1,612,907	61,587	-	1,674,494
Vehicles	785,266	83,887	(35,432)	833,721
Leasehold improvements	570,964	70,048	-	641,012
Residences	548,284	-	-	548,284
Fences and seawalls	371,702	-	-	371,702
Leasehold land	330,000	-	-	330,000
Furniture and fixtures	164,530	7,942	-	172,472
Nonutility Plant:				
LPG terminal	<u>174,206</u>	<u>7,656</u>	-	<u>181,862</u>
	<u>19,278,598</u>	<u>231,120</u>	<u>(35,432)</u>	<u>19,474,286</u>
Less accumulated depreciation	<u>(6,162,023)</u>	<u>(1,125,029)</u>	<u>34,717</u>	<u>(7,252,335)</u>
	<u>13,116,575</u>	<u>(893,909)</u>	<u>(715)</u>	<u>12,221,951</u>
Construction work-in-progress	<u>-</u>	<u>54,758</u>	-	<u>54,758</u>
	<u>\$ 13,116,575</u>	<u>\$ (839,151)</u>	<u>\$ (715)</u>	<u>\$ 12,276,709</u>

MARSHALLS ENERGY COMPANY, INC.

Notes to Financial Statements
September 30, 2005 and 2004

(5) Taxes Payable

Pursuant to the Income Tax Act of 1989, as amended by the Income Tax Amendment Act of 1991, sales of electricity by public utility companies are exempt from gross revenue tax. Accordingly, MEC is required to pay gross revenue tax on all revenue with the exception of electricity sales at the rate of 3%. As of September 30, 2005 and 2004, MEC is liable for gross revenue tax to RepMar amounting to \$40,820 and \$40,461, respectively.

Pursuant to the Import Duties Act of 1989, as amended by the Import Duties (Amendment) Act of 1996, MEC is exempted from import duties. Pursuant to the Import Duties (Amendment) Act, 2005, no import duty shall be levied on residual fuel oils and diesel oil imported by MEC solely for the purpose of power generation. MEC is, however, required to pay import duty on diesel oil imported for resale.

(6) Notes Payable

	<u>2005</u>	<u>2004</u>
On November 18, 1997, MEC entered into a loan agreement with the Federal Financing Bank (FFB) in the amount of \$12.5 million for the construction of a new power plant, with loan repayments guaranteed by the Rural Utilities Service (RUS). MEC is required to submit drawdown requests to RUS for approval of loan advances. Interest rates are calculated based on the FFB rates at the date of the loan advances and range from 5.49% to 7.25% per annum. Principal and interest are payable in quarterly installments of \$273,770 through January 2, 2018. The mortgage notes have been unconditionally guaranteed by RepMar, under which RepMar will make debt service payments to RUS in the event of default by MEC, and have been collateralized by a leasehold mortgage and security agreement over the assets of MEC. These notes are subject to certain coverage ratio requirements. MEC is not in compliance with these ratio requirements as of September 30, 2005 and 2004.	\$ 9,415,887	\$ 9,781,020
Less current installments	<u>511,970</u>	<u>488,981</u>
Long-term debt	\$ <u>8,903,917</u>	\$ <u>9,292,039</u>

Long-term debt changed during the years ended September 30, 2005 and 2004:

<u>2005</u>				
<u>Balance</u> <u>October 1, 2004</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>September 30, 2005</u>	<u>Balance due</u> <u>in One Year</u>
\$ <u>9,292,039</u>	\$ <u>-</u>	\$ <u>388,122</u>	\$ <u>8,903,917</u>	\$ <u>511,970</u>
<u>2004</u>				
<u>Balance</u> <u>October 1, 2003</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>September 30, 2004</u>	<u>Balance due</u> <u>in One Year</u>
\$ <u>9,781,020</u>	\$ <u>-</u>	\$ <u>488,981</u>	\$ <u>9,292,039</u>	\$ <u>488,981</u>

MARSHALLS ENERGY COMPANY, INC.

Notes to Financial Statements
September 30, 2005 and 2004

(6) Notes Payable, Continued

Future repayment commitments are as follows:

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2006	\$ 511,970	\$ 583,124	\$ 1,095,094
2007	550,388	559,987	1,110,375
2008	724,230	629,359	1,353,589
2009	628,047	467,046	1,095,093
2010	668,314	426,784	1,095,098
2011-2015	4,048,177	1,427,299	5,475,476
2016-2018	<u>2,284,761</u>	<u>184,513</u>	<u>2,469,274</u>
	<u>\$ 9,415,887</u>	<u>\$ 4,278,112</u>	<u>\$ 13,693,999</u>

(7) Related Party Transactions

MEC is wholly-owned by RepMar and is therefore affiliated with all RepMar-owned and affiliated entities. RepMar subscribes for electricity generated by MEC and is charged for electricity usage based on a tariff rate of \$0.14 cents per kilowatt hour for monthly bills less than 500 kilowatt hours, or \$0.205 cents per kilowatt hour for bills greater than 500 kilowatt hours. In addition, RepMar purchases fuel from MEC at the same commercial terms and conditions as afforded to third parties. MEC's receivables from related parties are afforded more favorable payment terms than those extended to unrelated parties.

Total transactions for the years ended September 30, 2005 and 2004, and the related receivables from and payables to affiliates, are as follows:

	<u>2005</u>			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 2,641,052	\$ 585,992	\$ 292,627	\$ 16,058
Majuro Water and Sewer Company, Inc.	220,412	14,575	524,410	502
Marshall Islands Social Security Administration	28,253	159,511	2,664	36,427
Majuro Resort, Inc.	287,073	26,095	73,898	505
Other	<u>1,135,293</u>	<u>53,847</u>	<u>207,098</u>	<u>2,581</u>
	<u>\$ 4,312,083</u>	<u>\$ 840,020</u>	<u>\$ 1,100,697</u>	<u>\$ 56,073</u>
	<u>2004</u>			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 1,963,634	\$ 653,518	\$ 531,336	\$ 1,366
Majuro Water and Sewer Company, Inc.	195,060	33,773	312,548	-
Marshall Islands Social Security Administration	24,658	267,494	1,828	57,379
Majuro Resort, Inc.	277,093	246	86,944	-
Other	<u>747,929</u>	<u>54,336</u>	<u>157,738</u>	<u>-</u>
	<u>\$ 3,208,374</u>	<u>\$ 1,009,367</u>	<u>\$ 1,090,394</u>	<u>\$ 58,745</u>

For the years ended September 30, 2005 and 2004, MEC received capital contributions from RepMar amounting to \$400,000 and \$173,994, respectively.

MARSHALLS ENERGY COMPANY, INC.

Notes to Financial Statements
September 30, 2005 and 2004

(7) Related Party Transactions, Continued

As of September 30, 2005 and 2004, MEC maintained a demand deposit account with an affiliated financial institution, amounting to \$2,592.

(8) Commitment and Contingency

Commitment

MEC purchases petroleum products from Mobil Oil Micronesia, Inc. (Mobil) on a consignment basis whereby Mobil continues to hold ownership and title to the product while it is held in storage at the MEC terminal storage tanks. Title and risk on the product remains with Mobil until the product passes the boundary of the MEC terminal. The value of consignment petroleum products as of September 30, 2005 and 2004 is approximately \$6,570,189 and \$1,030,332, respectively. MEC assumes responsibility for the proper and safe storage/handling of the product while under MEC storage. However, MEC carries insurance coverage on such consignment inventories.

Contingency

Management acknowledges that it is currently dependent on RepMar and its affiliates to pay for actual services rendered in order to maintain MEC as a going concern. Should RepMar and its affiliates choose to discontinue payment for services rendered, MEC management may have to consider alternative measures including, among other possibilities, an increase in electricity and fuel rates to maintain MEC as a going concern.

Pursuant to Cabinet Minute 107 (2005), RepMar has guaranteed MEC's debt to Mobil up to the sum of \$9.3 million and up to thirty days after the invoice date of stock on hand as of December 31, 2005.

As of September 30, 2005, MEC current liabilities exceed current assets by approximately \$1.8 million. Management's plans to reduce this deficiency include entering into new fuel supply contracts with fishing companies, evaluating the financial viability of leasing a portion of the tank farm to a third party, aggressively collecting past due accounts and maintaining the approved pricing template that allows MEC to automatically adjust tariffs for movements in world oil prices.

(9) Risk Management

MEC 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. MEC has elected to purchase commercial insurance from independent third parties for the risks of loss to which it is exposed. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

(10) Subsequent Events

MEC increased electricity tariff rates effective November 1, 2005.

In December 2005, MEC entered into a one year diesel fuel supply contract with a supplier.

On January 13, 2006, MEC entered into a \$3 million and \$2 million bank line of credit facility and promissory note, respectively.

MARSHALLS ENERGY COMPANY, INC.

Schedule of Revenues, Expenses and
Changes in Net Assets by Source
Year Ended September 30, 2005

(With comparative information for the year ended September 30, 2004)

	Generation	Distribution	Contracts	Tank		Wojtje	Namdrik	Mejitt	MEC-Gas	Admin- istration	Totals	
				Farm	Jaluit						2005	2004
Operating revenues:												
Fuel and gas sales	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 407,886	\$ -	\$ 13,882,183	\$ 11,314,817
Cost of sales	-	-	-	(11,036,586)	-	-	-	-	(195,373)	-	(11,231,959)	(9,168,423)
Gross profit on sales	-	-	-	2,437,711	-	-	-	-	212,513	-	2,650,224	2,146,394
Electric and service billings	9,496,962	17,364	-	-	123,021	57,646	17,065	-	-	-	9,712,058	8,619,539
Other income	3,940	77,963	18,000	11,775	18,315	4,499	40	-	944	44,674	180,150	191,150
Total operating revenues, net	9,500,902	95,327	18,000	2,449,486	141,336	62,145	17,105	-	213,457	44,674	12,542,432	10,957,083
Operating expenses:												
Fuel and lubricants	8,935,059	-	-	-	244,510	-	-	-	-	-	9,179,569	6,117,175
Salaries, wages and benefits	928,266	485,147	7,278	82,257	215,645	153,089	4,149	-	38,344	564,672	2,478,847	2,278,300
Repairs and supplies	696,808	489,190	-	94,275	36,482	21,298	1,519	-	27,638	46,302	1,413,512	1,327,321
Depreciation and amortization	858,274	94,709	-	31,743	8,740	23,076	-	-	8,770	104,443	1,129,755	1,125,029
Gross revenue tax	116	2,299	531	397,667	540	133	-	-	12,055	1,317	414,658	342,635
Freight	28,935	52,186	-	790	-	18,113	235	-	102,954	8,349	211,562	-
Diesel import tax	-	-	-	171,334	-	-	-	-	-	-	171,334	88,795
Insurance	83,290	24,427	-	40,413	3,537	1,350	246	-	4,067	10,009	167,339	148,606
Office	3,150	1,858	-	-	21,993	5,125	1,625	-	112,969	112,969	146,720	346,658
Bad debts	-	-	-	-	-	-	-	-	-	71,053	71,053	274,237
Travel	15,222	3,992	-	-	317	123	188	-	-	37,256	57,098	55,615
Staff training	-	-	-	-	-	-	-	-	-	53,694	53,694	76,562
Professional fees	-	-	-	-	-	-	-	-	-	53,063	53,063	10,426
Communications	2,887	5,957	-	390	6,714	-	-	-	991	24,616	41,555	31,384
Entertainment	-	-	-	-	38	554	-	-	-	30,260	30,852	21,968
Laundry and uniforms	8,529	5,454	-	-	10,408	3,084	63	-	-	2,550	30,088	58,871
Equipment rental	1,559	4,059	-	1,330	-	-	-	-	8,090	-	15,038	-
Advertising	-	-	-	-	-	-	-	-	-	6,389	6,389	4,392
Customer claims	3,337	-	-	-	-	-	-	-	-	3,337	3,337	-
Miscellaneous	14,450	3,380	-	1,825	-	-	-	-	125	56,914	76,694	27,918
Total operating expenses	11,579,882	1,172,658	7,809	822,024	548,924	225,945	8,025	-	203,034	1,183,856	15,752,157	12,335,892
Operating income (loss)	(2,078,980)	(1,077,331)	10,191	1,627,462	(407,588)	(163,800)	9,080	-	10,423	(1,139,182)	(3,209,725)	(1,378,809)
Nonoperating income (expense):												
Interest expense	-	-	-	-	-	-	-	-	-	(606,213)	(606,213)	(636,616)
Bad debt recovery	-	-	-	-	-	-	-	-	-	250,000	250,000	-
Total nonoperating income (expense), net	-	-	-	-	-	-	-	-	-	(356,213)	(356,213)	(636,616)
Capital contributions	-	-	-	-	-	-	-	400,000	-	-	400,000	173,994
Change in net assets	\$ (2,078,980)	\$ (1,077,331)	\$ 10,191	\$ 1,627,462	\$ (407,588)	\$ (163,800)	\$ 9,080	\$ 400,000	\$ 10,423	\$ (1,495,395)	\$ (3,165,938)	\$ (1,841,431)

See accompanying independent auditors' report.