

**MARSHALLS ENERGY COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC
OF THE MARSHALL ISLANDS)**

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

YEARS ENDED SEPTEMBER 30, 2020 AND 2019

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Years Ended September 30, 2020 and 2019
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INDEPENDENT AUDITORS' REPORT

Board of Directors
Marshalls Energy Company, Inc.:

Report on the Financial Statements

We have audited the accompanying financial statements of Marshalls Energy Company, Inc. (MEC), a component unit of the Republic of the Marshall Islands, which comprise the statements of net position as of September 30, 2020 and 2019, 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 Marshalls Energy Company, Inc. as of September 30, 2020 and 2019, 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**COVID-19**

As discussed in Note 12 to the financial statements, MEC has determined that the COVID-19 pandemic may negatively impact its business, results of operations and net position. MEC is unable to reasonably estimate its ultimate financial impact. Our opinion is not modified with respect to this matter.

Other Matters***Required Supplementary Information***

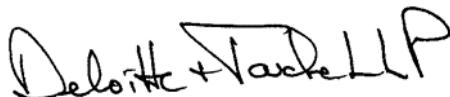
Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 to 7 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting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

Other Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Other Supplementary Information listed in the accompanying table of contents is presented for purposes of additional analysis and is not a required part of the financial statements. The Other Supplementary Information is the responsibility of MEC's management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Other Supplementary Information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 2, 2021, on our consideration of MEC'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 solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of MEC's 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 MEC's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Deloitte & Touche LLP". The signature is fluid and cursive, with "Deloitte" on the top line and "& Touche LLP" on the bottom line.

November 2, 2021

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

**Management's Discussion and Analysis
Years Ended September 30, 2020 and 2019**

Marshalls Energy Company, Inc. (MEC) herewith presents a discussion and analysis of the company's financial performance for the fiscal year ended 30th September, 2020. It is to be read in conjunction with the financial statements following this section.

FINANCIAL HIGHLIGHTS

MEC's net position increased by \$11.5 million in fiscal year 2020 compared to an increase of \$0.5 million in fiscal year 2019. In 2020, total net utility operating revenues were \$19.1 million, a slight increase of \$0.7 million from \$18.4 million net utility operating revenues in fiscal year 2019. Total utility operating expenses were \$17 million and \$19.3 million in fiscal years 2020 and 2019, respectively. The decrease of \$2.3 million or 12% is mainly due to the net impact of a decrease in cost of fuel, cost of power and depreciation expense of \$1.8 million (or 18%), \$1 million (or 23%) and \$0.5 million (or 35%), respectively, offset by an increase in administrative and general expense and distribution operation expense of \$0.7 million (or 31%) and \$0.3 million (or 21%), respectively. The decrease in cost of fuel relates to a decrease in global fuel prices experienced during fiscal year 2020 compared to fiscal year 2019. Average fuel price for fiscal year 2020 decreased by 18% compared to fiscal year 2019. Cost of fuel continues to be a significant component of generation operating costs and represents 49% and 53% of total operating costs in fiscal years 2020 and 2019, respectively.

Total operating revenues from nonutility operations, fuel sales being the major component, were \$12.6 million and \$16.3 million in fiscal years 2020 and 2019, respectively. This is a decrease of \$3.7 million (or 23%), which relates mostly to a decrease in global fuel prices and a decrease in gallons sold. Provision for doubtful accounts expense were for fuel sales and were charged against operating revenues in the amounts of \$1.7 million and \$2.5 million for fiscal years 2020 and 2019, respectively. The provision for doubtful accounts expense relates to one customer. Total nonutility operating expense decreased by \$4.3 million (or 25%), from \$16.9 million in fiscal year 2019 to \$12.6 million in fiscal year 2020 and is in line with the decrease in global fuel prices in fiscal year 2020 compared to fiscal year 2019.

MEC received operational subsidies from RepMar in the amount of \$1.9 million in fiscal year 2020 compared to \$2 million in fiscal year 2019. The bulk of the operational subsidies pertains to grant funding in the amount of \$1.5 million (for each fiscal year) from the 11th European Development Fund (EDF11) under the ACP-EU Partnership Agreement. This grant was received as budget support to MEC and was used to support reform initiatives set out in the report published under the ADB Technical Assistance (TA) for Capacity Building and Sector Reform for Renewable Investments in the Pacific. The remaining operational subsidies received of \$0.4 million and \$0.5 million in fiscal years 2020 and 2019, respectively, represented cost recovery support for the operations of the Wotje and Jaluit power plants. No subsidies were received to support fund the gap in solar tariff for maintenance services towards solar unit in the outer islands.

MEC also received \$2.1 million in fiscal year 2020 from the Government of Japan under a Non-Project Grant Aid for fuel support.

FINANCIAL ANALYSIS OF MEC

The Statement of Net Position and the Statement of Revenues, Expenses and Changes in Net Position provide an indication of MEC's financial condition. MEC's net position reflects the difference between total assets and total liabilities. An increase in net position over time normally indicates an improvement in financial condition. As illustrated in the figures below, MEC's net position increased by \$11.5 million in fiscal year 2020 compared to an increase of \$0.5 million in fiscal year 2019.

MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)

Management's Discussion and Analysis
Years Ended September 30, 2020 and 2019

FINANCIAL ANALYSIS OF MEC, CONTINUED

Statements of Net Position

A summary of MEC's Statements of Net Position is presented below:

Summary Statements of Net Position
As of September 30

	2020	2019	\$ Change 2020-2019	% Change 2020-2019	2018
Assets:					
Current and other assets	\$ 23,531,792	\$ 19,449,883	\$ 4,081,909	21.0%	\$ 21,532,051
Capital assets	<u>11,300,905</u>	<u>6,338,653</u>	<u>4,962,252</u>	78.3%	<u>7,199,765</u>
Total assets	<u>34,832,697</u>	<u>25,788,536</u>	<u>9,044,161</u>	35.1%	<u>28,731,816</u>
Liabilities:					
Current and other liabilities	9,863,089	11,738,213	(1,875,124)	(16.0)%	13,583,990
Long-term debt	<u>5,850,336</u>	<u>6,428,742</u>	<u>(578,406)</u>	(9.0)%	<u>8,006,332</u>
Total liabilities	<u>15,713,425</u>	<u>18,166,955</u>	<u>(2,453,530)</u>	(13.5)%	<u>21,590,322</u>
Net position:					
Net investment in capital assets	11,300,905	6,125,040	5,175,865	84.5%	5,843,850
Restricted	358,453	-	358,453		-
Unrestricted	<u>7,459,914</u>	<u>1,496,541</u>	<u>5,963,373</u>	398.5%	<u>1,297,644</u>
Total net position	<u>\$ 19,119,272</u>	<u>\$ 7,621,581</u>	<u>\$ 11,497,691</u>	150.9%	<u>\$ 7,141,494</u>

Total assets increased by \$9 million (or 35%) from \$25.8 million in fiscal year 2019 to \$34.8 million in fiscal year 2020 and decreased by \$2.9 million (or 10%) from \$28.7 million in fiscal year 2018 to \$25.8 million in fiscal year 2019. Current and other assets increased in fiscal year 2020 by \$4.1 million (or 21%) while capital assets increased in fiscal year 2020 by \$5 million (or 78%). The increase in current and other assets mainly relates to an increase in cash holdings of \$5.2 million (or 182%) and prepayments and deposits of \$1 million (or 199%) offset by a decrease in net accounts receivable of \$1.2 million (or 22%) and fuel and supplies of \$1 million (or 13%). The increase in capital assets mainly relates to an increase in electric plant in service as a result of a Memorandum of Understanding signed by RepMar for the transfer of ownership of RepMar assets maintained and operated by MEC to MEC. Total capital contributions amounted \$5.5 million, which represented capital assets of \$37.9 million net of accumulated depreciation of \$32.4 million.

Total liabilities decreased by \$2.5 million (or 14%) from \$18.2 million in fiscal year 2019 to \$15.7 million in fiscal year 2020 and decreased by \$3.4 million (or 16%) from \$21.6 million in fiscal year 2018 to \$18.2 million in fiscal year 2019. Current and other liabilities decreased in fiscal year 2020 by \$1.9 million (or 16%) while long-term debt decreased in fiscal year 2020 by \$0.6 million (or 9%). The decrease in current and other liabilities mainly relates to a decrease in accounts payable of \$2.8 million (or 62%) offset by an increase in counterpart funding of \$1 million relative to a Government of Japan Grant in Aid for fuel purchases. The decrease in long-term debt of \$0.6 million (or 9%) relates to fiscal year 2020 annual debt service payments on RUS and ADB debt.

MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)

Management's Discussion and Analysis
Years Ended September 30, 2020 and 2019

FINANCIAL ANALYSIS OF MEC, CONTINUED

Statements of Revenues, Expenses and Changes in Net Position

The net position increased by \$11.5 million from a net position of \$7.6 million in fiscal year 2019 to \$19.1 million in fiscal year 2020. A summary of MEC's Statements of Revenues, Expenses, and Changes in Net Position is presented below:

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

	2020	2019	\$ Change 2020-2019	% Change 2020-2019	2018
Operating revenues:					
Utility revenues	\$ 19,119,166	\$ 18,454,203	\$ 664,963	3.6%	\$ 18,317,571
Nonutility revenues	12,640,353	16,313,432	(3,673,079)	(22.5)%	16,023,676
Total operating revenues	<u>31,759,519</u>	<u>34,767,635</u>	<u>(3,008,116)</u>	<u>(8.7)%</u>	<u>34,341,247</u>
Operating expenses:					
Utility expenses	17,058,578	19,324,068	(2,265,490)	(11.7)%	18,440,541
Nonutility expenses	12,645,273	16,915,826	(4,270,553)	(25.2)%	16,076,545
Total operating expenses	<u>29,703,851</u>	<u>36,239,894</u>	<u>(6,536,043)</u>	<u>(18.0)%</u>	<u>34,517,086</u>
Operating profit (loss)	<u>2,055,668</u>	<u>(1,472,259)</u>	<u>3,527,927</u>	<u>(239.6)%</u>	<u>(175,839)</u>
Nonoperating revenues:					
RMI subsidies	1,932,372	2,016,514	(84,142)	(4.2)%	1,169,925
Japan Grant Aid	2,100,611	-	2,100,611	-	-
Other grants	-	90,435	(90,435)	(100.0)%	-
	<u>4,032,983</u>	<u>2,106,949</u>	<u>1,926,034</u>	<u>91.4%</u>	<u>1,169,925</u>
Nonoperating expenses:					
Interest expense	103,685	154,603	(50,918)	(32.9)%	224,810
	<u>5,984,966</u>	<u>480,087</u>	<u>5,504,879</u>	<u>-</u>	<u>769,276</u>
Capital contributions	<u>5,512,725</u>	<u>-</u>	<u>5,512,725</u>	<u>100.0%</u>	<u>-</u>
Change in net position	<u>\$ 11,497,691</u>	<u>\$ 480,087</u>	<u>\$ 11,017,604</u>	<u>2294.9%</u>	<u>\$ 769,276</u>

The Statements of Revenue, Expenses and Changes in Net Position identify the various revenue and expense items that contributed to the change in net position. Total operating earnings for fiscal year 2020 were \$2 million, and which were primarily attributable to utility operations. Total operating earnings for fiscal year 2020 increased by \$3.5 million (or 240%) compared to an operating loss of \$1.5 million for fiscal year 2019.

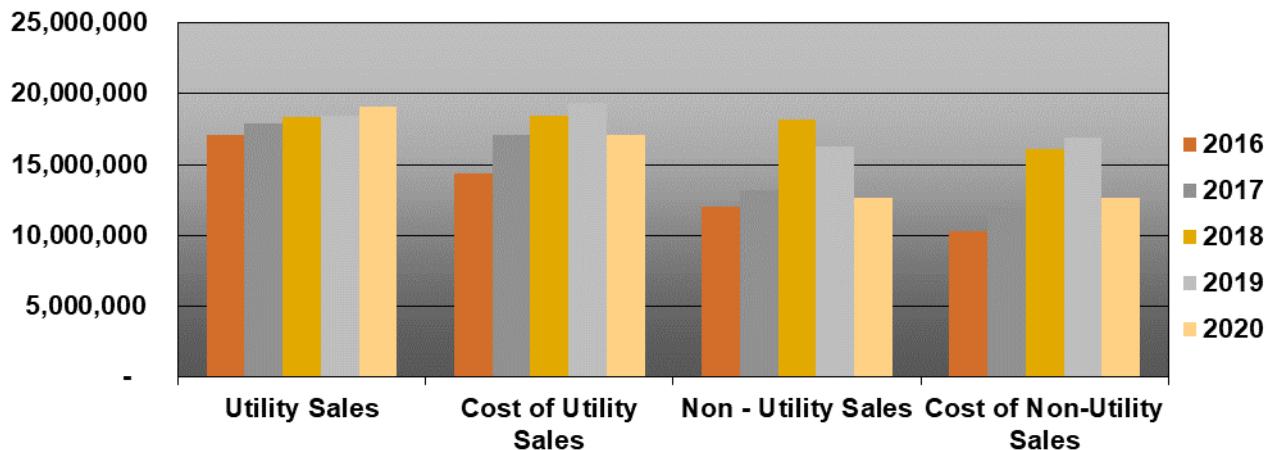
Total operating revenues decreased in fiscal year 2020 by \$3 million (or 9%) to a total of \$31.8 million compared to \$34.8 million in fiscal year 2019. Utility revenues increased by \$0.7 million (or 4%) from \$18.4 million in fiscal year 2019 to \$19.1 million in fiscal year 2020. The slight increase relates to an increase in cash power sales compared to 2019. Nonutility revenues primarily relate to diesel fuel sales. Nonutility revenues decreased by \$3.7 million (or 23%) from \$16.3 million in fiscal year 2019 to \$12.6 million in fiscal year 2020. The decrease mainly relates to a decrease in the selling price as a result of a reduction in global fuel prices in 2020. Total operating expenses decreased in fiscal year 2020 by \$6.5 million (or 18%) to a total of \$29.7 million compared to \$36.2 million in fiscal year 2019. Utility expenses decreased by \$2.3 million (or 12%) from \$19.3 million in fiscal year 2019 to \$17.1 million in fiscal year 2020 while nonutility expenses decreased by \$4.3 million (or 25%) from \$16.9 million in fiscal year 2019 to \$12.6 million in fiscal year 2020. The decrease in both categories relates to a decrease in global fuel prices in fiscal year 2020.

MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)

Management's Discussion and Analysis
Years Ended September 30, 2020 and 2019

FINANCIAL ANALYSIS OF MEC, CONTINUED

The graphic below shows the major components of the Statement of Revenue and Expenses trend for the past five years:



CAPITAL ASSETS AND DEBT

Net capital assets increased by \$5 million or 78% from \$6.3 million in fiscal year 2019 to \$11.3 million in fiscal year 2020. The increase is due primarily to the transfer of Majuro public power distribution service assets from RepMar to MEC in January 2020. A summary of MEC's capital assets at September 30, 2020 compared with 2019 and 2018 is presented below:

Summary Schedule of Capital Assets
As of September 30

	2020	2019	\$ Change 2020-2019	% Change 2020-2019	2018
Utility plant:					
Power plant engines	\$ 23,314,238	\$ 20,090,438	\$ 3,223,800	16.0%	\$ 20,090,438
Tank farm	23,900,000	-	23,900,000	-	-
Distribution	3,316,665	-	3,316,665	-	-
Solar power systems	8,564,830	1,110,417	7,454,413	671.3%	1,110,417
Other	8,606,505	8,313,478	293,027	3.5%	8,378,257
Nonutility plant:					
LPG terminal	209,994	181,862	28,132	15.5%	181,862
	67,912,232	29,696,195	38,216,037	128.7%	29,760,974
Accumulated depreciation	(57,198,279)	(24,223,392)	(32,974,887)	136.1%	(23,217,090)
	10,713,953	5,472,803	5,241,150	95.8%	6,543,884
CWIP	586,952	865,850	(278,898)	(32.2)%	655,881
	<u>\$ 11,300,905</u>	<u>\$ 6,338,653</u>	<u>\$ 4,962,252</u>	<u>78.3%</u>	<u>\$ 7,199,765</u>

Please refer to note 5 of the accompanying financial statements for additional information regarding MEC's capital assets.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Management's Discussion and Analysis
Years Ended September 30, 2020 and 2019

CAPITAL ASSETS AND DEBT, CONTINUED

A summary of MEC's long-term debt at September 30, 2020 compared with 2019 and 2018 is presented below:

Summary Schedule of Long-term Debt
As of September 30

	2020	2019	\$ Change 2020-2019	% Change 2020-2019	2018
Rural Utilities Service	\$ -	\$ 213,612	\$ (213,612)	(100.0)%	\$ 1,355,915
Asian Development Bank	<u>\$ 5,850,336</u>	<u>\$ 6,215,130</u>	<u>\$ (364,794)</u>	<u>(5.9)%</u>	<u>\$ 6,650,417</u>
	<u>\$ 5,850,336</u>	<u>\$ 6,428,742</u>	<u>\$ (578,406)</u>	<u>(9.0)%</u>	<u>\$ 8,006,332</u>

In 1997, MEC obtained a \$12.5 million loan from the Rural Utilities Service for the purpose of financing the construction of a new power plant. This loan was paid in full in fiscal year 2020. In 2010, MEC obtained a \$10 million loan from the Asian Development Bank (ADB) through RepMar for the purpose of paying off a bank loan. This loan matures in 2034. Please refer to note 6 of the accompanying financial statements for additional information regarding MEC's long-term debt.

MEC FOCUS IN THE COMING FISCAL YEAR

MEC finalized its 3-year Business Plan (BP) in September 2020. The BP is a legal requirement under the State-Owned Enterprises Act, 2015. The BP outlines the key objectives and strategic actions for fiscal years 2021 to 2024. An important component of the key objectives is the implementation of recommendations set out in the ADB Technical Assistance Report for Capacity Building and Sector Reform for Renewable Energy Investments in the Pacific, dated November 2017. The BP will drive the operational and management strategies and is MEC's key focus over the next 3 years to achieving MEC's vision and enhancing the quality of life for the people of the RMI. The BP contains a total of 46 strategic actions, spread over 17 key objectives and covers 7 key areas.

The global emergence of the coronavirus disease 2019 (COVID-19) in FY2020 is having an extraordinary impact on Pacific Island economies, including the RMI, and across the globe. The RMI has been spared any confirmed cases of COVID-19 through community transmission and has taken strong proactive measures to protect the health of the nation. The structure of the RMI economy is heavily dependent upon the public sector as well as fisheries activities. With the advent of COVID-19, global oil prices have substantially dropped due to exceeding supply over demand. While the drop in global oil prices is considered to be temporary, MEC is expected to benefit from this through lower operating costs. MEC's fuel sales related to fisheries activities may see a decline; however, with the drop in global oil prices, we believe that MEC will be able to weather the current situation. MEC operations have been slightly impacted by COVID-19. The impact has been mostly in the area of delayed shipments or receipt of orders and the area of fuel sales where MEC has experienced both a decrease in fuel price and fuel sales demand. The drop in fuel demand in February 2020 was the result of zero incoming foreign vessels. We can all agree that COVID-19 and the RMI National Disaster Committee (NDC) 30-day quarantine versus 14 days has to do with the low demand (averaging 15K gallons per month) due to a reduction of incoming foreign vessels in FY2020. MEC had a 75K-100K gallon fuel demand from foreign vessels before the month of February. Hopefully, with the discontinuance of the RMI Health Travel Advisory and restrictions by the NDC and the opening of the RMI borders, we will see our business gain traction to normalcy.

ADDITIONAL INFORMATION

This discussion and analysis is designed to provide MEC's customers and other stakeholders with an overview of the company's operations and financial condition as at 30th September, 2020. Should the reader have questions regarding the information included in this report, or wish to request additional financial information, please contact the Marshalls Energy Company, Inc. Chief Executive Officer at P.O. Box 1439, Majuro, Marshall Islands, MH 96960.

**MARSHALLS ENERGY COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)**

Statements of Net Position
September 30, 2020 and 2019

	2020	2019
ASSETS		
Utility plant:		
Electric plant in service	\$ 67,702,238	\$ 29,514,333
Less accumulated depreciation and amortization	<u>(57,188,630)</u>	<u>(24,041,530)</u>
	10,513,608	5,472,803
Construction work in progress	586,952	865,850
Net utility plant	<u>11,100,560</u>	<u>6,338,653</u>
Nonutility property	209,969	181,862
Less accumulated depreciation	<u>(9,624)</u>	<u>(181,862)</u>
Nonutility property, net	200,345	-
Total capital assets	<u>11,300,905</u>	<u>6,338,653</u>
Long-term replacement parts	1,058,941	967,885
Deposit on acquisition of capital assets	-	300,187
Total non-current assets	<u>12,359,846</u>	<u>7,606,725</u>
Current assets:		
Cash	7,697,189	2,852,351
Restricted cash	358,453	-
Time certificates of deposit	2,998,764	2,944,977
Accounts receivables, net	4,142,757	5,329,696
Due from employees	-	15,823
Fuel and supplies	5,744,019	6,826,160
Deposit on acquisition of supplies	795,063	-
Prepayments	626,606	112,804
Security deposit	110,000	100,000
Total current assets	<u>22,472,851</u>	<u>18,181,811</u>
Total assets	<u>\$ 34,832,697</u>	<u>\$ 25,788,536</u>
NET POSITION AND LIABILITIES		
Net position:		
Net investment in capital assets	\$ 11,300,905	\$ 6,125,040
Restricted	358,453	-
Unrestricted	7,459,914	1,496,541
Total net position	<u>19,119,272</u>	<u>7,621,581</u>
Commitments and contingencies		
Noncurrent liabilities:		
Long-term debt	5,508,272	5,878,156
Counterpart fund payable	999,389	-
Unearned fuel purchase incentive, net of current portion	-	1,470,497
Accrued leave, net of current portion	300,262	173,424
Total noncurrent liabilities	<u>6,807,923</u>	<u>7,522,077</u>
Current liabilities:		
Current portion of long-term debt	342,064	550,586
Accounts payable - fuel	496,346	3,580,240
Accounts payable - other	727,264	467,038
Payable to affiliates	503,295	493,885
Accrued leave	269,553	202,720
Accrued taxes	1,955,570	1,976,190
Other accrued liabilities	96,521	236,090
Unearned fuel purchase incentive, current portion	-	183,812
Unearned revenue - power	3,033,593	2,369,708
Unearned revenue - fuel	1,481,296	584,609
Total current liabilities	<u>8,905,502</u>	<u>10,644,878</u>
Total liabilities	<u>15,713,425</u>	<u>18,166,955</u>
Total net position and liabilities	<u>\$ 34,832,697</u>	<u>\$ 25,788,536</u>

See accompanying notes to financial statements.

**MARSHALLS ENERGY COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)**

Statements of Revenues, Expenses and Changes in Net Position
Years Ended September 30, 2020 and 2019

	2020	2019
Utility operations:		
Operating revenues:		
Electricity sales	\$ 19,727,133	\$ 18,456,541
Other	60,060	87,250
	<u>19,787,193</u>	<u>18,543,791</u>
Provision for doubtful accounts	(668,027)	(89,588)
	<u>19,119,166</u>	<u>18,454,203</u>
Total net operating revenues		
Operating expenses:		
Cost of fuel	8,370,141	10,177,626
Cost of power	3,268,655	4,220,789
Administrative and general	2,771,162	2,119,112
Distribution operations	1,778,006	1,468,998
Depreciation and amortization	870,614	1,337,543
	<u>17,058,578</u>	<u>19,324,068</u>
Total operating expenses		
Operating income (loss) from utility operations	<u>2,060,588</u>	<u>(869,865)</u>
Nonutility operations:		
Operating revenues:		
Fuel sales	13,527,504	17,948,882
Propane sales	369,569	447,998
Lubricants sales	243,214	60,693
Other	196,731	369,539
	<u>14,337,018</u>	<u>18,827,112</u>
Provision for doubtful accounts	(1,696,665)	(2,513,680)
	<u>12,640,353</u>	<u>16,313,432</u>
Total net operating revenues		
Operating expenses:		
Cost of fuel	11,600,391	15,933,405
Cost of propane and lubricants	442,747	310,177
Other	602,135	672,244
	<u>12,645,273</u>	<u>16,915,826</u>
Total operating expenses		
Operating loss from nonutility operations	<u>(4,920)</u>	<u>(602,394)</u>
Operating income (loss)	<u>2,055,668</u>	<u>(1,472,259)</u>
Nonoperating income (expense):		
RepMar subsidies	1,932,372	2,016,514
Japan Grant Aid	2,100,611	-
Other grants	-	90,435
Interest expense	(103,685)	(154,603)
	<u>3,929,298</u>	<u>1,952,346</u>
Total nonoperating income (expense), net		
Earnings before capital contributions	<u>5,984,966</u>	<u>480,087</u>
Capital contributions:		
Republic of the Marshall Islands	5,512,725	-
Change in net position	<u>11,497,691</u>	<u>480,087</u>
Net position at beginning of year	7,621,581	7,141,494
Net position at end of year	<u>\$ 19,119,272</u>	<u>\$ 7,621,581</u>

See accompanying notes to financial statements.

**MARSHALLS ENERGY COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)**

**Statements of Cash Flows
Years Ended September 30, 2020 and 2019**

	2020	2019
Cash flows from operating activities:		
Cash received from customers	\$ 34,750,411	\$ 36,379,462
Cash payments to suppliers for goods and services	(30,000,739)	(34,464,883)
Cash payments to employees for services	(3,579,540)	(3,498,496)
Net cash provided by (used for) operating activities	<u>1,170,132</u>	<u>(1,583,917)</u>
Cash flows from noncapital financing activities:		
Operating RepMar subsidies received	1,757,920	2,016,514
Other grants received	3,100,000	90,435
Principal paid on long-term debt	(364,794)	(435,287)
Interest paid on long-term debt	(100,598)	(96,153)
Net cash provided by noncapital financing activities	<u>4,392,528</u>	<u>1,575,509</u>
Cash flows from capital and related financing activities:		
Deposit on acquisition of capital assets	-	(300,187)
Acquisition and construction of capital assets	(88,883)	(476,431)
Principal paid on long-term debt	(213,612)	(1,142,303)
Interest paid on long-term debt	(3,087)	(54,180)
Net cash used for capital and related financing activities	<u>(305,582)</u>	<u>(1,973,101)</u>
Cash flows from investing activities:		
Net increase in time certificates of deposit	<u>(53,787)</u>	<u>(548,058)</u>
Net change in cash	5,203,291	(2,529,567)
Cash at beginning of year	2,852,351	5,381,918
Cash at end of year	<u>\$ 8,055,642</u>	<u>\$ 2,852,351</u>
Consisting of:		
Cash	\$ 7,697,189	\$ 2,852,351
Restricted cash	358,453	-
	<u>\$ 8,055,642</u>	<u>\$ 2,852,351</u>
Reconciliation of operating income (loss) to net cash provided by (used for) operating activities:		
Operating income (loss)	\$ 2,055,668	\$ (1,472,259)
Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities:		
Depreciation and amortization	870,614	1,337,543
Provision for doubtful accounts	2,364,692	2,603,268
Decrease (increase) in assets:		
Accounts receivable	(934,372)	(1,794,691)
Due from employees	15,823	39,220
Fuel and supplies	1,082,141	(860,003)
Deposits and other prepayments	(1,318,865)	491,849
Long-term replacement parts	(91,056)	(78,797)
Increase (decrease) in liabilities:		
Accounts payable - fuel	(3,083,894)	(2,498,475)
Accounts payable - other	260,226	92,032
Payable to affiliates	9,410	(187,124)
Accrued leave	193,671	376,144
Accrued taxes	(20,620)	(139,785)
Other accrued liabilities	(139,569)	(112,748)
Unearned fuel purchase incentive	(1,654,309)	(183,341)
Unearned income	1,560,572	803,250
Net cash provided by (used for) operating activities	<u>\$ 1,170,132</u>	<u>\$ (1,583,917)</u>
Noncash capital and related financing activities:		
Transfer of assets from RepMar:		
Capital assets	\$ (37,894,878)	-
Accumulated depreciation	32,382,153	-
Capital contribution	5,512,725	-
	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to financial statements.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(1) Organization

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

An exclusive franchise to construct, maintain and operate a distribution system for furnishing electrical power within Majuro Atoll was granted to MEC by RepMar on March 8, 1983. Simultaneously, RepMar leased to MEC, for a nominal amount, a 12-megawatt power plant, a 6-million-gallon capacity fuel storage facility, electrical transmission systems and related facilities on Majuro Atoll. The term of both the lease and the franchise is for a 50-year period commencing on December 1, 1996.

Pursuant to Cabinet Minute C.M. 162 (93), RepMar leased to MEC, for a nominal amount, the right to operate and manage the power generating and distribution system in Jaluit Atoll effective November 1, 1993. The term of the lease is for a 50-year period commencing on December 1, 1996.

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

MEC is governed by an eight-member RMI Combined Utilities Board of Directors appointed by the Cabinet of RepMar. The RMI Combined Utilities Board of Directors also have governance over KAJUR, which is a component unit of RepMar.

MEC'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 MEC conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental entities, specifically proprietary funds.

MEC considers utility and nonutility revenues and costs that are directly related to the generation, transmission and distribution of electricity and fuel sale operations to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, and GASB Statement No. 61, *The Financial Reporting Entity: Omnibus - an amendment of GASB Statements No. 14 and 34*, 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.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(2) Summary of Significant Accounting Policies, Continued

To conform to these requirements, equity is presented in the following net position categories:

- Net investment in capital assets - capital assets, net of accumulated depreciation and related debt, plus construction or improvement of those assets.
- Restricted: Nonexpendable net position subject to externally imposed stipulations that require MEC to maintain such permanently. As of September 30, 2020 and 2019, MEC does not have nonexpendable restricted net position.
- Restricted: Expendable net position whose use by MEC is subject to externally imposed stipulations that can be fulfilled by actions of MEC pursuant to those stipulations or that expire with the passage of time. As of September 30, 2020, MEC has expendable net position of \$358,453 associated with a repairs and maintenance fund established in accordance with the Subsidiary Loan Agreement between RepMar and the Asian Development Bank (ADB).
- 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.

When both restricted and unrestricted resources are available for use for the same purpose, it is MEC's policy to use unrestricted resources first, then restricted resources as they are needed.

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.

Revenue Recognition

Sales of electricity are recorded as billed to customers on a monthly billing cycle basis. Unbilled revenues are not accrued as the most recent meter reading date approximates the end of the reporting period. Revenue from fuel and propane sales are billed to customers on a daily basis based on the actual quantity of fuel and propane delivered.

Cash and Time Certificates of Deposit

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

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(2) Summary of Significant Accounting Policies, Continued

Cash and Time Certificates of Deposit, Continued

For purposes of the statements of net position and cash flows, cash is defined as cash on hand and cash held in demand accounts. Deposits maintained in time certificates of deposit with original maturity dates greater than three months are separately classified. As of September 30, 2020 and 2019, the carrying amount of cash and time certificates of deposit was \$11,054,406 and \$5,797,328, respectively, and the corresponding bank balances were \$11,264,140 and \$5,384,979, respectively. Of the bank balance amounts, \$5,328,848 and \$1,871,787, respectively, were maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2020 and 2019, bank deposits in the amount of \$250,000 were FDIC insured. The remaining bank deposits of \$5,935,292 and \$3,513,192, respectively, were maintained in a financial institution not subject to depository insurance. MEC does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC coverage are uncollateralized. Accordingly, these deposits were exposed to custodial credit risk.

As of September 30, 2020, a cash deposit of \$358,453 was restricted for repairs and maintenance of capital assets directly related to power generation and distribution in accordance with the Subsidiary Loan Agreement between RepMar and the ADB. (see note 5).

Receivables

All receivables are due from government agencies, businesses and individuals located within the Republic of the Marshall Islands and are interest free and uncollateralized. The allowance for uncollectible accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. Management determines the adequacy of the allowance for uncollectible accounts based upon review of the aged accounts receivable. The allowance is established through a provision for bad debts charged to expense. Bad debts are written off against the allowance on the specific identification method.

Fuel and Supplies

Fuel and supplies are valued at the lower of cost (moving average) or market (net realizable value).

Prepayments

Prepayments represent certain payments made to vendors or persons for services reflecting costs applicable to future accounting periods.

Long-term Replacement Parts

Long-term replacement parts are slow-moving inventory not reasonably expected to be realized in cash during MEC's normal operating cycle and are valued at the lower of cost (moving average) or market (net realizable value).

Plant and Nonutility Property

Plant and nonutility property with a cost that equals or exceeds \$500 is capitalized. Such assets are stated at cost. Depreciation of plant and nonutility property and amortization of leasehold land and residences are calculated on the straight-line method based on the estimated useful lives of the respective assets. Costs pertaining to distribution and line supplies are expensed during the year of installation as MEC considers the estimated useful lives of these supplies to be less than one year.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(2) Summary of Significant Accounting Policies, Continued

Plant and Nonutility Property, Continued

The estimated useful lives of these assets are as follows:

Power plant engines	20 years
Plant and machinery	3 - 10 years
Vehicles	2 - 4 years
Leasehold improvements	20 years
Residences	20 years
Fences and seawalls	10 years
Leasehold land	20 years
Solar power systems	15 years
Furniture and fixtures	3 - 5 years
Land and building	20 years
Computer software	3 - 5 years

Deferred Outflows of Resources

In addition to assets, the statements 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. MEC has no items that qualify for reporting in this category.

Deferred Inflows of Resources

In addition to liabilities, the statements 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. MEC has no items that qualify for reporting in this category.

Compensated Absences

MEC recognizes the cost of accrued annual and sick leave at the time such leave is earned. As of September 30, 2020 and 2019, MEC recorded accrued annual and sick leave of \$569,815 and \$376,144, respectively, which is included within the statements of net position as accrued leave. Sick leave will not be advanced or paid to employees upon termination of their employment. Unused sick leave may be accumulated and carried over in subsequent payroll years. Unused annual or vacation leave hours in excess of the 208 hours annual limit will not be carried over into a succeeding payroll year. Annual or vacation time can be taken up to a maximum of twenty (20) days in a payroll year.

Taxes

Corporate profits are not subject to income tax in the Republic of the Marshall Islands. The Government of the Republic of the Marshall Islands imposes a gross revenue tax of 3% on revenues. Pursuant to the Income Tax Act of 1989, as amended, sales of electricity by public utility companies are exempt from gross revenue tax. Accordingly, MEC is exempt from gross revenue tax on the sale of electric services. MEC is required to pay gross revenue tax on all other revenues. Pursuant to the Import Duties (MEC Exemption) Act of 2008, MEC is exempt from paying import duty on all types of fuel imported in the Republic of the Marshall Islands, including fuel imported for power generation and for commercial resale.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended September 30, 2020, GASB issued Statement No. 95, *Postponement of the Effective Dates of Certain Authoritative Guidance*, which postpones the effective dates of GASB Statement No. 84, 89, 90, 91, 92 and 93 by one year and GASB Statement No. 87 by 18 months; however, earlier application of the provisions addressed in GASB Statement No. 95 is encouraged and is permitted to the extent specified in each pronouncement as originally issued. In accordance with GASB Statement No. 95, management has elected to postpone implementation of these statements.

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*. This Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. The requirements of this Statement will enhance consistency and comparability by (1) establishing specific criteria for identifying activities that should be reported as fiduciary activities and (2) clarifying whether and how business-type activities should report their fiduciary activities. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 84 will be effective for fiscal year ending September 30, 2021.

In June 2017, GASB issued Statement No. 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and as inflows of resources or outflows of resources recognized based on the payment provisions of the contract. Management believes that this statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 87 will be effective for fiscal year ending September 30, 2022.

In June 2018, GASB issued Statement No. 89, *Accounting for Interest Cost Incurred Before the End of a Construction Period*. The objectives of this Statement are (1) to enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and (2) to simplify accounting for interest cost incurred before the end of a construction period. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 89 will be effective for fiscal year ending September 30, 2022.

In March 2018, GASB issued Statement No. 90, *Majority Equity Interests - An Amendment of GASB Statements No. 14 and 61*. The primary objectives of this Statement are to improve the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and to improve the relevance of financial statement information for certain component units. It defines a majority equity interest and specifies that a majority equity interest in a legally separate organization should be reported as an investment if a government's holding of the equity interest meets the definition of an investment. A majority equity interest that meets the definition of an investment should be measured using the equity method, unless it is held by a special-purpose government engaged only in fiduciary activities, a fiduciary fund, or an endowment (including permanent and term endowments) or permanent fund. Those governments and funds should measure the majority equity interest at fair value. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 90 will be effective for fiscal year ending September 30, 2021.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In May 2019, GASB issued Statement No. 91, *Conduit Debt Obligations*. The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 91 will be effective for fiscal year ending September 30, 2023.

In January 2020, GASB issued statement No. 92, *Omnibus 2020*. The objectives of this Statement are to enhance comparability in accounting and financial reporting and to improve the consistency of authoritative literature by addressing practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics and includes specific provisions about the effective date of Statement No. 87, Leases, and Implementation Guide No. 2019-3, Leases, for interim financial reports, the terminology used to refer to derivative instruments and the applicability of certain requirements of Statement No. 84, Fiduciary Activities, to postemployment benefits. The requirements related to the effective date of GASB Statement No. 87 and Implementation Guide 2019-3, reissuance recoveries and terminology used to refer to derivative instruments are effective upon issuance. In accordance with GASB Statement No. 95, the remaining requirements of GASB Statement No. 92 is effective for the fiscal year ending September 30, 2022.

In March 2020, GASB issued Statement No. 93, *Replacement of Interbank Offered Rates*. The primary objective of this statement is to address those and other accounting and financial reporting implications of the replacement of an IBOR. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. Except for paragraphs 11b, 13, and 14, GASB Statement No. 93 will be effective for fiscal year ending September 30, 2021. The requirement in paragraphs 11b, 13, and 14 are effective for fiscal year September 30, 2022.

In March 2020, GASB issued Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*. The primary objective of this statement is to improve financial reporting by addressing issues related to public-private and public-public partnership arrangements. This statement also provides guidance for accounting and financial reporting for availability payment arrangements. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 94 will be effective for fiscal year ending September 30, 2023.

In May 2020, GASB issued Statement No. 96, *Subscription-Based Information Technology Arrangements*. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users (governments). This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-to-use subscription asset - an intangible asset - and a corresponding subscription liability; (3) provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and (4) requires note disclosures regarding a SBITA. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 96 will be effective for fiscal year ending September 30, 2023.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In June 2020, GASB issued Statement No. 97, *Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans - an amendment of GASB Statements No. 14 and No. 84, and a supersession of GASB Statement No. 32*. The primary objectives of this Statement are to (1) increase consistency and comparability related to the reporting of fiduciary component units in circumstances in which a potential component unit does not have a governing board and the primary government performs the duties that a governing board typically would perform; (2) mitigate costs associated with the reporting of certain defined contribution pension plans, defined contribution other postemployment benefit (OPEB) plans, and employee benefit plans other than pension plans or OPEB plans (other employee benefit plans) as fiduciary component units in fiduciary fund financial statements; and (3) enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code (IRC) Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans. GASB Statement No. 97 will be effective for fiscal year ending September 30, 2022.

Estimates

The preparation of financial statements in accordance with GAAP 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) Accounts Receivable

Accounts receivable at September 30, 2020 and 2019, consist of the following:

	<u>2020</u>	<u>2019</u>
RepMar and other affiliates	\$ 11,040,800	\$ 10,569,599
Other:		
Electricity	4,435,049	3,734,270
Solar	1,482,825	1,318,905
Fuel	774,551	528,366
Other	<u>235,030</u>	<u>962,160</u>
Less allowance for uncollectible accounts	<u>17,968,255</u> <u>(13,825,498)</u>	<u>17,113,300</u> <u>(11,783,604)</u>
	<u>\$ 4,142,757</u>	<u>\$ 5,329,696</u>

MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)

Notes to Financial Statements
September 30, 2020 and 2019

(4) Fuel and Supplies

Fuel and supplies at September 30, 2020 and 2019, consist of the following:

	<u>2020</u>	<u>2019</u>
Fuel	\$ 2,892,409	\$ 4,906,862
Distribution and power plant supplies	2,390,425	1,641,378
Lubricants	411,484	227,800
Propane gas	<u>49,701</u>	<u>50,120</u>
	<u>\$ 5,744,019</u>	<u>\$ 6,826,160</u>

(5) Capital Assets

Capital asset activity for the years ended September 30, 2020 and 2019 is as follows:

	2020		
	October 1, 2019	Additions	Disposals
Utility Plant:			September 30, 2020
Power plant engines	\$ 20,090,438	\$ 3,223,800	\$ -
Tank farm	-	23,900,000	-
Distribution	-	3,316,665	-
Plant and machinery	2,335,357	239,132	-
Land and building	1,846,877	-	1,846,877
Solar power systems	1,110,417	7,454,413	-
Vehicles	1,100,608	48,581	(96,018)
Leasehold improvements	641,012	-	641,012
Residences	561,073	-	561,073
Fences and seawalls	371,702	-	371,702
Leasehold land	330,000	-	330,000
Computer software	43,981	19,364	-
Furniture and fixtures	<u>1,082,868</u>	<u>81,968</u>	<u>-</u>
	29,514,333	38,283,923	(96,018)
Less accumulated depreciation and amortization	<u>(24,041,530)</u>	<u>(33,243,118)</u>	<u>96,018</u>
	5,472,803	5,040,805	-
Construction work-in-progress	<u>865,850</u>	<u>28,687</u>	<u>(307,585)</u>
	<u>6,338,653</u>	<u>5,069,492</u>	<u>(307,585)</u>
			<u>11,100,560</u>
Nonutility Plant:			
LPG terminal	181,862	209,969	(181,862)
Less accumulated depreciation and amortization	<u>(181,862)</u>	<u>(9,624)</u>	<u>181,862</u>
	<u>-</u>	<u>200,345</u>	<u>-</u>
	<u>\$ 6,338,653</u>	<u>\$ 5,269,837</u>	<u>\$ (307,585)</u>
			<u>\$ 11,300,905</u>

MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)

Notes to Financial Statements
September 30, 2020 and 2019

(5) Capital Assets, Continued

	2019		
	October 1, 2018	Additions	Disposals
Utility Plant:			September 30, 2019
Power plant engines	\$ 20,090,438	\$ -	\$ 20,090,438
Plant and machinery	2,261,207	104,528	(30,378)
Land and building	1,846,877	-	1,846,877
Solar power systems	1,110,417	-	1,110,417
Vehicles	1,215,611	20,000	(135,003)
Leasehold improvements	641,012	-	641,012
Residences	561,073	-	561,073
Fences and seawalls	371,702	-	371,702
Leasehold land	330,000	-	330,000
Computer software	42,865	1,116	43,981
Furniture and fixtures	<u>1,107,910</u>	<u>140,818</u>	<u>(165,860)</u>
	29,579,112	266,462	(331,241)
Less accumulated depreciation and amortization	<u>(23,035,228)</u>	<u>(1,337,543)</u>	<u>331,241</u>
	6,543,884	(1,071,081)	-
Construction work-in-progress	<u>655,881</u>	<u>209,969</u>	<u>-</u>
	<u>7,199,765</u>	<u>(861,112)</u>	<u>-</u>
Nonutility Plant:			<u>6,338,653</u>
LPG terminal	181,862	-	181,862
Less accumulated depreciation and amortization	<u>(181,862)</u>	<u>-</u>	<u>(181,862)</u>
	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ 7,199,765</u>	<u>\$ (861,112)</u>	<u>\$ -</u>
			<u>\$ 6,338,653</u>

In accordance with the Subsidiary Loan Agreement between RepMar and the Asian Development Bank (ADB), MEC created a separate bank account dedicated for repair and maintenance funds (R&M Fund). Starting October 1, 2010, MEC made automatic \$35,000 monthly transfers into the R&M Fund from its revenue accounts. Amounts in the R&M Fund shall be used exclusively for repair, maintenance, procurement of spare parts, materials and equipment (and related labor costs) directly related to power generation and distribution. As of September 30, 2020 and 2019, the R&M Fund has a balance of \$358,453 and \$142,399, respectively.

(6) Long-Term Debt

Notes and Loan Payable

Long-term debt at September 30, 2020 and 2019 is as follows:

	Interest Rate	Maturity Dates	2020	2019
Rural Utilities Service	5.49% - 7.25%	2020	\$ -	\$ 213,612
Asian Development Bank	1%	2034	<u>5,850,336</u>	<u>6,215,130</u>
			<u>\$ 5,850,336</u>	<u>\$ 6,428,742</u>

The Rural Utilities Service (RUS) mortgage notes have been unconditionally guaranteed by RepMar, under which RepMar will make debt service payments to RUS in the event of default by MEC, and have been collateralized by a leasehold mortgage and security agreement over the assets of MEC.

MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)

Notes to Financial Statements
September 30, 2020 and 2019

(6) Long-Term Debt, Continued

Notes and Loan Payable, Continued

Annual repayment requirements to maturity for principal and interest are as follows:

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2021	\$ 342,064	\$ 85,636	\$ 427,700
2022	375,470	80,050	455,520
2023	381,141	74,379	455,520
2024	386,898	68,622	455,520
2025	392,741	62,779	455,520
2026-2030	2,054,496	223,104	2,277,600
2031-2034	<u>1,917,526</u>	<u>62,958</u>	<u>1,980,484</u>
	<u>\$ 5,850,336</u>	<u>\$ 657,528</u>	<u>\$ 6,507,864</u>

Change in Long-term Debt

A summary of changes in long-term debt for the years ended September 30, 2020 and 2019 is as follows:

	<u>Balance October 1, 2019</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2020</u>	<u>Due Within One Year</u>
Notes payable: RUS loan	\$ 213,612	\$ -	\$ (213,612)	\$ -	\$ -
Loan payable: ADB	<u>6,215,130</u>	<u>-</u>	<u>(364,794)</u>	<u>5,850,336</u>	<u>342,064</u>
	<u>\$ 6,428,742</u>	<u>\$ -</u>	<u>\$ (578,406)</u>	<u>\$ 5,850,336</u>	<u>\$ 342,064</u>
	<u>Balance October 1, 2018</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2019</u>	<u>Due Within One Year</u>
Notes payable: RUS loan	\$ 1,355,915	\$ -	\$ (1,142,303)	\$ 213,612	\$ 213,612
Loan payable: ADB	<u>6,650,417</u>	<u>-</u>	<u>(435,287)</u>	<u>6,215,130</u>	<u>336,974</u>
	<u>\$ 8,006,332</u>	<u>\$ -</u>	<u>\$ (1,577,590)</u>	<u>\$ 6,428,742</u>	<u>\$ 550,586</u>

Debt Covenants

Asian Development Bank:

MEC obtained a subsidiary loan from the Asian Development Bank (ADB), through RepMar. The ADB Subsidiary Loan Agreement, dated September 8, 2010, is utilized to pay off a bank loan that was originally procured for operating purposes. The Loan Agreement specifies that in case of default, RepMar, at its option, may by notice to MEC declare the principal of the subsidiary loan then outstanding to be due and payable immediately together with the interest and other charges.

MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)

Notes to Financial Statements
September 30, 2020 and 2019

(6) Long-Term Debt, Continued

Debt Covenants, Continued

Rural Utilities Service:

The RUS Loan Agreement, dated May 1, 1997, sets forth covenants to ensure proper operation and maintenance of the electric utility system and payment of debt service. The primary requirements of the loan agreement is summarized below:

Rate Covenant - MEC has covenanted to at all times fix, prescribe and collect rates, fees and charges in connection with the services furnished by the electric utility system that will be sufficient to yield the sum of net income during each fiscal year equal to at least 125% of the annual debt service. TIER is defined as net income (after tax) plus interest divided by interest expense. The Loan Agreement prohibits MEC, without the prior written consent of RUS, to incur additional indebtedness while MEC maintains a TIER below 1.0; or if the additional indebtedness will cause MEC's TIER to fall below 1.0; or an Event of Default has occurred and is continuing.

Events of default with finance related consequences - the Loan Agreement specifies a number of Events of Default and related Remedies. MEC shall furnish to RUS promptly, after becoming aware, notice of the occurrence of any default under the Loan Documents or the receipt of any notice with respect to the occurrence of any event with which the giving of notice or the passage of time, or both, could become an Event of Default.

Acceleration - Upon the occurrence of an Event of Default and is continuing, RUS may, by notice in writing to MEC, declare all unpaid principal of and all interest accrued on the Notes to be immediately due and payable and, upon such declaration, all such principal and interest shall become immediately due and payable.

(7) Change in Long-Term Liabilities

Changes in other long-term liabilities during the years ended September 30, 2020 and 2019 were as follows:

	Balance October 1, <u>2019</u>	Additions	Reductions	Balance September 30, 2020	Due Within One Year
Accrued leave	\$ 376,144	\$ 359,612	\$ (165,941)	\$ 569,815	\$ 269,553
Counterpart fund fund payable (see Note 9)	-	999,389	-	999,389	-
Unearned fuel purchase incentive (see Note 10)	<u>1,654,309</u>	-	<u>(1,654,309)</u>	-	-
	<u>\$ 2,030,453</u>	<u>\$ 1,359,001</u>	<u>\$ (1,820,250)</u>	<u>\$ 1,569,204</u>	<u>\$ 269,553</u>
	Balance October 1, <u>2018</u>	Additions	Reductions	Balance September 30, 2019	Due Within One Year
Accrued leave	\$ -	\$ 376,144	\$ -	\$ 376,144	\$ 202,720
Unearned fuel purchase incentive (see Note 10)	<u>1,837,650</u>	-	<u>(183,341)</u>	<u>1,654,309</u>	<u>183,812</u>
	<u>\$ 1,837,650</u>	<u>\$ 376,144</u>	<u>\$ (183,341)</u>	<u>\$ 2,030,453</u>	<u>\$ 386,532</u>

MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)

Notes to Financial Statements
September 30, 2020 and 2019

(8) Employee Retirement Plan

MEC, together with KAJUR and MWSC, have implemented a defined contribution retirement savings plan (the Plan) for their respective employees, whereby employees eighteen years and older are eligible to participate upon one year of employment. Plan participants may contribute any amount of their salaries to be matched 100% by their respective employers up to 10% of base salaries. Withdrawal from the Plan occurs upon termination of employment, death, or financial hardship. Plan assets are held in a trust fund administered by a trustee in accordance with the trust agreement. Management has the authority to establish or amend Plan provisions and contribution requirements. MEC contributed \$78,701 and \$85,638 to Plan participant accounts during the years ended September 30, 2020 and 2019, respectively, and total combined plan assets were \$1,200,577 and \$1,616,246 as of September 30, 2020 and 2019, respectively.

(9) Related Party Transactions

MEC is wholly-owned by RepMar and is therefore affiliated with all RepMar-owned and affiliated entities, including KAJUR and MWSC. RepMar subscribes for electricity generated by MEC and is charged for electricity usage at substantially the same rates as those charged to commercial establishments. In addition, RepMar purchases fuel from MEC at the same commercial terms and conditions as afforded to third parties. MEC's receivables from related parties are afforded more favorable payment terms than those extended to unrelated parties.

A summary of related party transactions for the years ended September 30, 2020 and 2019, and the related receivable and payable balances as of September 30, 2020 and 2019, are as follows:

	2020			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 2,810,442	\$ 1,069,458	\$ 666,539	\$ 480,111
Kwajalein Atoll Joint Utilities Resources, Inc.	3,266,355	66,980	6,166,163	-
Majuro Water and Sewer Company, Inc.	329,547	5,705	3,177,695	-
Marshall Islands Social Security Administration	36,347	641,992	10,257	-
Majuro Resort, Inc.	434,029	52,440	557,774	3,642
Marshall Islands National Telecommunications Authority	581,111	87,300	157,606	17,844
College of Marshall Islands	480,308	-	153,776	-
Other	<u>994,248</u>	<u>129,788</u>	<u>150,990</u>	<u>1,698</u>
	<u>\$ 8,932,387</u>	<u>\$ 2,053,663</u>	<u>\$ 11,040,800</u>	<u>\$ 503,295</u>
	2019			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 2,905,367	\$ 1,177,785	\$ 1,270,054	\$ 451,651
Kwajalein Atoll Joint Utilities Resources, Inc.	4,143,584	-	5,477,036	-
Majuro Water and Sewer Company, Inc.	415,638	31,784	2,957,694	-
Marshall Islands Social Security Administration	26,565	484,425	4,138	-
Majuro Resort, Inc.	451,233	15,949	472,494	2,162
Marshall Islands National Telecommunications Authority	553,280	92,554	97,292	23,862
College of Marshall Islands	372,987	-	130,997	-
Other	<u>1,004,306</u>	<u>152,988</u>	<u>159,894</u>	<u>16,210</u>
	<u>\$ 9,872,960</u>	<u>\$ 1,955,485</u>	<u>\$ 10,569,599</u>	<u>\$ 493,885</u>

The allowance for uncollectable accounts pertaining to receivables from affiliates amounted to \$9,767,130 and \$7,694,877 as of September 30, 2020 and 2019, respectively.

During the year ended September 30, 2020, MEC transferred a 10,000 gallon fuel tank to Kwajalein Atoll Joint Utilities Resources, Inc. (KAJUR) at cost in the amount of \$68,929. At September 30, 2020, KAJUR has yet to remit payment associated with this sale.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(9) Related Party Transactions, Continued

During the years ended September 30, 2020 and 2019, MEC received subsidies from RepMar as follows:

	<u>2020</u>	<u>2019</u>
General Fund:		
Jaluit and Wotje operations	\$ 432,372	\$ 516,260
European Development Fund:		
Renewal Energy and Energy Efficiency Grant	<u>1,500,000</u>	<u>1,500,254</u>
	<u>\$ 1,932,372</u>	<u>\$ 2,016,514</u>

As of September 30, 2020, the amount of \$174,452 relating to General Fund subsidies is due from RepMar.

On January 3, 2020, the RepMar Cabinet authorized and approved the transfer from RepMar to MEC of all assets associated with Majuro public power distribution services. Capital assets of \$37,894,878, net of accumulated depreciation of \$32,382,153, were transferred representing capital contributions of \$5,512,725.

During the years ended September 30, 2020 and 2019, MEC was the subrecipient of RepMar grant funding in the amount of \$1,500,000 and \$1,500,254, respectively, from the 11th European Development Fund (EDF11) under the ACP-EU Partnership Agreement to support reform of the energy sector in RMI.

In 2015, the Government of Japan and RepMar concluded a grant agreement for Non-Project Grant Aid in the amount of JPY100,000,000 with MEC as the ultimate grantee. The purpose of the Grant is to assist in the supply of petroleum fuel to MEC and mitigating the social and economic difficulties caused by volatile and sustained high oil prices. The Grant was paid directly by the Government of Japan through an independent procurement agent to MEC's fuel supplier. During the year ended September 30, 2017, MEC received the equivalent gallons of fuel from the supplier in the amount of \$726,263. As part of the agreement, MEC was required to establish a counterpart fund with RepMar in the amount of \$275,952 no later than July 5, 2018. As of September 30, 2020 and 2019, MEC has fully satisfied the requirement to make counterpart fund payments to RepMar.

In 2020, the Government of Japan and RepMar entered into a grant agreement for Grant Aid in the amount of JPY33,390,000 with MEC as the ultimate grantee. The purpose of the Grant is to assist in the supply of petroleum fuel to MEC and mitigating the social and economic difficulties caused by volatile and sustained high oil prices. The Grant was paid directly by the Government of Japan through an independent procurement agent to MEC's fuel supplier. During the year ended September 30, 2020, MEC received the equivalent gallons of fuel from the supplier in the amount of \$3,100,000. As part of the agreement, MEC was required to establish a counterpart fund with RepMar in the amount of \$999,389 no later than March 19, 2023. As of September 30, 2020, MEC has reported a long-term liability of \$999,389 to set aside the counterpart fund payments to RepMar.

As of September 30, 2020 and 2019, MEC is liable for current and delinquent gross revenue taxes to RepMar, totaling \$1,764,706 and \$1,803,718, respectively. In addition, MEC is liable for current and delinquent withholding payroll taxes to RepMar, totaling \$17,891 and \$25,288, respectively. Accrued taxes payable exclude related penalties and interest.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(10) Commitments and Contingencies

Commitments

In 2017, MEC entered into a diesel fuel supply agreement (“the supply agreement”) with ExxonMobil Asia Pacific Pte. Ltd. (ExxonMobil) for an initial period of three years with automatic renewal for an additional period of seven years. In accordance with the supply agreement, MEC is obligated to purchase a minimum quota of 310,000 bbls per annum. Concurrently, MEC entered into a marketing assistance program agreement (“the marketing agreement”) with ExxonMobil whereby ExxonMobil provided \$2,000,000 to MEC as a fuel purchase incentive for the purpose of assisting MEC in the marketing of ExxonMobil products. In the event that MEC is unable to purchase the minimum quota, MEC will be subject to certain damages as outlined in the marketing agreement. Accordingly, MEC will recognize the fuel purchase incentive over the term of the supply agreement. As of September 30, 2019, MEC has recorded a liability of \$1,654,309 associated with the marketing agreement as unearned fuel purchase incentive in the accompanying financial statements. In July 2020, MEC did not renew the supply agreement with ExxonMobil and repaid unliquidated fuel purchase incentive of \$1,654,309. (see Note 13)

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

MEC is a party to several legal proceedings arising from its operations; however, no provision for any liability was made in the accompanying financial statements due to the uncertainty of the legal proceeding outcomes. Although financial exposure has yet to be determined, MEC's management believes that the provision for any liability will not be material to the accompanying financial statements.

MEC is in the process of developing and implementing plans and systems to ensure effective waste oil management and environmental protection. MEC's management believes that no provision for any liability, if any, which may arise from this matter is required to be reflected in the accompanying financial statements.

MEC has a material amount of unpaid gross revenue and withholding payroll taxes payable to RepMar as of September 30, 2020. The nonpayment of taxes is an effort to address increasing accounts receivable balances due from related parties via an offsetting exercise to reduce each party's liabilities. MEC's management believes that no provision for any additional liability, if any, which may arise from this matter is required to be reflected in the accompanying financial statements.

MEC has a material amount of nonmoving construction work-in-progress as of September 30, 2020. The non-movement of construction work-in-progress is due to (a) MEC is in the process of working on various covenants imposed by the grantor prior to grant finalization; and (b) existing land disputes between landowners. MEC's management believes that no impairment, if any, that may arise from this matter is required to be reflected in the accompanying financial statements

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements
September 30, 2020 and 2019

(11) Risk Management

MEC is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. MEC has elected to purchase commercial insurance from independent third parties for the risks of loss to which it is exposed. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

Insurance proceeds of \$3,410,336 received in 2007 for fire damage to MEC's power plant building and engines were recorded net of estimated repair costs. Subsequent to the year ended September 30, 2019, MEC received \$320,000 against this claim with the balance being fully provided for during the year ended September 30, 2019. During the year ended September 30, 2020, MEC has written off the remaining balance of the claim and reversed the corresponding allowance for uncollectible accounts.

(12) COVID-19 Pandemic

On March 11, 2020, the World Health Organization declared the novel strain of coronavirus (COVID-19) a global pandemic and recommended the containment and mitigation measures worldwide. On October 28, 2020, one confirmed case was identified in the Marshall Islands that was subsequently isolated and contained. On November 17, 2020, an additional three cases were identified and which were isolated and contained. As of November 2, 2021, no community transmission has been identified. MEC has determined that should community transmission occur within the Marshall Islands, it may negatively impact MEC's operations and MEC may become dependent upon the financial support of RepMar. However, the effect of the pandemic on RepMar is also uncertain and future available funding to RepMar component units may be limited. Therefore, while MEC expects this matter to potentially have a negative impact on its business, results of operations, and financial position, the related financial impact cannot be reasonably estimated at this time.

(13) Subsequent Events

On November 13, 2020, MEC entered into a diesel fuel supply agreement with Winson Oil Bunkering Pte. Ltd. for an initial period of five years with automatic renewal for an additional period of five years, unless one of the parties serves a notice of intention not to renew the contract at least 180 days prior to the expiry of the contract.

On June 1, 2021, MEC entered into a sales and purchase agreement for a shipping vessel in the amount of \$2,450,000.

MARSHALLS ENERGY COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Schedule of Revenues, Expenses and Changes in Net Position by Division
Year Ended September 30, 2020

	Generation	Distribution	Tank Farm	Jaluit	Wotje	Solar	MEC Gas	Admin.	TOTAL
Operating revenues:									
Fuel, propane and lube sales	\$ -	\$ -	\$ 13,762,844	\$ 7,379	\$ 495	\$ -	\$ 369,569	\$ -	\$ 14,140,287
Cost of sales	-	-	11,786,752	-	-	-	256,386	-	12,043,138
Gross profit on sales	-	-	1,976,092	7,379	495	-	113,183	-	2,097,149
Electric and service billings	19,151,322	-	-	234,236	151,500	190,075	-	-	19,727,133
Service and other income	-	70,009	84,309	17,599	421	-	4,179	80,274	256,791
Less provision for doubtful accounts	(639,543)	-	(1,555,550)	-	-	(163,920)	-	(5,679)	(2,364,692)
Total electricity sales and other income	18,511,779	70,009	(1,471,241)	251,835	151,921	26,155	4,179	74,595	17,619,232
Total net operating revenue	18,511,779	70,009	504,851	259,214	152,416	26,155	117,362	74,595	19,716,381
Operating expenses:									
Fuel and lubes	8,372,944	13,998	-	149,347	141,519	-	-	-	8,677,808
Salaries, wages and benefits	1,232,535	668,548	85,532	148,983	162,742	302,723	52,487	1,084,790	3,738,340
Repairs and maintenance	536,261	679,030	32,672	56,476	7,099	2,000	87,223	64,883	1,465,644
Depreciation and amortization	562,330	93,628	12,880	3,422	1,340	74,028	12,919	110,067	870,614
Professional and consulting fees	57,097	-	313,063	-	-	-	-	48,478	418,638
Gross revenue tax	-	2,103	398,074	653	27	-	10,890	784	412,531
Insurance	175,765	12,301	92,692	9,251	9,251	-	-	31,383	333,727
Office	62,107	4,412	54,775	5,001	4,208	925	2,689	135,820	269,937
Freight and handling	48,715	109,306	14,540	40,814	9,682	198	-	19,070	242,325
Import tax	80,875	104,606	1,849	3,638	143	9,021	3,171	16,151	219,454
Auto, POL and maintenance	25,972	96,566	10,783	5,944	2,513	2,161	3,982	35,940	183,861
Utility	42,371	417	10,458	9,782	-	-	-	86,580	149,608
Membership and other fees	6,315	1,300	1,380	-	-	-	-	99,511	108,576
Bank charges	200	-	-	-	-	-	-	94,996	95,196
Communications	32,639	6,033	2,897	2,082	2,435	615	1,081	37,765	85,547
Donations	984	68,840	-	-	-	-	133	9,648	79,605
Security services	14,372	-	15,679	-	-	-	32,353	830	63,234
Equipment rental	3,250	1,180	955	50,330	-	4,424	-	1,761	61,900
Travel	3,385	-	656	26,993	1,217	5,076	-	10,167	47,494
Staff training	-	6,389	4,594	-	-	-	1,600	29,999	42,582
Safety and uniforms	25,813	3,369	6,121	148	-	65	1,106	3,067	39,689
Entertainment	637	1,510	512	1,153	859	-	-	23,493	28,164
Lease rental	-	-	-	5,275	3,833	-	-	7,830	16,938
Advertising	201	201	1,574	-	-	-	627	6,698	9,301
Total operating expenses	11,284,768	1,873,737	1,061,686	519,292	346,868	401,236	213,415	1,959,711	17,660,713
Operating income (loss)	7,227,011	(1,803,728)	(556,835)	(260,078)	(194,452)	(375,081)	(96,053)	(1,885,116)	2,055,668
Nonoperating income (expense):									
RepMar subsidies	-	-	-	269,473	162,899	-	-	1,500,000	1,932,372
Japan Grant Aid	-	-	2,100,611	-	-	-	-	-	2,100,611
Interest expense	-	-	-	-	-	-	-	(103,685)	(103,685)
	-	-	2,100,611	269,473	162,899	-	-	1,396,315	3,929,298
Capital contributions									
Republic of the Marshall Islands	5,512,725	-	-	-	-	-	-	-	5,512,725
Change in net position	\$ 12,739,736	\$ (1,803,728)	\$ 1,543,776	\$ 9,395	\$ (31,553)	\$ (375,081)	\$ (96,053)	\$ (488,801)	\$ 11,497,691

See accompanying independent auditors' report.

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
Marshalls Energy Company, Inc.:

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the Marshalls Energy Company, Inc. (MEC), which comprise the statement of net position as of September 30, 2020, and the related statements of revenues, expenses, and changes in net position and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated November 2, 2021.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered MEC's internal control over financial reporting (internal control) as a basis for designing 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 MEC's internal control. Accordingly, we do not express an opinion on the effectiveness of MEC'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.

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

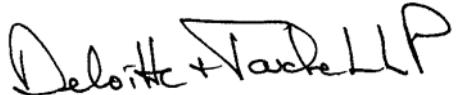
As part of obtaining reasonable assurance about whether MEC's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. 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 2020-001 and 2020-002.

MEC's Response to Findings

MEC's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. MEC'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.

A handwritten signature in black ink that reads "Deloitte + Haskells LLP". The signature is fluid and cursive, with "Deloitte" on the first line and "+ Haskells LLP" on the second line.

November 2, 2021

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Schedule of Findings and Responses
Year Ended September 30, 2020

Finding No. 2020-001

Local Noncompliance

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. 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 supply, service, or construction item without completion when it is determined in writing that there is only one source for the required supply, service, or construction them.

Condition: The below were awarded to vendors without documentation of the basis of the award, with no quotations obtained from an adequate number of qualified vendors and/or with no evidence of competitive sealed bidding.

<u>Category</u>	<u>Amount</u>
Engine overhaul	\$ 649,581
Insurance	248,729
Professional fees	210,885
Cost of goods sold	59,500
Lubricants	47,318
Maintenance supplies	40,276
Equipment rental	<u>12,000</u>
	 <u>\$ 1,268,289</u>

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

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

Recommendation: We recommend that management establish adequate internal control policies and procedures requiring compliance with RepMar's Procurement Code. We recommend management complete documentation of procurement process, from requesting of proposals from a number of qualified vendors, evaluation of submitted bids to documentation of rationale for vendor selected. Specifically, if there are limited bids received, management should document the matter and perform additional procedures to document compliance with the competitive sealed bidding requirement of the code, if applicable.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Schedule of Findings and Responses, Continued
Year Ended September 30, 2020

Finding No. 2020-001, Continued

Local Noncompliance

Prior Year Status: Recommendation concerning management to establish policies and procedures pertaining to compliance with RepMar's Procurement Code was reported as a finding in the audit of MEC for fiscal years 2016 through 2019.

Auditee Response and Corrective Action Plan: MEC recognizes the need to formally establish its own procurement policy tailored to the specialized needs of the industry.

For engine parts related to overhaul, MEC's Deutz engines have very limited suppliers of genuine or quality parts. The particular vendor was selected based on review of parts listed by the mechanics and recommendation made by them.

For the insurance vendor, MEC has had the same vendor for the past 10 years at least and because of MEC's aged assets and recent fire, MEC has had difficulties in satisfying data collection and other minimum requirements for other insurance providers and has continued with the same insurance provider who has been willing to continue their insurance.

For professional fees, these relate to one consulting firm who was engaged with MEC and their engagement, at that point in time, was detrimental to the nation's fuel supply security and this was communicated to the BOD who reviewed and agreed with the urgency and approved the contract.

For COGS and equipment rental, this relates to charter of vessels to transport fuel to KAJUR and Jaluit and currently there is a shortage of vessels operating to transport fuel so in organizing such delivery MEC engages the vessel that is available at that point in time; relates to fuel supply security for powerplants on Ebeye and Jaluit.

For lubes, because of volumes for powerplant usage and for resale and because of increase in fuel sales, MEC always seeks the most competitive lube prices and any purchases is always supported by 3 quotes.

For maintenance supplies, these relate to charges from vendors who were involved in the past with construction and implementation of the facility's systems and MEC continued with their services as hiring a new vendor would be inefficient and not cost effective.

As of the date of this report, MEC's internal procurement policy is being developed by management and to be finalized and approved by the Board within the next fiscal year.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Schedule of Findings and Responses, Continued
Year Ended September 30, 2020

Finding No. 2020-002

Local Noncompliance

Criteria: 48 MIRC Chapter 1, Income Tax Act of 1989, Section 110, states that every business shall on or before the last day of the following the close of each quarter, pay the amount of tax imposed on gross revenues under Section 109 of the Chapter.

Condition: MEC filed and paid gross revenue taxes for the year ended September 30, 2020 in a manner inconsistent with the criteria. In addition, gross revenue taxes from previous years in the amount of \$1,670,835 have not been paid.

Cause: The cause of the above condition is the lack of policies and procedures to monitor timely payment of gross revenue taxes.

Effect: The effect of the above condition is noncompliance with RepMar Income Tax Act of 1989, as amended.

Recommendation: We recommend management establish policies and procedures to comply with the RepMar Income Tax Act of 1989, as amended.

Prior Year Status: Recommendation concerning management to establish policies and procedures pertaining to compliance with the RepMar Income Tax Act of 1989, as amended, was reported as a finding in the audit of MEC for fiscal years 2016 through 2019.

Auditee Response and Corrective Action Plan: MEC understands this noncompliance. The reason for the nonpayment of taxes is an effort to address increasing accounts receivable balance of an SOE, which amounted to \$6.1 million as of September 30, 2020, via an offsetting exercise to reduce each party's liabilities. An exercise of this nature is not unprecedented. It previously resulted in an offset of \$2.3 million for outstanding obligations and accounts receivable between the GRMI, MEC, and MIR.

MEC is greatly concerned with the financial burden KAJUR continues to impose as a result of its inability to meet its annual fuel bill obligation and is trying all possible avenues to have the outstanding balance addressed.

**MARSHALLS ENERGY COMPANY, INC.
(A Component Unit of the Republic of the Marshall Islands)**

Unresolved Prior Year Findings
Year Ended September 30, 2020

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