

MAJURO RESORT, INC.
(A COMPONENT UNIT OF THE REPUBLIC
OF THE MARSHALL ISLANDS)

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2016 AND 2015

MAJURO RESORT, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Years Ended September 30, 2016 and 2015
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INDEPENDENT AUDITORS' REPORT

Board of Directors
Majuro Resort, Inc.:

Report on the Financial Statements

We have audited the accompanying financial statements of Majuro Resort, Inc. (MRI), a component unit of the Republic of the Marshall Islands, which comprise the statements of net position as of September 30, 2016 and 2015, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Majuro Resort, Inc. as of September 30, 2016 and 2015, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis-of-Matter

Going Concern

The accompanying financial statements have been prepared assuming that MRI will continue as a going concern. As discussed in Note 6 to the financial statements, MRI's recurring losses from operations raise substantial doubt about its ability to continue as a going concern. Management's plans concerning these matters are also discussed in Note 6 to the financial statements. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

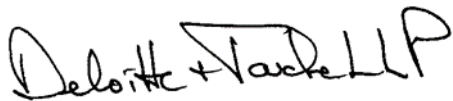
Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 to 8 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 9, 2017, on our consideration of MRI's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering MRI's internal control over financial reporting and compliance.



June 9, 2017

MAJURO RESORT, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Management's Discussion and Analysis
Years Ended September 30, 2016 and 2015

This section of the Majuro Resort, Inc. (MRI) annual financial report presents our discussion and analysis of MRI's financial performance for the fiscal year that ended on September 30, 2016. The discussion and analysis should be read in conjunction with the audited financial statements, which follow this section.

Financial Highlights

Total assets increased by \$26,795 or 1% from \$1,863,355 in 2015 to \$1,890,150 in 2016. The increase in total assets was mainly the effect of the increase in cash reserves at the end of the fiscal year by \$135,329 offset by the decrease in net receivables by \$62,387 and capital assets by \$40,239.

Gross operating revenues for 2016 were \$3,528,373 and represent an increase of \$393,767 or 13% compared to 2015. Compared to FY2014, total operating revenues was higher by \$535,645 or 18%. The increase in FY2016 operating revenues was the combined effect in the increased revenue performance in the rooms by \$133,502, which can be largely attributed to the increase in average room rate and occupancy; increase in food and beverage revenue by \$201,471; and increase in other revenue of \$63,313.

Total departmental operating profit for the full twelve-month period was \$1,658,144 compared to 2015, which was \$1,572,311 or an increase of \$85,833 or 5%. This also represents an increase over 2014 departmental profit by \$400,493. As a percentage of total revenues, overall departmental operating profit for 2016 was at 47%, which represents 3% lower than 2015 and 5% higher than 2014.

Operating expenses for 2016 amounted to \$1,737,805 compared to 2015, which was \$1,663,473 or an increase of \$74,332 or 4%. As a percentage of total revenues, overall operating expenses for 2016 was at 49%, which represents a decrease of 4% and 6% in 2015 and 2014, respectively. The increase in operating expenses during the year was primarily attributable to the increase in maintenance, sales and marketing, and general and administrative expenses.

Financial Analysis

The Statement of Net Position and the Statement of Revenues, Expenses and Changes in Net Position provide an indication of MRI's financial condition. MRI's net position reflects the difference between assets and liabilities. A summary of MRI's Statement of Net Position is presented below:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Current and other assets	\$ 574,649	\$ 507,615	\$ 474,474
Capital assets	<u>1,315,501</u>	<u>1,355,740</u>	<u>1,576,627</u>
Total assets	\$ <u>1,890,150</u>	\$ <u>1,863,355</u>	\$ <u>2,051,101</u>
Current liabilities	\$ <u>1,430,515</u>	\$ <u>1,310,794</u>	\$ <u>1,403,307</u>
Net position:			
Net investment in capital assets	1,315,501	1,355,740	1,576,627
Unrestricted	<u>(855,866)</u>	<u>(803,179)</u>	<u>(928,833)</u>
Total net position	<u>459,635</u>	<u>552,561</u>	<u>647,794</u>
Total liabilities and net position	\$ <u>1,890,150</u>	\$ <u>1,863,355</u>	\$ <u>2,051,101</u>

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Management's Discussion and Analysis
Years Ended September 30, 2016 and 2015

Total assets increased by \$26,795 or 1% from \$1,863,355 in 2015 to \$1,890,150 in 2016. The increase in total assets was the effect of the increase in cash by \$135,329 offset by decrease in net receivables by \$62,387 at the end of the fiscal year. Receivables mainly comprise government and government-related agencies in which the hotel experienced a slow turnover over the past years. There has been a decrease in net book value of capital assets by \$40,239. Inventories and prepayments decreased by \$4,412 and \$1,496, respectively.

On the other hand, total liabilities increased by \$119,721 or 9% from \$1,310,794 in 2015 to \$1,430,515 in 2016. MRI's liabilities increased due to an increase in accrued expenses and trade payables.

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

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Gross Profit:			
Departmental revenues	\$ 3,455,265	\$ 3,187,005	\$ 2,807,276
Departmental expenses	<u>1,797,121</u>	<u>1,614,694</u>	<u>1,549,625</u>
Total gross profit	1,658,144	1,572,311	1,257,651
Operating expenses	1,737,805	1,663,473	1,656,290
Total operating loss	(79,661)	(91,162)	(398,639)
Non-operating revenues (expenses), net	<u>(13,265)</u>	<u>(4,071)</u>	<u>82,048</u>
Change in net position	\$ <u><u>(92,926)</u></u>	\$ <u><u>(95,233)</u></u>	\$ <u><u>(316,591)</u></u>

A summary of MRI's departmental revenues is presented below:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Departmental revenues:			
Rooms	\$ 1,759,452	\$ 1,625,950	\$ 1,589,032
Food and beverage	1,644,989	1,443,518	1,278,067
Telephone	1,943	6,462	2,473
Others	121,989	58,676	123,156
Less bad debts recovery (expense)	(73,108)	<u>52,399</u>	<u>(185,452)</u>
	\$ <u><u>3,455,265</u></u>	\$ <u><u>3,187,005</u></u>	\$ <u><u>2,807,276</u></u>

A summary of MRI's departmental expenses is presented below:

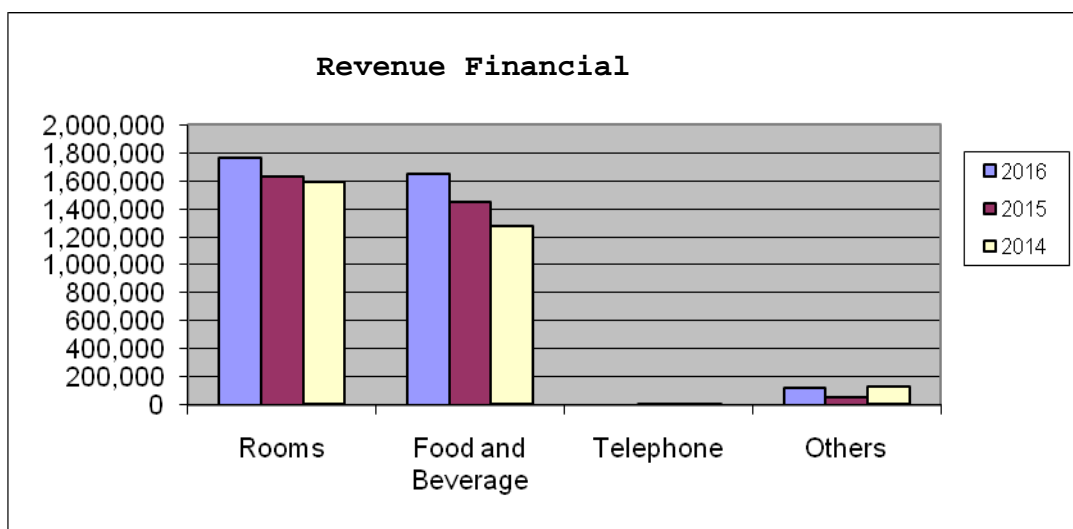
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Departmental expenses:			
Rooms	\$ 418,157	\$ 388,367	\$ 383,411
Food and beverage	1,318,101	1,184,275	1,125,466
Telephone	7,170	9,469	15,800
Others	<u>53,693</u>	<u>32,583</u>	<u>24,948</u>
	\$ <u><u>1,797,121</u></u>	\$ <u><u>1,614,694</u></u>	\$ <u><u>1,549,625</u></u>

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Management's Discussion and Analysis
Years Ended September 30, 2016 and 2015

The Statement of Revenues, Expenses and Changes in Net Position identify various revenue and expense items that impact the change in net position. Gross operating revenues for 2016 increased by \$393,767 from \$3,134,606 in 2015 to \$3,528,373 in 2016. Room revenues for 2016 increased by \$133,502 or 8% from 2015 and increased by \$170,420 or 11% from 2014. The average occupancy ratio increased in 2016 to 53.45% from 50.75% in 2015 and the average room rate increased from \$60.73 in 2015 to \$62.63 in 2016. Food and beverage revenue for 2016 was \$1,644,989, which showed an increase of \$201,471 over 2015 and an increase of \$366,922 over 2014. Meanwhile, telephone revenues and revenues from other operating departments posted a net increase of \$58,794 as compared to last year.

The following graph shows the major components of revenue for financial periods 2016, 2015 and 2014, all of which cover a twelve (12) month period ending September 30.



Statement of Hotel Occupancy Performance

The following table shows a comparison of financial and statistical information affecting room revenue performance for the years 2016, 2015, 2014, 2013 and 2012.

Occupancy Performance	2016	2015	2014	2013	2012
% of total occupancy	53.45%	50.75%	49.41%	45.04%	47.96%
Average rate	\$ 62.63	\$ 60.73	\$ 61.23	\$ 55.50	\$ 45.27
% of paid occupancy	53.33%	50.66%	49.33%	44.97%	47.87%
Average rate	\$ 62.77	\$ 61.06	\$ 61.33	\$ 55.59	\$ 45.35
Group rooms	-	-	-	-	-
% of total occupancy	-	-	-	-	-
Average rate	-	-	-	-	-

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Management's Discussion and Analysis
 Years Ended September 30, 2016 and 2015

Paid occupancy ratio in 2016 was 53% as compared to 51% in 2015 and 49% in 2014.

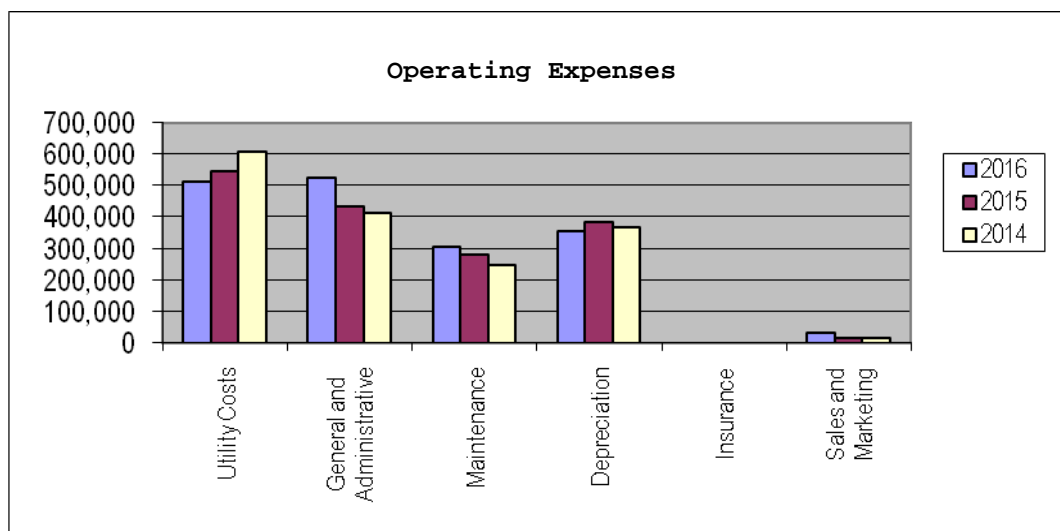
The hotel paid occupancy ratio for the current year has increased over the past two (2) years while the average paid room rate for the current year has slightly increased.

Operating Expenses

Total operating expenses increased by \$74,332 from \$1,663,473 in 2015 to \$1,737,805 in 2016 as a result of the increase in maintenance, sales and marketing, and general and administrative expenses. As a percentage of total revenues, operating expenses for 2016 represents 49% or a decrease of 4% compared to 2015 and 6% decrease over 2014.

Utility costs showed a decrease of \$31,698 from \$545,047 in 2015 to \$513,349 in 2016. The decrease was primarily contributed by the efforts of MIR to change old equipment to energy saver, change of water heater even with the increase in energy rate. General and administrative expenses showed an increase of \$92,677, depreciation posted a decrease of \$28,736 while the maintenance cost increased by of \$24,663.

The following graph shows the major components of operating expenses for financial periods 2016, 2015 and 2014, all of which cover a twelve (12) month period ending September 30.



Capital Assets and Debt

Net capital assets decreased by \$40,239 due to increase in accumulated depreciation of its acquisitions and building improvement. Certain capital equipment was purchased to replace damaged equipment due to wear and tear. MRI had various capital projects such as remodeling of ENRA restaurant, Jakaro Bar extension & roofing project, employee bathroom and locker project, purchase of air conditioning units and other reinforcements. There was also an increase in motor vehicles with the purchase of a brand new shuttle bus to transport hotel guests.

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Management's Discussion and Analysis
Years Ended September 30, 2016 and 2015

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

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Building and structure	\$ 2,714,168	\$ 2,580,460	\$ 2,547,970
Furniture and fixtures	1,547,086	1,438,871	1,342,770
Office equipment	249,296	244,090	241,105
Other equipment	113,638	113,638	109,838
Motor vehicles	<u>299,953</u>	<u>229,916</u>	<u>200,038</u>
At Cost	4,924,141	4,606,975	4,441,721
Accumulated depreciation	<u>(3,608,640)</u>	<u>(3,251,235)</u>	<u>(2,865,094)</u>
Net Book Value	\$ <u><u>1,315,501</u></u>	\$ <u><u>1,355,740</u></u>	\$ <u><u>1,576,627</u></u>

For additional information concerning capital assets, please see note 4 to the financial statements.

MRI did not incur any long-term debt during 2016 nor was any such debt due and outstanding at year end.

Management's Discussion and Analysis for the year ended September 30, 2015 is set forth in the report on the audit of MRI's financial statements dated August 18, 2016. That Discussion and Analysis explains the major factors impacting the 2015 financial statements and may be obtained from the contact information below.

Economic Factors and Next Year's Performance

The following factors may have a great impact on next year's operations:

MRI has been aggressively promoting the destination through outside sales agents such as Booking.com and through social media. It is catering a wide range of tourists within and outside the Pacific. It has also opened its doors to Japanese tourists with the help of Ray Crew Dive Center located within the hotel vicinity. Exposure to travel magazines, travel agents, wholesalers, retailers as well as the general public is being accomplished through a combination of advertising, public relations, direct marketing, trade shows and promotions with the help of its new Marketing Manager.

The RMI Government is now playing an active role in promoting the Marshall Islands to generate sufficient numbers of visitors through conferences, workshops, trainings and seminars that is being sponsored and hosted by the RMI.

There is a continuous growth in guest arrivals brought about by the service provided by Nauru Airlines between Majuro, FSM and Australia. This will have a great impact in the tourism industry and country as a whole. With the current number of visitors to Majuro, MRI management is optimistic about the amount of increase in room revenues for 2017. Upcoming conferences and seminars that will be hosted by RMI for 2017 will also give us an advantage in hotel room occupancy as well as the food and beverage operations.

Combined efforts in searching for ways to increase collections and cut on costs and expenses to improve cash flow and help generate funds in order to meet obligations. MRI new management has established measures to improve its collection campaign in order to recover long-outstanding receivables.

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Management's Discussion and Analysis
Years Ended September 30, 2016 and 2015

Additional Financial Information

The discussion and analysis is designed to provide MRI's customers and other interested parties with an overview of MRI'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 Resort, Inc. General Manager at P.O. Box 3279, Majuro, MH 96960.

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Statements of Net Position
September 30, 2016 and 2015

<u>ASSETS</u>	<u>2016</u>	<u>2015</u>
Current assets:		
Cash	\$ 297,852	\$ 162,523
Receivables:		
Trade	345,846	342,206
Affiliates	351,778	356,245
Other	26,948	15,400
	<u>724,572</u>	<u>713,851</u>
Less allowance for doubtful accounts	(538,923)	(465,815)
Total receivables, net	<u>185,649</u>	<u>248,036</u>
Inventories	<u>53,424</u>	<u>57,836</u>
Prepaid expenses	<u>37,724</u>	<u>39,220</u>
Total current assets	<u>574,649</u>	<u>507,615</u>
Property, plant and equipment, net	<u>1,315,501</u>	<u>1,355,740</u>
	<u>\$ 1,890,150</u>	<u>\$ 1,863,355</u>
 <u>LIABILITIES AND NET POSITION</u> 		
Current liabilities:		
Accounts payable	\$ 167,628	\$ 132,694
Payable to affiliates	702,583	605,963
Accrued expenses	560,304	572,137
Total current liabilities	<u>1,430,515</u>	<u>1,310,794</u>
Commitment and contingencies		
Net position:		
Net investment in capital assets	1,315,501	1,355,740
Unrestricted	(855,866)	(803,179)
Total net position	<u>459,635</u>	<u>552,561</u>
	<u>\$ 1,890,150</u>	<u>\$ 1,863,355</u>

See accompanying notes to financial statements.

MAJURO RESORT, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Statements of Revenues, Expenses and Changes in Net Position
Years Ended September 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Revenues:		
Rooms	\$ 1,759,452	\$ 1,625,950
Food and beverage	1,644,989	1,443,518
Telephone	1,943	6,462
Other	<u>121,989</u>	<u>58,676</u>
Total revenues	3,528,373	3,134,606
Less recovery from (provision for) doubtful accounts	<u>(73,108)</u>	<u>52,399</u>
Net revenues	<u>3,455,265</u>	<u>3,187,005</u>
Cost of sales:		
Rooms	418,157	388,367
Food and beverage	1,318,101	1,184,275
Telephone	7,170	9,469
Other	<u>53,693</u>	<u>32,583</u>
Total cost of sales	<u>1,797,121</u>	<u>1,614,694</u>
Gross profit	<u>1,658,144</u>	<u>1,572,311</u>
Operating expenses:		
General and administrative	527,971	435,294
Utility costs	513,349	545,047
Depreciation	357,405	386,141
Maintenance	306,319	281,656
Sales and marketing	<u>32,761</u>	<u>15,335</u>
Total operating expenses	<u>1,737,805</u>	<u>1,663,473</u>
Operating loss	(79,661)	(91,162)
Nonoperating expenses:		
Interest expense	<u>(13,265)</u>	<u>(4,071)</u>
Change in net position	(92,926)	(95,233)
Net position at beginning of year	<u>552,561</u>	<u>647,794</u>
Net position at end of year	<u>\$ 459,635</u>	<u>\$ 552,561</u>

See accompanying notes to financial statements.

MAJURO RESORT, INC.
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Statements of Cash Flows
Years Ended September 30, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Cash received from customers	\$ 3,517,652	\$ 3,212,991
Cash payments to suppliers for goods and services	(2,071,594)	(2,163,717)
Cash payments to employees for services	(980,298)	(844,254)
Net cash provided by operating activities	465,760	205,020
Cash flows from noncapital financing activities:		
Interest paid	(13,265)	(4,071)
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(317,166)	(165,254)
Net change in cash	135,329	35,695
Cash at beginning of year	162,523	126,828
Cash at end of year	\$ 297,852	\$ 162,523
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (79,661)	\$ (91,162)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	357,405	386,141
Bad debt (recovery) expense	73,108	(52,399)
(Increase) decrease in assets:		
Receivables:		
Trade	(3,640)	33,212
Affiliates	4,467	30,143
Other	(11,548)	15,030
Inventories	4,412	(13,439)
Prepaid expenses	1,496	(9,993)
Increase (decrease) in liabilities:		
Accounts payable	34,934	(15,737)
Payable to affiliates	96,620	(78,983)
Accrued expenses	(11,833)	2,207
Net cash provided by operating activities	\$ 465,760	\$ 205,020

See accompanying notes to financial statements.

MAJURO RESORT, INC.
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Notes to Financial Statements
September 30, 2016 and 2015

(1) Organization

Majuro Resort, Inc. (MRI) dba Marshall Islands Resort, a component unit of the Republic of the Marshall Islands (RepMar), was formed on November 8, 1995, as a corporation. The primary business of MRI is the operation of a 150-room hotel on the atoll of Majuro in the Republic of the Marshall Islands. MRI is governed by a five-member Board of Directors appointed by the Cabinet of RepMar. MRI'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 MRI conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities, specifically proprietary funds.

GASB 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: Omnibus*, and modified by 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 modify certain other financial statement disclosure requirements.

To conform to the requirements of GASB Statement No. 34, equity is presented in the following net position categories:

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

Basis of Accounting

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

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Notes to Financial Statements
September 30, 2016 and 2015

(2) Summary of Significant Accounting Policies, Continued

Cash

Custodial risk is the risk that in the event of a bank failure, MRI'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. MRI does not have a deposit policy for custodial credit risk.

For purpose of the statements of net position and cash flows, cash is defined as cash on hand and cash held in demand accounts. As of September 30, 2016 and 2015, the carrying amount of cash was \$297,852 and \$162,523, respectively, and the corresponding bank balances were \$330,287 and \$239,088 respectively. Of the bank balances, \$263,116 and \$218,872, respectively, were maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance with the remaining amounts of \$67,171 and \$20,216, respectively, being maintained in a financial institution not subject to depository insurance. As of September 30, 2016 and 2015, bank deposits in the amount of \$250,000 and \$218,872, respectively, were FDIC insured. MRI 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 hotel customers and others located within the Republic of the Marshall Islands and the South Pacific region.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is stated at an amount that management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. The allowance is established through a provision for bad debts charged to expense.

Inventories

Inventories are stated at the lower of cost (average costing) or market (net realizable value).

Operating Supplies

China, glass, linen, silverware and uniforms are charged to expense in the year of purchase.

Property, Plant and Equipment

Property, plant and equipment with a cost that equals or exceeds \$100 are capitalized. Such assets are stated at cost. Depreciation is calculated using the straight-line method based on the estimated useful lives of the respective assets.

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Notes to Financial Statements
September 30, 2016 and 2015

(2) Summary of Significant Accounting Policies, Continued

Deferred Outflows of Resources

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

Deferred Inflows of Resources

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

Taxes

Corporate profits are not subject to income tax in the Republic of the Marshall Islands. The Government of the Republic of the Marshall Islands imposes a gross receipts tax (GRT) of 3% on revenues. MRI, being a component unit of the Republic of the Marshall Islands as defined in the State-Owned Enterprises Act, 2015, is exempt from payment of GRT.

Advertising Costs

MRI expenses advertising costs as incurred. During the years ended September 30, 2016 and 2015, MRI incurred advertising costs of \$10,702 and \$9,422, respectively.

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 nonvesting accumulating rights to receive sick benefits. As of September 30, 2016 and 2015, the accumulated vacation leave liability amounted to \$46,632 and \$54,100, respectively, and is included within the statements of net position as accrued expenses.

New Accounting Standards

During the year ended September 30, 2016, MRI implemented the following pronouncements:

- GASB Statement No. 72, *Fair Value Measurement and Application*, which addresses accounting and financial reporting issues related to fair value measurements and requires entities to expand their fair value disclosures by determining major categories of debt and equity securities within the fair value hierarchy on the basis of the nature and risk of the investment.
- GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which eliminates two of the four categories of authoritative GAAP that exist under the existing hierarchy prescribed by Statement No. 55. The two categories that will remain under the new standard are (1) GASB Statements and (2) GASB technical bulletins and implementation guides in addition to AICPA guidance that the GASB clears.

MAJURO RESORT, INC.
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Notes to Financial Statements
September 30, 2016 and 2015

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

- GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*, addresses for certain external investment pools and their participants the accounting and financial reporting implications that result from changes in the regulatory provisions referenced by previous accounting and financial reporting standards. Those provisions were based on the Investment Company Act of 1940, Rule 2a7. Rule 2a7 contains the Securities and Exchange Commission's regulations that apply to money market funds and were significantly amended in 2014.

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

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

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

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. The provisions in Statement No. 75 are effective for fiscal years beginning after June 15, 2017. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In August 2015, GASB issued Statement No. 77, *Tax Abatement Disclosures*, which requires governments that enter into tax abatement agreements to disclose certain information about the agreements. The provisions in Statement No. 77 are effective for fiscal years beginning after December 15, 2015. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In December 2015, GASB issued Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*, which addresses a practice issue regarding the scope and applicability of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The provisions in Statement No. 78 are effective for fiscal years beginning after December 15, 2015. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

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Notes to Financial Statements
September 30, 2016 and 2015

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In January 2016, GASB issued Statement No. 80, *Blending Requirements for Certain Component Units - an amendment of GASB Statement No. 14*, which improves financial reporting by clarifying the financial statement presentation requirements for certain component units. The provisions in Statement No. 80 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In March 2016, GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements*, which improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. The provisions in Statement No. 81 are effective for fiscal years beginning after December 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In March 2016, GASB issued Statement No. 82, *Pension Issues - an amendment of GASB Statements No. 67, No. 68, and No. 73*, which addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The provisions in Statement No. 82 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

Estimates

The preparation of financial statements in accordance 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 deferred outflows of resources, liabilities and deferred inflows of resources, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(3) Risk Management

MRI 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. MRI 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. MRI does not maintain general liability insurance; property insurance; and fire, lightning and typhoon insurance for its hotel building and contents. In the event of an insurable loss, MRI may be self-insured to a material extent.

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Notes to Financial Statements
September 30, 2016 and 2015

(4) Property, Plant and Equipment

Capital asset activity for the years ended September 30, 2016 and 2015 was as follows:

	<u>Estimated Useful Lives</u>	Balance at October 1, <u>2015</u>	<u>Additions</u>	Balance at September 30, <u>2016</u>
Building and structure	17 years	\$ 2,580,460	\$ 133,708	\$ 2,714,168
Furniture and fixtures	3 years	1,438,871	108,215	1,547,086
Office equipment	3 years	244,090	5,206	249,296
Other equipment	3 years	113,638	-	113,638
Motor vehicles	3 years	<u>229,916</u>	<u>70,037</u>	<u>299,953</u>
		4,606,975	317,166	4,924,141
Less accumulated depreciation		<u>(3,251,235)</u>	<u>(357,405)</u>	<u>(3,608,640)</u>
		\$ <u>1,355,740</u>	\$ <u>(40,239)</u>	\$ <u>1,315,501</u>

	<u>Estimated Useful Lives</u>	Balance at October 1, <u>2014</u>	<u>Additions</u>	Balance at September 30, <u>2015</u>
Building and structure	17 years	\$ 2,547,970	\$ 32,490	\$ 2,580,460
Furniture and fixtures	3 years	1,342,770	96,101	1,438,871
Office equipment	3 years	241,105	2,985	244,090
Other equipment	3 years	109,838	3,800	113,638
Motor vehicles	3 years	<u>200,038</u>	<u>29,878</u>	<u>229,916</u>
		4,441,721	165,254	4,606,975
Less accumulated depreciation		<u>(2,865,094)</u>	<u>(386,141)</u>	<u>(3,251,235)</u>
		\$ <u>1,576,627</u>	\$ <u>(220,887)</u>	\$ <u>1,355,740</u>

(5) Related Party Transactions

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

MRI's hotel service is provided to RepMar and all RepMar-owned and affiliated entities. Services are provided to these entities at the same rates charged to third parties; however, MRI provides more favorable payment terms to its affiliates than those afforded to third parties.

MRI utilizes services from certain affiliated entities at substantially more favorable terms than those incurred from third parties.

MAJURO RESORT, INC.
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Notes to Financial Statements
September 30, 2016 and 2015

(5) Related Party Transactions, Continued

A summary of related party balances and transactions as of September 30, 2016 and 2015 and for the years then ended are as follows:

	2016			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 366,828	\$ 89,913	\$ 269,756	\$ 134,540
Marshall's Energy Company, Inc.	15,698	453,333	8,529	492,126
Marshall Islands National Telecommunications Authority	16,644	102,306	7,418	8,736
Marshall Islands Social Security Administration	867	195,714	10	53,820
Majuro Water and Sewer Company, Inc.	1,546	59,592	795	5,746
Other	<u>131,191</u>	<u>90,053</u>	<u>65,270</u>	<u>7,615</u>
	<u>\$ 532,774</u>	<u>\$ 990,911</u>	<u>\$ 351,778</u>	<u>\$ 702,583</u>
	2015			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 345,029	\$ 76,944	\$ 297,330	\$ 184,305
Marshall's Energy Company, Inc.	68,800	485,974	5,362	340,623
Marshall Islands National Telecommunications Authority	21,121	86,721	9,843	9,621
Marshall Islands Social Security Administration	409	170,315	-	60,336
Majuro Water and Sewer Company, Inc.	1,617	62,583	576	5,690
Other	<u>229,974</u>	<u>79,637</u>	<u>43,134</u>	<u>5,388</u>
	<u>\$ 666,950</u>	<u>\$ 962,174</u>	<u>\$ 356,245</u>	<u>\$ 605,963</u>

In 2015, MRI purchased a used Toyota van from the General Manager in the amount of \$8,000.

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

(6) Commitment and Contingencies

Commitment

MRI leases the land on which the hotel is situated at \$10,212 per year plus 2.5% of gross revenue earned. These payments are suspended until such time as any person or entity other than RepMar or any agency thereof holds 75% of the ownership of the lessee, or its successor in the interest in the hotel. The lease also requires that 5% of the initial outstanding shares of the lessee or its successor be issued to the lessor. Neither MRI nor RepMar have issued shares to the lessor at September 30, 2016 and 2015.

MRI leases business space to a commercial entity at \$1,850/month expiring on November 30, 2017, subject to an annual renewal.

MAJURO RESORT, INC.
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Notes to Financial Statements
September 30, 2016 and 2015

(6) Commitment and Contingencies, Continued

Contingencies

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, which contemplates the continuation of MRI as a going concern. MRI sustained substantial operating losses during the years ended September 30, 2016 and 2015 of \$79,661 and \$91,162, respectively, and used a substantial amount of working capital in its operations resulting in a working capital deficiency of \$855,866 and \$803,179 during the years ended September 30, 2016 and 2015, respectively. Management acknowledges that it is currently dependent on RepMar for cash funding in order to maintain MRI as a going concern. Although RepMar has provided funding in the past, MRI does not have a formal agreement with RepMar to provide funds in the future. Management believes that the continuation of MRI's operations is dependent upon the future financial support of RepMar, deferment in payment of certain liabilities, and/or significant improvements in operations.

In view of these matters, realization of a major portion of the assets in the accompanying statement of net position at September 30, 2016, is dependent upon continued operations of MRI, which, in turn, is dependent upon MRI's ability to provide service to its customers and the success of future operations. Management believes that actions presently being undertaken to revise MRI's operating requirements, including the generation of positive cash flows from operations, and increasing occupancy rates and average room rates, provide the opportunity for MRI to continue as a going concern.

At September 30, 2016 and 2015, MRI did not file sales and local government taxes until August 2014, which may not be in compliance with Majuro Atoll Local Government (Malgov) local ordinances. As a result, sales taxes of \$334,415 and \$334,382 and local government taxes of \$345,580 and \$345,055 as of September 30, 2016 and 2015, respectively, remain outstanding and of which \$493,414 and \$492,857, are included as accrued expenses in the accompanying statements of net position. Unfavorable resolution of this matter could expose MRI to additional penalties and interest. Penalties and interest are estimated to be \$163,199 and \$163,065 as of September 30, 2016 and 2015, respectively. No such action has yet been filed. At September 30, 2016 and 2015, the financial statements do not include any adjustments that might result from the outcome of this uncertainty. Management is currently negotiating the settlement of sales and local government taxes with Malgov.

At September 30, 2016 and 2015, MRI is liable for delinquent withholding taxes, totaling \$126,883 and \$184,305, respectively. On November 12, 2013, MRI entered into an agreement with RepMar to resolve the settlement of certain delinquent withholding taxes whereby RepMar will deduct 20% from all payments due to MRI until such time that the delinquent withholding taxes liability has been fully satisfied. In addition, RepMar agreed to waive the payment of penalties and interest as long as MRI remains current on withholding taxes payable commencing October 2013. As of September 30, 2016, MRI has remitted current withholding taxes.

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

Board of Directors
Majuro Resort, Inc.:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Majuro Resort, Inc. (MRI), which comprise the statement of net position as of September 30, 2016, and the statements of revenues, expenses and changes in net position and of cash flows for the year then ended and the related notes to the financial statements, and have issued our report thereon dated June 9, 2017. Our report included an emphasis-of-matter paragraph regarding a going concern uncertainty.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

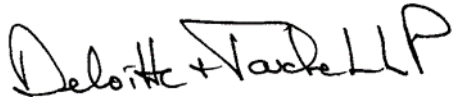
As part of obtaining reasonable assurance about whether MRI's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as items 2016-001 and 2016-002.

MRI's Response to Findings

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

Purpose of this Report

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



June 9, 2017

MAJURO RESORT, INC.
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Schedule of Findings and Responses
Year Ended September 30, 2016

Finding No.: 2016-001
Area: Prior Year Sales and Local Government Tax

Criteria: Majuro Atoll Local Government (Malgov) local ordinances require payment of 4% sales tax and three dollar per night room tax by consumers and these taxes are to be remitted to Malgov on a monthly basis.

Condition: Management accrued and filed sales and local taxes during FY16. However, potential interest and penalties for prior year unrecorded sales taxes and unfiled sales and local taxes have not been recorded as management believes that the amount can be negotiated with Malgov.

Cause: MRI did not pay these taxes as management believes that they paid for the sales tax when MRI purchased items. Management believes paying the sales tax would result in double taxation. Local government hotel room taxes were not paid since management believes that MRI is owned by RepMar.

Effect: Noncompliance with local laws and regulations could result from this condition which may result in penalties and interest.

Prior Year Status: Non-filing of sales and local government taxes was reported as a finding in the audits of MRI for fiscal years 2006 through 2015.

Recommendation: We recommend that MRI initiate discussions with Malgov regarding interest and penalties on prior year unrecorded sales taxes and unfiled sales and local taxes.

Auditee Response and Corrective Action Plan: MRI provided information to the Ministry of Finance with regards to the government taxes from 2006 through 2015. We are still waiting for updates based on the discussion between the Ministry of Finance and Majuro Atoll Local Government.

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Schedule of Findings and Responses, Continued
Year Ended September 30, 2016

Finding No.: 2016-002
Area: Procurement

Criteria: RepMar's Procurement Code states the following:

- (a) Section 124 - unless otherwise authorized by law, all Government contracts shall be awarded by competitive sealed bidding.
- (b) Section 127 - procurement of goods and services not exceeding \$25,000 may be made in accordance with small purchase procedures promulgated by Repmar's Policy Office; provided, however, that procurement requirements shall not be artificially divided so as to constitute a small purchase under this Section. Small purchase procedures are those relatively simple and informal methods for securing services, supplies, or other property that do not cost more than \$25,000. RepMar's Ministry of Finance has previously declared that if small purchase procedures are used, price or rate quotations shall be obtained from an adequate number of qualified sources.
- (c) Section 128 - a contract may be awarded for a supply, service, or construction item without competition when it is determined in writing that there is only one source for the required supply, service, or construction item.
- (d) Section 129 - notwithstanding any other provision of this Act, emergency procurement may be made when there exists a threat to public health, welfare, or safety under emergency conditions as defined in regulations promulgated by the Policy Office; provided, that such emergency procurement shall be made with such competition as is practicable under the circumstances. A written determination of the basis for the emergence and for the selection of the particular contractor shall be included in the contract file.

Condition: The following payments were not adequately documented to evidence compliance with the procurement process set forth in the criteria:

- 1) Construction materials for pool stage roofing (\$15,047)
- 2) Construction materials for the employee bathroom and locker (\$60,587)
- 3) No competitive bidding for one 30-seater shuttle bus (\$51,550)
- 4) Airfare for an employee's 14-day business trip to Manila (\$2,820)
- 5) Various purchases of room supplies, kitchen and restaurant needs (\$44,099)

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

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

Prior Year Status: The lack of compliance with RepMar's Procurement Code was reported as a finding in the audits of MRI for fiscal years 2013 through 2015.

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

MAJURO RESORT, INC.
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Schedule of Findings and Responses, Continued
Year Ended September 30, 2016

Finding No.: 2016-002, Continued
Area: Procurement

Auditee Response and Corrective Action Plan: MRI's lack of compliance with the procurement procedure were caused by various factors such as:

- (1) Limited product availability on island - not all vendors on island provide the products/services that the establishment needs;
- (2) Time Constraint – there are purchases that are needed urgently from various repairs due to wear and tear especially when it comes to hotel maintenance;
- (3) Payment Plan – purchase of vehicle was based on the most affordable payment plan provided by the vendors; and
- (4) Limited airlines – since we have only have one airline carrier on island that will be able to provide the service on the specific dates of travel.

MRI management designated a Property Service Manager who will oversee these purchases to make sure that documentation of procurement procedures is in compliance with RepMar's procurement code.

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Unresolved Prior Year Findings
Year Ended September 30, 2016

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