MARSHALL ISLANDS SHIPPING CORPORATION

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

FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2010 AND 2009

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Marshall Islands Shipping Corporation:

We have audited the accompanying statements of net assets of the Marshall Islands Shipping Corporation (MISC), a component unit of the Republic of the Marshall Islands (RepMar), as of September 30, 2010 and 2009, and the related statements of revenues, expenses, and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of MISC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

Except as discussed in the following paragraph, we conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of MISC's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Because of the inadequacy of accounting records, we were unable to form an opinion regarding the amount at which copra purchases payable (stated at $200,637) is recorded in the accompanying statement of net assets at September 30, 2009, and the validity of other revenues, cost of goods sold expense, and materials and supplies expense (stated at $336,590, $218,989 and $404,381, respectively) that are recorded in the accompanying statement of revenues, expenses and changes in net assets for the year ended September 30, 2009.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had the accounting records concerning copra purchases payable, other revenues, cost of goods sold expense, and materials and supplies expense been adequate, such financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of MISC as of September 30, 2010 and 2009, 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 8 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 MISC'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 such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 27, 2011 on our consideration of internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte + Touche LLP

July 27, 2011

Marshall Islands Shipping Corporation (MISC) herewith presents a discussion and analysis of MISC's financial performance for the financial year ended September 30, 2010. It is to be read in conjunction with the financial statements following this section.

FINANCIAL HIGHLIGHTS

MISC's net assets decreased by $102,722 (82%) in 2010 compared to a decrease in net assets of $239,269 (66%) in 2009. This decrease in net assets is attributed mainly to the decrease in subsidy from the Republic of the Marshall Islands (RepMar). MISC's subsidy received from RepMar was decreased by $122,697 (11%) from $1,091,847 in 2009 compared to $969,150 in 2010.

Total net operating revenues increased by $26,910 (or 2%) to $1,296,317 in 2010 compared to $1,269,407 in 2009. The revenue generated from the sale of goods aboard the shipping vessels to the various outer islands is the main driver for the slight 2% increase in MISC's revenue for 2010.

Total operating expenses, on the other hand, were $2,368,189 in 2010 compared to $2,600,523 in 2009. MISC decreased its total operating expenses by $232,334 (or 9%) in almost all of its expense line items with only a few minor exceptions. The fuel cost component continues to be the second leading cost factor for MISC and decreased by $48,813 or (11%). The decrease in fuel costs is a result of less number of field trips taken during 2010 due to the deteriorating conditions of the shipping vessels. There were a total of 42 field trips taken during 2010 compared to 61 field trips taken during 2009.

Although MISC was able to successfully reduce its total operating expenses, it is essential to note that MISC's operating expenses for 2010 do not include major repairs and maintenance expenses (i.e. dry docking services) due to insufficient revenue generation and funding availability.

MISC's operating loss decreased by $259,244 (19%) from $1,331,116 in 2009 compared to $1,071,872 in 2010. Despite the slight operating revenue gain and efforts to reduce its operating expenses during 2010, MISC continues to operate at a loss at approximately over $1M annually. Unless management is able to increase its rates with the approval of RepMar, it is expected that MISC will always operate at a loss and must rely heavily on RepMar to subsidize its operations, which accounts for approximately 43% of MISC's revenue during 2010.

FINANCIAL ANALYSIS OF MISC

The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets provide an indication of MISC's financial condition. MISC'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. As illustrated in the figures below, MISC's net assets decreased for the year ended 30th September 2010.

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

	2010	2009	2008
Current and other assets	$ 317,346	$ 297,548	$ 270,106
Capital assets	228,839	283,767	298,020
Total assets	$ 546,185	$ 581,315	$ 568,126

Current liabilities	$ 522,903	$ 455,311	$ 202,853
Total liabilities	522,903	455,311	202,853
Net assets:			
Invested in capital assets	228,839	283,767	298,020
Unrestricted	(205,557)	(157,763)	67,253
Total net assets	23,282	126,004	365,273
Total net assets	$ 546,185	$ 581,315	$ 568,126

Total assets have increased from $568,126 in 2008 to $581,315 in 2009 but have decreased to $546,185 in 2010. The slight increase in total assets by $13,189 (2%) from 2008 to 2009 is due to an increase in current assets by $27,442 (10%) and a decrease in capital assets by $14,253 (5%). In 2010, the decrease in total assets by $35,130 (6%) is due to an increase in current assets by $19,798 (7%) and a decrease in capital assets by $54,928 (19%).

Net capital assets decreased slightly from $298,020 in 2008 to $283,767 in 2009 and decreased further to $228,839 in 2010. In 2010, net capital assets decreased by $54,928 (19%) as a result of the annual depreciation charge of $84,572 offset by the purchases of miscellaneous equipment, motor boats, and furniture in the amount of $15,021 and the purchase of vehicles costing $14,623.

Total liabilities increased significantly from $202,853 in 2008 to $455,311 in 2009 and increased further to $522,903 in 2010. The $252,458 (124%) increase in total liabilities from 2008 to 2009 is primarily due to copra purchase payables taken over by MISC from Tobolar Copra Processing Plant, Inc. (Tobolar) during 2009. In 2010, total liabilities increased by $67,592 (15%). Copra purchases payable decreased by $99,747 (50%) and offset by an increase in deposit from Tobolar for the amount of $100,000 as per the agreement entered with Tobolar to lend MISC the funds for paying copra producers in the outer islands. All other current liabilities (Accounts Payables, Payables to affiliates and Other) increased by $67,339 (26%).

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

	2010	2009	2008
Operating revenues	$ 1,296,317	$ 1,269,407	$ 1,500,688
Operating expenses	2,368,189	2,600,523	2,682,755
Operating loss	(1,071,872)	(1,331,116)	(1,182,067)
RMI Subsidy	969,150	1,091,847	1,008,150
Change in Net Assets	$ (102,722)	$ (239,269)	$ (173,917)

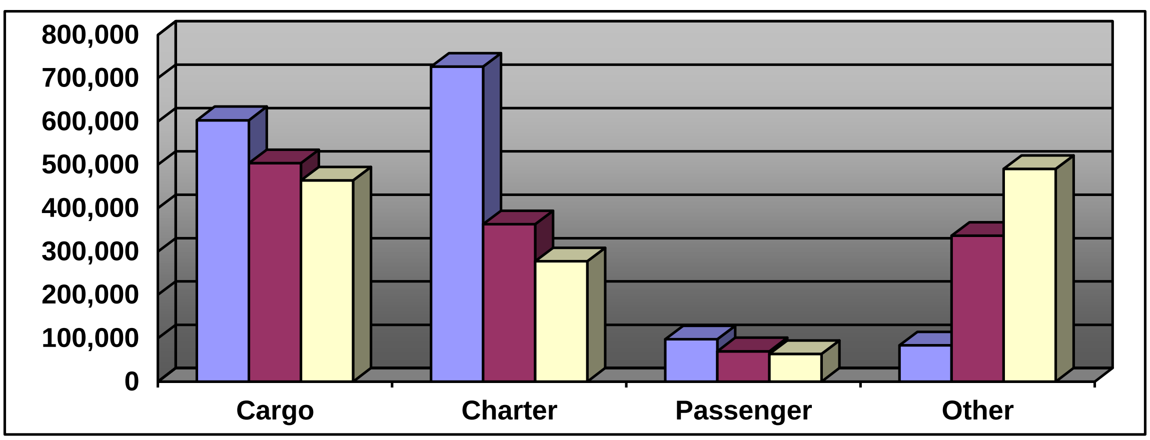
The Statements of Revenue, Expenses and Changes in Net Assets identify the various revenue and expense items that contributed to the change in net assets. MISC's total revenue decreased significantly in 2009 by $231,281 (15%) to a total of $1,269,407 compared to $1,500,688 in 2008. In 2010, MISC's total revenue slightly increased by $26,910 (2%) to a total of $1,296,317. The significant decline in MISC's revenue during 2009 is primarily from MISC's top two revenue sources (Charter and Cargo) and was due to the adverse affects of the global fuel crisis resulting in a reduction in the number of fieldship trips in 2009.

Charter revenue decreased by $363,231 (50%) to $363,427 in 2009 from $726,658 in 2008. Additionally for 2009, cargo revenue decreased by $99,024 (16%) to $504,114 and passenger revenue decreased by $27,854 (28%) to $69,965. In 2010, charter revenue decreased further by $86,031 (24%) to $277,396; cargo revenue decreased further by $40,026 (8%); and passenger revenue further decreased by $6,017 (9%). Although there was a bit of relief in fuel prices during 2010, MISC has yet to recover from its loss in revenue due to less fieldship trips in 2010 due to deteriorating conditions of the shipping vessels. From 2008, MISC's major sources of revenue through the charter, cargo and passenger revenue have continued on a declining trend.

In lieu of the global fuel crisis, private vendors (i.e. Payless) sales of goods aboard the shipping vessels to the outer island consumers ceased and was resumed by MISC operations in 2009. Accordingly, MISC recorded new revenue sources for the sale of goods in 2009 and 2010 of $228,414 and $398,196, respectively. Furthermore, MISC began collecting copra on behalf of Tobolar in 2009, which resulted in another new revenue source for copra buying fees in 2009 and 2010 of $59,589 and $78,067, respectively.

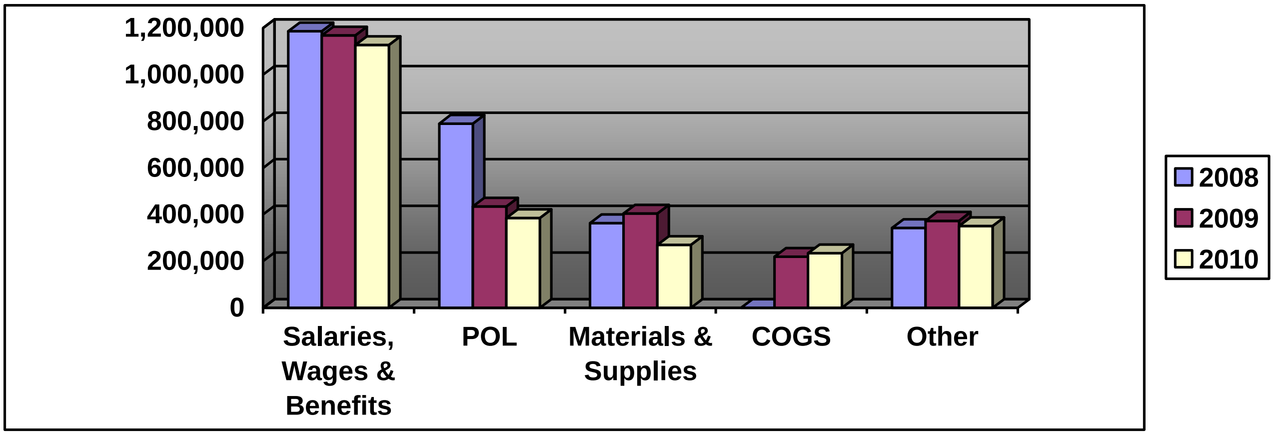
The operating loss before non-operating revenues (i.e. RepMar subsidy) for 2010 was $1.07M in 2010 compared to $1.33M and $1.19M in 2009 and 2008, respectively. The increase in operating loss by $149,049 (13%) in 2009 is primarily due to the global fuel crisis which resulted in significant decrease in revenue generated by the Charter, cargo and passenger sources. In 2010, the operating loss decreased by $259,244 (19%) due to MISC efforts to reduce its operational costs and ability to maintain its revenue stream.

Operating subsidies of $969,150 were received in 2010 compared to $1,091,847 in 2009 and $1,008,150 in 2008. The subsidy received from RepMar increased by $83,697 (8%) and decreased by $122,697 (11%) in 2009 and 2010, respectively. MISC did not receive any capital contributions from RepMar during 2010, 2009 and 2008. With its current rate structure, MISC is not able to cover its operational cost without financial support from RepMar. The graphic below shows the major components of MISC's operating revenue from 2008 through to 2010:



MISC's total operating expenses have been on a decreasing trend. Total operating expenses decreased by $82,232 (3%) from $2.68M in 2008 compared to $2.60M in 2009. In 2010, total operating expenses decreased significantly by $232,334 (10%) to $2.37M. Overall, MISC was able to reduce its operational expenses in almost all of its expense line items, particularly with the following top three components of operating expenses: (1) Salaries, Wages and Benefits, (2) Petroleum, Oil & Lube (POL), and (3) Materials and Supplies.

The following graphic shows the major components of operating expenses from 2008 through to 2010:



Salaries, wages and benefits remain as the leading operational expense. As illustrated in the above graph, MISC has consistently decreased this operating expense component over the past years. The salaries, wages, and benefits expense decreased by $17,034 (1%) from $1.19M in 2008 to $1.17M in 2009 and decreased further by $41,553 (4%) to $1.13M in 2010.

Similarly, POL expenses have also been on a declining trend. POL expenses decreased significantly by $356,048 (45%) from $790,470 in 2008 to $434,422 in 2009 and decreased further by $48,813 (11%) to $385,609 in 2010. The declining trend in fuel costs in 2009 is in line with the decrease in global fuel prices after the 2008 fuel crisis. The decrease in fuel costs in 2010, however, is a result of less fieldship trips made by MISC due to the deteriorating conditions of the shipping vessels. MISC field trips to the outer island decreased by 31% for a total of 42 field trips as opposed to 61 field trips taken in both 2008 and 2009. The shipping vessels were taken out of service to allow for repairs that needed to be completed. In 2010, the average cost of fuel per field trip was $10,343 compared to $5,837 and $12,959 in 2009 and 2008, respectively.

Materials and supplies expenses increased slightly by $40,449 (11%) from $363,932 in 2008 to $434,422 in 2009 and decreased significantly by $134,798 (33%) in 2010. The challenges of limited revenue and funding availability facing MISC today is a main factor in the significant decrease in materials and supplies during 2010. Without sufficient cash injection, MISC is not able to proceed with major and ongoing repairs and maintenance necessary for the up keeping of the shipping vessels.

Cost of goods sold (COGS) is an operating expense component introduced in 2009 for the sale of goods service aboard the shipping vessels to the outer island consumers. COGS increased by $15,796 (7%) from $218,989 in 2009 to $234,785 in 2010. Most importantly, the revenue generated from the sale of goods increased by $169,782 (74%) to $398,196 in 2010 compared to $228,414 in 2009. As an indicator of its success for an alternative source of income for MISC, the gross margin for the sale of goods increased in 2010.

CAPITAL ASSETS AND DEBT

Net capital assets decreased by $54,928 in 2010 as a result of total depreciation for the year of $84,572 less the acquisition of equipment, vehicles, motor boats and furniture in the amount of $29,644.

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

MISC did not incur any long-term debt during the year nor did MISC have any outstanding long-term debt at the end of the year.

CASH FLOW

Net cash used for operating activities for 2010 was $1.11M compared to net cash used for operating activities of $0.99M in 2009 and $0.91M in 2008. The cash provided by operational activities was absorbed entirely by MISC's operational costs. Additionally, injection of cash flow from RepMar subsidies were received in the amount of $0.97M, $1.09M and $1.06M during 2010, 2009 and 2008, respectively. Similarly, RepMar subsidies were utilized by MISC to cover its operational expenses.

FUTURE OUTLOOK ON SUSTAINABILITY

MISC plays an important role in the lives of people living in the outer islands. The regular fieldtrip services are essential to transfer people and basic needs from the Capital city to the Outer Islands and vice versa.

As an indicator of MISC's future outlook on sustainability, MISC's net assets are not in a deficiency status as of yet but have been on a declining trend over the past years. MISC's net assets decreased significantly by $239,269 (66%) from $365,273 in 2008 to $126,004 in 2009 and decreased even further by $102,722 (82%) to $23,282 in 2010. With MISC's declining trend in net assets, management expects MISC's net assets to reach deficiency status by 2011. As such, this marks a critical time for MISC to develop and implement short term and long term strategic goals for the future viability and sustainability of MISC.

Historically, the operating revenue generated by MISC has never been sufficient enough to cover the related expenses necessary to operate the shipping vessels and sea-transport services provided. With operating losses over $1M annually, MISC continues to be dependent on financial support from RepMar. Most importantly, MISC is not able to generate sufficient revenue through its operations due to its low rate structure. There hasn't been a rate increase of any kind for the sea-transport services since the establishment of MISC. As a state owned entity, MISC is not able to increase its rates without the approval of RepMar. MISC has made numerous requests to RepMar but have yet to be successful.

It is the intention of MISC to continue its lobbying efforts for the authority and flexibility to increase its rates to account for inflation and the fluctuation of fuel costs.

The future outlook on sustainability for MISC is also threatened by the deteriorating conditions of the shipping vessels. Due to budget constraints, MISC has not been able to ensure that the shipping vessels undergo the requirements of dry docking services. MISC was forced to scale back on its field trip schedule for necessary repairs and maintenance on the shipping vessels. Unfortunately, MISC's efforts could not prevent the loss of one of its shipping vessels in January 2011. MISC cannot continue to operate with the conditions of its shipping vessels today. The current shipping vessel fleet must be taken out of service for dry docking.

To summarize, MISC's future outlook on sustainability is dependent on, but not limited to, the following factors:

- Approval from RepMar to increase MISC's rate structure,
- Ongoing recipient of RepMar subsidy,
- Dry dock existing shipping vessel fleet,
- Seek opportunities to replace and add to the existing fleet,
- Establish a repairs and maintenance account,
- Explore other financing opportunities (i.e. ADB, World Bank, RUS, etc.)
- Continue with budgetary controls to minimize operational expenses where possible.

MISC FOCUS IN THE COMING FISCAL YEAR

MISC's focus in the coming fiscal year includes, but is not limited to, the following:

- MISC will submit a proposal and obtain approval from Cabinet to increase MISC rates. As previously mentioned, MISC cannot continue to operate with its current rate structure. At a minimum, MISC goal is to propose a rate increase to cover the fluctuating cost of fuel.
- MISC will seek/recruit assistance from available resources such as ADB and other consultants to develop a Comprehensive Recovery Plan (CRP) for MISC.
- MISC will implement JICA study for MISC shipping vessels repair and maintenance plan. With the sinking of one of MISC's shipping vessels, a team of experts provided by JICA have conducted and completed an assessment study to assess MISC's shipping vessel needs and establish a repairs and maintenance costing schedule.
- MISC will begin the process of dry docking for its existing shipping vessel fleet for which financial support from RepMar is critical.

ADDITIONAL FINANCIAL INFORMATION

This discussion and analysis is designed to provide MISC's customers and other stake holders with an overview of the company's operations and financial condition as at September 30, 2010. Should the reader have questions regarding the information included in this report, or wish to request additional financial information, please contact the Marshall Islands Shipping Corporation General Manager at P.O. Box 1198, Majuro, Marshall Islands, MH 96960.

MARSHALL ISLANDS SHIPPING CORPORATION

Statements of Net Assets
September 30, 2010 and 2009

ASSETS	2010	2009
Current assets:		
Cash	$ 153,409	$ 226,780
Receivables:		
Affiliates	158,197	37,454
Trade	15,904	50,401
Employees	3,341	3,167
	177,442	91,022
Less allowance for doubtful accounts	(21,861)	(29,226)
Total receivables, net	155,581	61,796
Inventory	8,356	8,972
Total current assets	317,346	297,548
Equipment, net	228,839	283,767
	$ 546,185	$ 581,315
LIABILITIES AND NET ASSETS		
Current liabilities:		
Accounts payable	$ 59,332	$ 79,827
Payable to affiliates	156,148	70,338
Copra purchases payable	100,890	200,637
Accrued payroll liabilities	106,533	104,509
Advance from Tobolar	100,000	-
Total liabilities	522,903	455,311
Commitment and contingency		
Net assets:		
Invested in capital assets	228,839	283,767
Unrestricted	(205,557)	(157,763)
Total net assets	23,282	126,004
	$ 546,185	$ 581,315

See accompanying notes to financial statements.

MARSHALL ISLANDS SHIPPING CORPORATION

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2010 and 2009

	2010	2009
Operating revenues:		
Cargo	$ 464,088	$ 504,114
Ship sales	398,196	228,414
Charter	277,396	363,427
Copra fee	78,067	59,589
Passenger	63,948	69,965
Other	14,622	48,587
	1,296,317	1,274,096
Less provision for doubtful accounts	-	(4,689)
Total operating revenues	1,296,317	1,269,407
Operating expenses:		
Salaries, wages and benefits	1,127,409	1,168,962
Petroleum, oil and lube	385,609	434,422
Material and supplies	269,583	404,381
Cost of goods sold	234,785	218,989
Foodstuffs	130,961	173,083
Depreciation	84,572	78,597
Rent	42,942	9,924
Utilities	23,336	12,010
Travel and entertainment	9,847	16,554
Repairs and maintenance	6,951	8,159
Professional fees	5,428	32,014
Contributions	4,266	7,515
Miscellaneous	42,500	35,913
Total operating expenses	2,368,189	2,600,523
Operating loss	(1,071,872)	(1,331,116)
Nonoperating revenues:		
Operating subsidies	969,150	1,091,847
Change in net assets	(102,722)	(239,269)
Net assets at beginning of year	126,004	365,273
Net assets at end of year	$ 23,282	$ 126,004

See accompanying notes to financial statements.

MARSHALL ISLANDS SHIPPING CORPORATION

Statements of Cash Flows
Years Ended September 30, 2010 and 2009

	2010	2009
Cash flows from operating activities:		
Cash received from customers	$ 1,202,532	$ 1,287,174
Cash payments to suppliers for goods and services	(1,190,024)	(1,114,577)
Cash payments to employees for services	(1,125,385)	(1,163,863)
Net cash used for operating activities	(1,112,877)	(991,266)
Cash flows from noncapital financing activities:		
RepMar subsidy received	969,150	1,091,847
Advance from Tobolar	100,000	-
Net cash provided by noncapital financing activities	1,069,150	1,091,847
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(29,644)	(64,344)
Net change in cash	(73,371)	36,237
Cash at beginning of year	226,780	190,543
Cash at end of year	$ 153,409	$ 226,780
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	$ (1,071,872)	$ (1,331,116)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	84,572	78,597
Bad debts	-	4,689
(Increase) decrease in assets:		
Receivables:		
Affiliates	(120,743)	19,588
Trade	27,132	(9,385)
Employees	(174)	2,875
Inventory	616	(8,972)
Increase (decrease) in liabilities:		
Accounts payable	(20,495)	57,527
Payable to affiliates	85,810	(10,805)
Copra purchases payable	(99,747)	200,637
Accrued payroll liabilities	2,024	5,099
Net cash used for operating activities	$ (1,112,877)	$ (991,266)

See accompanying notes to financial statements.

(1) Organization

The Marshall Islands Shipping Corporation (MISC), a component unit of the Republic of the Marshall Islands (RepMar), was created under Public Law 2005-41, the Marshall Islands Shipping Corporation Act, 2004. MISC was established to manage and operate RepMar's shipping vessels. MISC's principal line of business is to provide sea transportation services; to carry on business as ship owners; and to build and maintain ships and vessels.

MISC is governed by a five-member Board of Directors, including one official each from the Ministry of Finance and the Marshall Islands Ports Authority and three members appointed by the Cabinet of RepMar.

MISC'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 MISC 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. MISC has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

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

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

- Invested in capital assets; capital assets, net of accumulated depreciation, plus construction or improvement of those assets.

- Unrestricted; net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

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.

(2) Summary of Significant Accounting Policies, Continued

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 statement 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. MISC considers revenues and costs that are directly related to operations of shipping vessels to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

Cash

Custodial credit risk is the risk that in the event of a bank failure, MISC's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. MISC does not have a deposit policy for custodial credit risk.

For purposes of the statements of net assets and cash flows, cash is defined as cash on hand and cash held in demand accounts. As of September 30, 2010 and 2009, the carrying amount of cash was $153,409 and $226,780, respectively, and the corresponding bank balances were $139,730 and $56,801, respectively, which were maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2010 and 2009, bank deposits in the amount of $139,730 and $56,801, respectively, were FDIC insured. MISC does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

Receivables

All receivables are uncollateralized and are due from affiliates or customers, located within the Republic of the Marshall Islands. 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 evaluation of the collectability of these accounts. The allowance is established through a provision for bad debts charged to expense.

Inventory

Inventory consists of items purchased for resale (on the ships) during outer islands voyages. Inventory is valued at the lower of cost (first-in, first out FIFO) or market value (net realized value).

Equipment

MISC has not adopted a formal capitalization policy for equipment; however, items with a cost that equals or exceeds $1,000 are generally capitalized. Depreciation is calculated using the straight-line method based on the estimated useful lives of the respective assets. The estimated useful lives of these assets is 5 years.

(2) Summary of Significant Accounting Policies, Continued

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 receipts tax of 3% on revenues. MISC is specifically exempt from this tax.

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits. As of September 30, 2010 and 2009, the accumulated vacation leave liability totals $69,779 and $68,658, respectively, and is included within the statements of net (liabilities) assets as other liabilities and accruals.

Revenue Recognition

Cargo, charter and passenger revenue are recognized when the transportation is provided. Other components of other operating revenue are recognized as revenue when the related goods and services are provided.

New Accounting Standards

During fiscal year 2010, MISC implemented the following pronouncements:

- GASB 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.

- GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which is intended to improve how state and local governments report information about derivative instruments - financial arrangements used by governments to manage specific risks or make investments - in their financial statements.

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

- GASB Statement No. 58, *Accounting and Financial Reporting for Chapter 9 Bankruptcies*, which provides guidance for governments that have petitioned for protection from creditors by filing for bankruptcy under Chapter 9 of the United States Bankruptcy Code, and establishes requirements for recognizing and measuring the effects of the bankruptcy process on assets and liabilities, and for classifying changes in those items and related costs.

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

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In March 2009, GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The provisions of this statement are effective for periods beginning after June 15, 2010. Management has not evaluated the effect that the implementation of this statement will have on the financial statements of MISC.

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

In June 2010, GASB issued Statement No. 59, *Financial Instruments Omnibus*, which updates and improves existing standards regarding financial reporting of certain financial instruments and external investment pools. The provisions of this statement are effective for periods beginning after June 15, 2010. Management has not evaluated the effect that the implementation of this statement will have on the financial statements of MISC.

Reclassifications

Certain reclassifications have been made to the 2009 financial statements to conform with the 2010 presentation.

(3) Risk Management

MISC 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. MISC has elected to purchase commercial automobile insurance from independent third parties for the risks of loss to which it is exposed with respect to the use of motor vehicles. Settled claims have not exceeded this commercial coverage for the last three years. MISC does not maintain general liability insurance; maritime insurance; and fire, lightning and typhoon insurance for its office building and contents. In the event of an insurable loss, MISC may be self-insured to a material extent.

(4) Equipment

Capital asset activity during the years ended September 30, 2010 and 2009 is as follows:

	2010			
	October 1, 2009	Additions	Retirements	September 30, 2010
Equipment	$ 300,369	$ 4,717	$ -	$ 305,086
Vehicles	108,949	14,623	-	123,572
Furniture	8,495	1,366	-	9,861
Motor boats	14,000	8,938	-	22,938
	431,813	29,644	-	461,457
Less accumulated depreciation	(148,046)	(84,572)	-	(232,618)
	$ 283,767	$ (54,928)	$ -	$ 228,839

	2009			
	October 1, 2008	Additions	Retirements	September 30, 2009
Equipment	$ 271,525	$ 28,844	$ -	$ 300,369
Vehicles	78,949	30,000	-	108,949
Furniture	8,495	-	-	8,495
Motor boats	8,500	5,500	-	14,000
	367,469	64,344	-	431,813
Less accumulated depreciation	(69,449)	(78,597)	-	(148,046)
	$ 298,020	$ 14,253	$ -	$ 283,767

(5) Related Party Transactions

MISC was created by the Nitijela of RepMar under Public Law 2005-41 and is thus considered a component unit of RepMar. Accordingly, MISC is affiliated with all RepMar-owned and affiliated entities, including Tobolar Copra Processing Plant, Inc. (Tobolar).

A summary of related party transactions for the years ended September 30, 2010 and 2009 is as follows:

	2010			
	Revenues	Expenses	Receivables	Payables
Tobolar	$ 444,545	$ -	$ 138,116	$ -
Marshall Islands Social Security Administration	-	209,376	-	74,250
Marshalls Energy Company, Inc.	_-	317,607	-	7,858
Majuro Water and Sewer Company, Inc.	-	6,483	-	1,200
Republic of the Marshall Islands	57,645	17,761	20,081	55,399
Other	1,089	49,487	-	17,441
	$ 503,279	$ 600,714	$ 158,197	$ 156,148

	2009			
	Revenues	Expenses	Receivables	Payables
Tobolar	$ 365,668	$ -	$ 8,607	$ -
Marshall Islands Social Security Administration	-	103,773	-	50,301
Marshalls Energy Company, Inc.	400	319,713	-	1,323
Majuro Water and Sewer Company, Inc.	-	3,466	-	-
Republic of the Marshall Islands	182,667	2,579	28,847	10,666
Other	1,126	10,577	-	8,048
	$ 549,861	$ 440,108	$ 37,454	$ 70,338

(5) Related Party Transactions, Continued

During the years ended September 30, 2010 and 2009, the operations of MISC were funded by appropriations, totaling $969,150 and $1,091,847, respectively, from the Nitijela of RepMar.

MISC occupies certain office space and utilizes four vessels belonging to RepMar at no cost. No lease agreements have been executed to formalize these arrangements. However, management is of the opinion that no rental payments for the use of these properties are anticipated. The fair value of these contributions is presently not determinable. Accordingly, the contributed use of facilities has not been recognized as revenue and expense in the accompanying financial statements. One of the vessels belonging to RepMar, Jeljelat Ae, sank on January 1, 2011 (note 7).

During the year ended September 30, 2010, Tobolar advanced $100,000 to MISC for the purpose of assisting MISC with the purchase of copra from growers in the outer islands. The term of the advance is for one year and is non-interest bearing.

(6) Commitment and Contingency

Commitment

The Company leases its warehouse for $40,714 per annum with the RMI Port Authority. This lease expires on July 31, 2014. The Company recorded $40,714 rent expense for the year ended September 31, 2010.

Total minimum future rental payments for non-cancelable lease agreement is as follows:

Year ending September 30,	
2011	$ 40,714
2012	40,714
2013	40,714
2014	33,928
	$ 156,070

Contingency

MISC receives a substantial amount of its revenue from annual RepMar appropriations. A significant reduction in the level of budgetary support from RepMar, if this were to occur, may have an effect on MISC's programs and activities. For the year ended September 30, 2011, RepMar appropriated funding to MISC in the amount of $1,150,500 for the purpose of funding operations.

(7) Subsequent Event

The MV Jeljelat Ae sank on January 1, 2011. No loss was recorded by MISC for this event as the vessel is owned by RepMar.