**MARSHALL ISLANDS SHIPPING CORPORATION**

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

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**FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT**

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**YEARS ENDED SEPTEMBER 30, 2021 AND 2020**

**MARSHALL ISLANDS SHIPPING CORPORATION**
**(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)**

Years Ended September 30, 2021 and 2020
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# INDEPENDENT AUDITOR'S REPORT

Board of Directors
Marshall Islands Shipping Corporation:

## Report on the Financial Statements

We have audited the accompanying financial statements of Marshall Islands Shipping Corporation (MISC), a component unit of the Republic of the Marshall Islands (RepMar), which comprise the statements of net position as of September 30, 2021 and 2020, 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.

### *Auditor's 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 MISC as of September 30, 2021 and 2020, 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.

Deloitte.

### ***Emphasis of Matters***

*Going Concern*

The accompanying financial statements have been prepared assuming that MISC will continue as a going concern. As discussed in Note 7 to the financial statements, MISC's recurring losses from operations raise substantial doubt about its ability to continue as a going concern. Management's plans concerning this matter are also discussed in Note 7 to the financial statements. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

*COVID-19*

As discussed in Note 8 to the financial statements, MISC determined that the COVID-19 pandemic may negatively impact its business, results of operations and net position.

Our opinion is not modified with respect to these matters.

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

## **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 29, 2022, on our consideration of MISC'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 MISC'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 MISC's internal control over financial reporting and compliance.

Deloitte & Touche LLP

December 29, 2022

Marshall Islands Shipping Corporation (MISC) herewith presents a management's discussion and analysis of the company's financial performance for the financial year ended 30th September 2021. It is to be read in conjunction with the financial statements following this section.

## FINANCIAL HIGHLIGHTS

MISC's net position at the end of the fiscal year 2021 increased by $560,774 (or 6.8%) to $8,812,938 in 2021 compared to a net position of $8,252,164 in 2020. The increase in net position from 2020 to 2021 of $560,774 is a positive indicator of the results of operations, and ongoing efforts by management to maintain expenses within operational revenues as well as nonoperational revenues in the form of RMI government subsidies. In addition, MISC was the recipient of RMI government capital contributions representing contributions for the purchase of new ships of $1,363,632 for MV Ribuuk Meto in 2020/2021 and $450,000 for SV Kwai in 2021.

MISC's total net operating revenues increased by $104,153 (or 9.8%) from $1,059,105 in 2020 to $1,163,258 in 2021. The increase in revenues from cargo, ship sales and passengers, offset by the decrease in revenues from charter, copra fee and other revenues such as fuel delivery revenue, was driven by two factors. The increase in cargo, ship sales and passenger revenues correspond to the increase in frequency of field trips from 22 field trips in 2020 to 29 field trips in 2021. The decrease in charter revenues was due to extraordinary circumstances in the form of the Dengue Fever outbreak in 2019 and 2020.

MISC's total operating expenses decreased by $715,793 (or 15.9%) from $4,488,371 in 2020 to $3,772,578 in 2021. MISC's leading operational expenses in 2021 were salaries, wages and benefits expense; depreciation expense; petroleum, oil and lube expense; materials and supplies expense; and cost of goods sold expense. Salaries, wages and benefits expense increased by $149,211 (or 9.9%) from $1,508,326 in 2020 to $1,657,537 in 2021. Depreciation expense increased by $27,721 (or 4.7%) from $593,673 in 2020 to $621,394 in 2021. Petroleum, oil and lube expense decreased by $35,530 (or 8%) from $442,042 in 2020 to $406,512 in 2021. Materials and supplies expense increased by $122,559 (or 77.1%) from $159,060 in 2020 to $281,619 in 2021. Cost of goods sold expense increased by $17,085 (or 13.3%) from $128,860 in 2020 to $145,945 in 2021.

MISC's operating loss decreased by $819,946 (or 23.9%) from $3,429,266 in 2020 to $2,609,320 in 2021. MISC's operating losses were funded by cash subsidies from RepMar. In line with MISC's operating losses, operating subsidies received from RepMar decreased by $533,251 (or 22.7%) from $2,348,075 in 2020 to $1,814,824 in 2021.

In addition to operating subsidies, MISC received capital subsidies to assist MISC with capital asset acquisitions. Capital subsidies received from RepMar decreased by $174,058 (or 17.5%) from $993,845 in 2020 to $819,787 in 2021. The capital subsidy received in 2021 from RepMar assisted MISC with the acquisition of MV Ribuuk Meto ($369,787) and SV Kwai ($450,000) whilst the amount received in 2020 assisted MISC with the acquisition of MV Ribuuk Meto.

MISC's change in net position increased by $656,520 (or 686%) from -$95,746 in 2020 to $560,774 in 2021. One of the drivers associated with this positive change was the $588,069 gain on forgiveness of debt between MISC and Tobolar Copra Processing Authority (TCPA). MISC and TCPA entered into an agreement whereby amounts associated with the sale and transfer of MV Tobolar from TCPA to MISC were forgiven.

Without the approval of RepMar to allow management of MISC to increase tariffs, it is expected that MISC will always operate at a loss and MISC's future sustainability will continue to be a burden on RepMar as a community service obligation.

## FINANCIAL ANALYSIS OF MISC

The Statements of Net Position and the Statements of Revenues, Expenses and Changes in Net Position provide an indication of MISC's financial condition. MISC'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, MISC's net position increased for the year ended 30th September 2021. A summary of MISC's Statements of Net Position is presented below:

**Summary Statements of Net Position**
As of September 30

| | 2021 | 2020 | $ Change 2021-2020 | % Change 2021-2020 | 2019 |
|---|---|---|---|---|---|
| Assets: | | | | | |
| Current and other assets | $ 658,232 | $ 602,837 | $ 55,395 | 9.2% | $ 1,324,989 |
| Capital assets | 8,774,440 | 8,652,543 | 121,897 | 1.4% | 8,321,050 |
| Total assets | 9,432,672 | 9,255,380 | 177,292 | 1.9% | 9,646,039 |
| Liabilities: | | | | | |
| Current and other liabilities | 619,734 | 1,003,216 | (383,482) | (38.2)% | 1,298,129 |
| Net position: | | | | | |
| Net investment in capital assets | 8,774,440 | 8,652,543 | 121,897 | 1.4% | 8,037,550 |
| Restricted | 283,626 | 195,388 | 88,238 | 45.2% | 377,708 |
| Unrestricted | (245,128) | (595,767) | 350,639 | (58.9)% | (67,348) |
| Total net position | $ 8,812,938 | $ 8,252,164 | $ 560,774 | 6.8% | $ 8,347,910 |

Total assets increased by $177,292 (or 1.9%) from $9,255,380 in 2020 to $9,432,672 in 2021. The increase was due to an increase in capital assets, net of accumulated depreciation, of $121,897 (or 1.4%) and an increase in current and other assets of $55,395 (or 9.2%). The increase in capital assets was due to acquisitions of $779,135 offset by net disposals of $35,844 and depreciation of $621,394. Capital asset acquisitions included a final payment of $369,787 for MV Ribuuk Meto and a one-time payment of $300,000 for the acquisition of SV Kwai, which were both delivered and placed into service in 2021. The increase in current and other assets was due to an increase in cash balances and net receivables of $110,891 (or 84%) and $14,549 (or 6%), respectively, offset by a decrease in inventory and prepaid drydock expense of $70,045 (or 33%).

Total liabilities decreased by $383,482 (or 38.2%) from $1,003,216 in 2020 to $619,734 in 2021. The decrease in liabilities was primarily driven by the reduction in MISC's obligations due to RepMar's related parties, including TCPA. Payables to affiliates decreased by $474,049 (or 62%) from $768,254 in 2020 to $293,205 in 2021 primarily as a result in a reduction of liabilities due to TCPA. MISC entered into an agreement with TCPA that resulted in the write-off of MISC's payable to TCPA of $588,069 and the recognition in 2021 of a gain on forgiveness of debt.

Total net position increased by $560,774 (or 6.8%) from $8,252,164 in 2020 to $8,812,938 in 2021. The increase was due primarily to the recognition of the $588,069 gain on forgiveness of debt, as discussed above. In 2021, MISC incurred a loss from operations of $2,609,320, which was principally funded by contributions received from RepMar of $1,814,824. In comparison, MISC incurred a loss from operations of $3,429,266 in 2020, which was principally funded by RepMar contributions of $2,348,075.

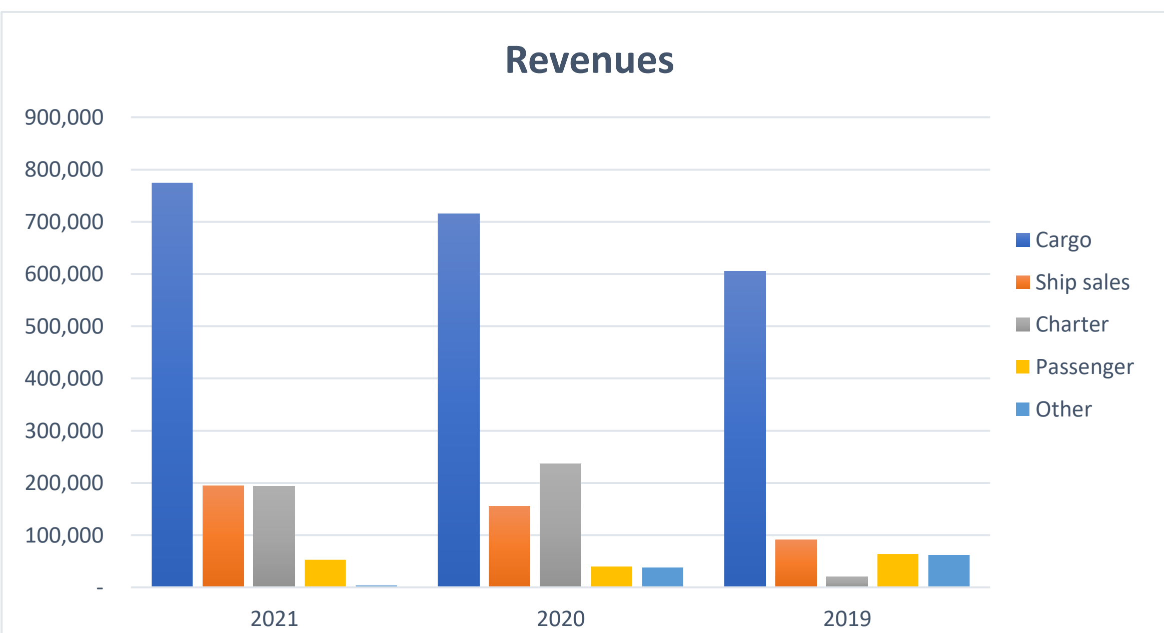
## FINANCIAL ANALYSIS OF MISC, CONTINUED

A summary of MISC'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

| | 2021 | 2020 | $ Change 2021-2020 | % Change 2021-2020 | 2019 |
|---|---|---|---|---|---|
| Operating: | | | | | |
| Operating revenues | $ 1,163,258 | $ 1,059,105 | $ 104,153 | 9.8% | $ 767,992 |
| Operating expenses | 3,772,578 | 4,488,371 | (715,793) | (15.9)% | 3,699,880 |
| Operating loss | (2,609,320) | (3,429,266) | 819,946 | (23.9)% | (2,931,888) |
| Nonoperating: | | | | | |
| Nonoperating revenues | 2,402,893 | 2,348,075 | 54,818 | 2.3% | 2,033,600 |
| Nonoperating expenses | (52,586) | (8,400) | (44,186) | 526.0% | (20,344) |
| | 2,350,307 | 2,339,675 | 10,632 | 0.5% | 2,013,256 |
| Capital contributions | 819,787 | 993,845 | (174,058) | (17.5)% | 724,400 |
| Change in net position | $ 560,774 | $ (95,746) | $ 656,520 | (685.7)% | $ (194,232) |

The Statements of Revenues, Expenses and Changes in Net Position identify the various revenue and expense items that contributed to the change in net position. MISC's total net operating revenues increased by $104,153 (or 9.8%) to a total of $1,163,258 in 2021 compared to $1,059,105 in 2020. In 2020, net operating revenues increased by $291,113 (or 38%) to a total of $1,059,105 from $767,992 in 2019. With the issuance by RepMar of "State of Health Emergency due to Dengue Fever Outbreak" on August 6, 2019 and "State of Health Emergency due to COVID-19 Pandemic" on February 7, 2020, relief efforts for outer island outreach activities to deliver relief goods, food baskets, and RMI government charter trip schedules resulted in the increase in MISC cargo and charter revenues. The graph below presents the major components of MISC's operating revenues from 2019 through 2021:



## FINANCIAL ANALYSIS OF MISC, CONTINUED

Total operating expenses decreased by $715,793 (or 15.9%) from $4,488,371 in 2020 to $3,772,578 in 2021. For 2021, the top five components of operating expenses were: (1) Salaries, Wages and Benefits, (2) Depreciation (3) Petroleum, Oil and Lube (POL), (4) Material and supplies, and (5) Cost of goods sold. The graph below presents the major components of MISC's operating expenses from 2019 through 2021:


Salaries, wages and benefits remain as the leading operational expense and increased by $149,211 (or 9.9%) from $1,508,326 in 2020 to $1,657,537 in 2021. Increase in salaries, wages and benefits is due to new hires and recruitment of employees for the new vessels SV Kwai and MV Ribuuk Meto, which entered into service in January 2021 and February 2021, respectively, and salary increases for certain employees.

Depreciation expense increased marginally by $27,721 (or 4.7%) from $593,673 in 2020 to $621,394 in 2021. This marginal increase is the result of the new vessel acquisitions offset by the write-off of certain assets associated with MV Tobolar.

POL expenses decreased by $35,530 (or 8%) from $442,042 in 2020 to $406,512 in 2021. In 2020, MISC received delivery of the new vessel MV Enen Kio, which incurred a $49,000 fuel cost from China where the ship was constructed. Excluding this 2020 cost, POL expense increased in 2021, which corresponds with the increase in frequency of field trips from 22 field trips in 2020 to 29 field trips in 2021.

Materials and supplies expense increased by $122,559 (or 77%) from $159,060 in 2020 to $281,619 in 2021 is due primarily to ancillary costs incurred in 2021 by Japan Marine Engineering Co. associated with the preparation and delivery of the new vessel MV Ribuuk Meto.

Ship sales services provide MISC an alternative source of income to subsidize operations. The increase in COGS by $17,085 (or 13.3%) from $128,860 in 2020 to $145,945 in 2021 corresponds with the increase in ship sales to customers from the outer islands during field trips.

## FINANCIAL ANALYSIS OF MISC, CONTINUED

With the establishment of the Shipping Vessel Repairs and Maintenance Act in 2011, an annual subsidy is granted by RepMar for proper and timely dry docking, repairs and maintenance to be undertaken by MISC. This is to ensure the good and operable conditions of MISC's fleet and for the safety and reliability of sea transportation services for the RMI outer island community. Drydock expense decreased by $187,814 (or 62.2%) from $302,092 in 2020 to $114,278 in 2021, with no drydocking activities taking place in 2020 or 2021 due to the lack of drydock funding being made available by the RepMar government.

The operating loss before nonoperating revenues (i.e., RepMar subsidy) decreased by $819,946 (or 23.9%) from $3,429,266 in 2020 to $2,609,320 in 2021. In 2020, although with control and the reduction of some expense categories, the operating loss was $3,429,266, which included impairment loss for two (2) ships - MV Ribuuk Ae and MV Tobolar, inclusive of the unamortized prepaid drydock costs, and depreciation of a new ship - MV Enen Kio.

Total subsidies for operations were $1,814,824 in 2021 compared to $2,348,075 in 2020. In 2018 and 2019, MISC was the recipient of subsidies associated with the Shipping Vessel Repairs and Maintenance Act, but MISC did not receive such in 2020 and 2021. The subsidy to support the Shipping Vessel Repairs and Maintenance Act fluctuates annually based on the repairs and maintenance schedule and costing developed with the technical assistance of the Japan International Cooperation Agency (JICA) and has taken into account major repairs that will need to be completed and the inclusion of two additional vessels to the MISC fleet.

As noted above, the operating subsidy received from RepMar in 2021 decreased by $532,451 (or 22.7%) from $2,348,075 in 2020 to $1,814,824 in 2021, with no drydock subsidy being received in 2020 or 2021. In addition, MISC received a capital subsidy of $819,787 in 2021, a decrease of $174,058 (or 17.5%) from $993,845 received in 2020. The amount received in 2021 represented contributions received from RepMar associated with the acquisition of MV Ribuuk Meto ($369,787) and SV Kwai ($450,000) whilst the amount received in 2020 represented contributions received from RepMar associated with the acquisition of MV Ribuuk Meto. With current fare rates unchanged since 1980 and no available landing craft for charter, MISC is not able to achieve full cost recovery to cover operational costs and maintain adequate major and ongoing repairs and maintenance without financial support from RepMar. The future financial sustainability and conditions of the MISC fleet will continue to depend on sufficient financial support from RepMar.

Management's Discussion and Analysis for the year ended September 30, 2020 is set forth in MISC's report on the audit of financial statements, which is dated October 27, 2021. That Management's Discussion and Analysis explains the major factors impacting 2020 financial statements and can be obtained from MISC's General Manager via the contact information below.

## CAPITAL ASSETS AND DEBT

Net capital assets increased by $121,897 (or 1.4%) from $8,652,543 in 2020 to $8,774,440 in 2021. Capital asset acquisitions in 2021 of $779,135 were offset by depreciation of $621,394.

During the year ended September 30, 2021, the new vessel MV Ribuuk Meto, previously under construction, was completed and delivered at a cost of $1,339,787. In addition, MISC acquired the refitted SV Kwai at a cost of $300,000.

## CAPITAL ASSETS AND DEBT, CONTINUED

A summary of MISC's capital assets as of September 30, 2021 compared with 2020 and 2019 is presented below:

**Summary Schedule of Capital Assets**
As of September 30

| | 2021 | 2020 | $ Change 2021-2020 | % Change 2021-2020 | 2019 |
|---|---|---|---|---|---|
| Vessels | $ 9,878,861 | $ 8,239,074 | $ 1,639,787 | 19.9% | $ 6,792,253 |
| Vehicles | 508,870 | 502,870 | 6,000 | 1.2% | 457,070 |
| Equipment | 345,128 | 397,586 | (52,458) | (13.2)% | 387,023 |
| Motor boats | 223,474 | 223,924 | (450) | (0.2)% | 221,229 |
| | 10,956,333 | 9,363,454 | 1,592,879 | 17.0% | 7,857,575 |
| Accumulated depreciation | (2,181,893) | (1,680,911) | (500,982) | 29.8% | (1,437,025) |
| | 8,774,440 | 7,682,543 | 1,091,897 | 14.2% | 6,420,550 |
| Vessels under construction | - | 970,000 | (970,000) | (100.0)% | 1,900,500 |
| | $ 8,774,440 | $ 8,652,543 | $ 121,897 | 1.4% | $ 8,321,050 |

Refer to Note 4 of the accompanying financial statements for additional information relating to MISC's capital assets.

In 2021, MISC received a $450,000 loan from the Marshall Islands Development Bank (MIDB) to assist with the SV Kwai acquisition. The loan was subsequently paid by RepMar in 2021 on behalf of MISC. As of September 30, 2021, MISC has no other long-term debt.

## CASH FLOWS

Net cash used for operating activities for 2021 was $1,727,843 compared to net cash used for operating activities of $1,683,332 in 2020. The cash provided by operational activities was absorbed entirely by MISC's operational costs. Additionally, cash flow injections from RepMar to subsidize MISC's operations were received in the amount of $1,814,824 and $2,324,230 during 2021 and 2020, respectively. No subsidies for vessel repairs and maintenance were received in 2021 and 2020. The repair and maintenance subsidy amounts are determined by a schedule developed in January 2011 under the JICA Preparatory Study for the "Project for Improvement of Domestic Shipping Services in the Marshall Islands". Finally, MISC received capital subsidies from RepMar in the amount of $369,787 and $839,020 in 2021 and 2020, respectively, which were used for the acquisition of MV Ribuuk Meto. In addition, MISC was the beneficiary of a $450,000 capital subsidy in 2021 whereby RepMar paid a loan on behalf of MISC from MIDB.

## FUTURE OUTLOOK ON SUSTAINABILITY

MISC plays an important role in the lives of people living in the outer islands. The regular field trip services are essential to transfer people and basic goods from the capital city to the outer islands and vice versa. As an indicator of MISC's future outlook on sustainability, MISC's has continued to improve and increase net position since 2012. In 2021, MISC's net position increased by $560,774 from $8,252,164 in 2020 to $8,812,938 in 2021. This is in comparison to the marginal decrease in MISC's net in 2020 of $95,746 from $8,347,910 in 2019 to $8,252,164 in 2020. Prior to that, MISC's net position increased to $8,542,142 in 2018, $1,437,797 in 2017, $401,081 in 2016, $279,970 in 2015, and $224,931 in 2014. The vast improvement in MISC's financial position from a net deficiency in 2012 to an increasing net position in 2014 - 2021 is a result of increases in revenue streams stemming from increases in charter trips in response to the ongoing relief efforts of the State of Drought Disaster originally issued in June - July 2013, 2016 climate change such as El Nino, 2017 climate change of heavy wave storm, along with the increases in field trips with the addition of the two shipping vessels donated by the Government of Japan, and the COVID-19 pandemic in 2020 and 2021.

## FUTURE OUTLOOK ON SUSTAINABILITY, CONTINUED

In addition to subsidies received from RepMar, the three vessels (MV Ribuuk Ae, MV Aemman, and MV Kwajelein) were formally transferred with net book values (NBV) of $6,432,862 in 2018. In February 2019, TCPA transferred MV Tobolar and other capital assets with NBV of $130,944. In 2020 and 2021, capital subsidies were received from RepMar for purchase of two vessels (MV Ribuuk Meto and SV Kwai). It is unfortunate that MV Ribuuk Ae sank in 2020 and MV Tobolar was decommissioned in 2021.

MISC's improved trend in net position overall provides an indicator of MISC management's efforts to reduce recurrent expenses. However, at the current passenger rate structure and limitation on vessel numbers/fleet size capacity, MISC will continue to have operational losses and rely on RepMar subsidies to minimize operational losses. In order to revive the MISC operations for future sustainability, MISC must be able to obtain RepMar approval to increase passenger tariff rates or continue to rely on a steady flow of subsidy amounts as a community service obligation to absorb operational losses of MISC to provide affordable sea-transport services to the people.

Historically, operating revenues generated by MISC have never been sufficient to cover the related expenses necessary to operate the shipping vessels and provide sea-transportation services. With operating losses over $1.2M to $3.4M annually, MISC continues to be dependent on financial support from RepMar. Most importantly, MISC is not able to generate sufficient revenues through operations due to the current passenger rate structure, which has been in place since the early 1980's, despite the increase in fuel costs and inflation rates. As a state-owned entity, MISC does not have the authority to increase tariff rates without the approval of RepMar. MISC made numerous requests to RepMar until such was approved on April 25, 2019 for a $10 increase in the freight rate or from $56.50 per ton to $66.50 per ton.

It is the intention of MISC to continue lobbying efforts for the authority and flexibility to increase tariff rates to account for the rising fuel costs and inflation rates. MISC's current strategic plan will expire in 2021; With tariff rates likely to remain at current levels, on-going financial support from RepMar will have to continue and may need to increase, as appropriate, to satisfy the community service obligation provided by MISC.

The future outlook on sustainability for MISC continues to be threatened by the deteriorating conditions of the shipping vessels. In 2011, RepMar passed the Shipping Vessel Repairs and Maintenance Act (R&M) to ensure that subsidy funding is made available on an annual basis to ensure that major repairs and services are performed regularly and for the procurement of safety equipment. The R&M Act provides a strong position for MISC to continue to advocate for and to receive subsidy for the sole purpose of repairs and maintenance needs of MISC's aging fleet. Without the R&M subsidy, the continued deteriorating conditions of more than half of MISC's fleet will have a negative impact on MISC's ability to provide safe and reliable shipping services. Furthermore, the operations of MISC are further hampered by the loss of MV Ribuuk Ae, which ran aground on Ujae Atoll in December 2019 and later sank in March 2020, followed by the decision to dispose of MV Tobolar in August 2020 and which was later decommissioned in April 2021.

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

- Approval from RepMar to increase MISC's tariff rate structure towards full cost recovery;
- Ongoing recipient of RepMar subsidy to support both MISC operations and the Shipping Vessel Repairs and Maintenance Act and New Ships;
- Develop and adhere to an ongoing annual repairs and maintenance schedules;
- Increase the number of vessels in MISC's fleet;
- Explore other grant financing opportunities (i.e., ADB, World Bank, RUS, etc.);

**FUTURE OUTLOOK ON SUSTAINABILITY, CONTINUED**

- Continue with budgetary controls to minimize operational expenses, where possible;
- Improve financial and operational management reporting and streamline processes:
- Capacity building opportunities for MISC personnel (administration and technical); and
- Implementation of community services obligations to comply with the SOE Act.

**MISC FOCUS IN THE COMING FISCAL YEAR**

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

- MISC, through the Board of Directors, will continue to lobby for the approval from Cabinet to increase MISC tariff rates, and to negotiate CSO agreements for identified commercial rates.
- With the support of MISC's Board of Directors, MISC will continue to implement and monitor activities laid out in the strategic plan addressing both the operational and financial goals of MISC. The strategic plans include:
  - Lobby and seek government and development partner opportunities to finance or co-finance procurement of additional shipping vessels to increase MISC's existing fleet;
  - Seek assistance from donor partners opportunities to finance or co-finance procurement of additional equipment or trucks to improve or streamline loading and unloading processes of the vessels to ensure quicker turn-around of the vessels and improve the efficiency of their transport services.
  - Develop a tariff rate template to incorporate rising costs and fluctuations of fuel prices and inflation rate;
  - Streamline operational processes (such as stevedoring, field trip scheduling, shipping vessel loading and unloading process to reduce downtime and turn ships around more frequently to increase services to the outer island);
  - Develop and improve management and financial reporting;
  - Address capacity building weaknesses and provide or seek opportunities for capacity building; and
  - Ensure adherence to the shipping repairs and maintenance schedule.

The Marshall Islands was not directly impacted by the COVID-19 pandemic being experienced elsewhere worldwide. No cases of COVID-19 were experienced in the Marshall Islands in 2021 and, as such, MISC was able to continue operations as usual subject to the continued support from RepMar. However, subsequent to year end, community transmission occurred in August 2022 that temporarily disrupted operations resulting in delays in MISC's field trip operations. MISC relied even further on RepMar support over that two-week period with continued reliance on RepMar for operational subsidies.

**ADDITIONAL FINANCIAL INFORMATION**

This discussion and analysis are designed to provide MISC's customers and other stakeholders with an overview of the Company's operations and financial condition as at 30$^{th}$ September 2021. Should the reader have questions regarding the information included in this report, or wish to request additional financial information, please contact the Marshall Islands Shipping Corporation General Manager at P.O. Box 1198, Majuro, Marshall Islands, MH 96960.

**MARSHALL ISLANDS SHIPPING CORPORATION**

Statements of Net Position
September 30, 2021 and 2020

| | 2021 | 2020 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash | $ 243,607 | $ 132,716 |
| Receivables: | | |
| Trade | 203,917 | 137,265 |
| Affiliates | 688,402 | 700,496 |
| Employees | 241,673 | 224,728 |
| | 1,133,992 | 1,062,489 |
| Less allowance for doubtful accounts | (863,922) | (806,968) |
| Total receivables, net | 270,070 | 255,521 |
| Inventory | 60,000 | 15,767 |
| Current portion of prepaid drydocking | 84,555 | 114,278 |
| Total current assets | 658,232 | 518,282 |
| Noncurrent assets: | | |
| Prepaid drydocking, net of current portion | - | 84,555 |
| Capital assets: | | |
| Nondepreciable capital assets | - | 970,000 |
| Capital assets, net of accumulated depreciation | 8,774,440 | 7,682,543 |
| Total noncurrent assets | 8,774,440 | 8,737,098 |
| | $ 9,432,672 | $ 9,255,380 |
| LIABILITIES AND NET POSITION | | |
| Current liabilities: | | |
| Accounts payable | $ 148,150 | $ 81,448 |
| Payable to affiliates | 293,205 | 768,254 |
| Accruals and other liabilities | 161,348 | 136,483 |
| Unearned revenue | 17,031 | 17,031 |
| Total liabilities | 619,734 | 1,003,216 |
| Commitments and contingencies | | |
| Net position: | | |
| Net investment in capital assets | 8,774,440 | 8,652,543 |
| Restricted | 283,626 | 195,388 |
| Unrestricted | (245,128) | (595,767) |
| Total net position | 8,812,938 | 8,252,164 |
| | $ 9,432,672 | $ 9,255,380 |

See accompanying notes to financial statements.

**MARSHALL ISLANDS SHIPPING CORPORATION**

Statements of Revenues, Expenses and Changes in Net Position
Years Ended September 30, 2021 and 2020

| | 2021 | 2020 |
|---|---|---|
| Operating revenues: | | |
| Cargo | $ 774,495 | $ 715,538 |
| Ship sales | 194,773 | 155,267 |
| Charter | 194,041 | 237,000 |
| Passenger | 52,716 | 39,986 |
| Copra fee | - | 32,401 |
| Fuel and other revenue | 4,187 | 6,021 |
| Total operating revenues | 1,220,212 | 1,186,213 |
| Provision for bad debts | (56,954) | (127,108) |
| Net operating revenues | 1,163,258 | 1,059,105 |
| Operating expenses: | | |
| Salaries, wages and benefits | 1,657,537 | 1,508,326 |
| Depreciation | 621,394 | 593,673 |
| Petroleum, oil and lube | 406,512 | 442,042 |
| Material and supplies | 281,619 | 159,060 |
| Cost of goods sold | 145,945 | 128,860 |
| Foodstuffs | 118,512 | 98,053 |
| Drydock expense | 114,278 | 302,092 |
| Rent | 110,887 | 258,875 |
| Professional fees | 82,315 | 48,741 |
| Travel and entertainment | 81,749 | 46,573 |
| Sitting fees | 57,700 | 63,405 |
| Communications | 23,956 | 24,766 |
| Freight | 19,918 | 3,804 |
| Utilities | 19,281 | 31,255 |
| Insurance | 16,677 | 2,199 |
| Contributions | 7,299 | 6,279 |
| Impairment loss | - | 744,228 |
| Stevedoring | - | 19,638 |
| Miscellaneous | 6,999 | 6,502 |
| Total operating expenses | 3,772,578 | 4,488,371 |
| Operating loss | (2,609,320) | (3,429,266) |
| Nonoperating revenues (expenses): | | |
| Operating subsidies | 1,814,824 | 2,348,075 |
| Gain on forgiveness of debt | 588,069 | - |
| Penalties and interest | (16,742) | - |
| Loss on disposal of capital assets | (35,844) | (8,400) |
| Total nonoperating revenues (expenses), net | 2,350,307 | 2,339,675 |
| Loss before capital contributions | (259,013) | (1,089,591) |
| Capital contributions | 819,787 | 993,845 |
| Change in net position | 560,774 | (95,746) |
| Net position at beginning of year | 8,252,164 | 8,347,910 |
| Net position at end of year | $ 8,812,938 | $ 8,252,164 |

See accompanying notes to financial statements.

**MARSHALL ISLANDS SHIPPING CORPORATION**

Statements of Cash Flows
Years Ended September 30, 2021 and 2020

| | 2021 | 2020 |
|---|---|---|
| Cash flows from operating activities: | | |
| Cash received from customers | $ 1,148,709 | $ 1,181,205 |
| Cash payments to suppliers for goods and services | (1,243,880) | (1,355,327) |
| Cash payments to employees for services | (1,632,672) | (1,509,210) |
| Net cash used for operating activities | (1,727,843) | (1,683,332) |
| Cash flows from noncapital financing activities: | | |
| Operating subsidies received | 1,814,824 | 2,324,230 |
| Cash flows from capital and related financing activities: | | |
| Capital contributions received | 369,787 | 839,020 |
| Proceeds from MIDB loan | 450,000 | - |
| Interest paid | (16,742) | - |
| Acquisition of capital assets | (779,135) | (1,655,407) |
| Net cash cash provided by (used for) capital and related financing activities | 23,910 | (816,387) |
| Net change in cash | 110,891 | (175,489) |
| Cash at beginning of year | 132,716 | 308,205 |
| Cash at end of year | $ 243,607 | $ 132,716 |
| Reconciliation of operating loss to net cash used for operating activities: | | |
| Operating loss | $ (2,609,320) | $ (3,429,266) |
| Adjustments to reconcile operating loss to net cash used for operating activities: | | |
| Impairment loss | - | 744,228 |
| Depreciation | 621,394 | 593,673 |
| Drydock | 114,278 | 302,092 |
| Provision for bad debts | 56,954 | 127,108 |
| (Increase) decrease in assets: | | |
| Receivables: | | |
| Affiliates | 12,094 | 11,896 |
| Trade | (66,652) | (52,942) |
| Employees | (16,945) | 43,007 |
| Inventory | (44,233) | (11,715) |
| Increase (decrease) in liabilities: | | |
| Accounts payable | 66,702 | 21,589 |
| Payable to affiliates | 113,020 | (25,143) |
| Accruals and other liabilities | 24,865 | (890) |
| Unearned revenue | - | (6,969) |
| Net cash used for operating activities | $ (1,727,843) | $ (1,683,332) |
| Summary disclosure of noncash capital and related financing activities: | | |
| Repayment of MIDB loan by RepMar: | | |
| Capital contributions | $ 450,000 | $ - |
| Repayment of long-term debt | (450,000) | - |
| | $ - | $ - |
| Impairment of MV Ribuuk Ae and MV Tobolar: | | |
| Prepaid drydocking | $ - | $ 305,887 |
| Capital assets | - | 778,824 |
| Accumulated depreciation | - | (340,483) |
| Impairment loss | - | (744,228) |
| | $ - | $ - |

See accompanying notes to financial statements.

## (1) Organization

Marshall Islands Shipping Corporation (MISC), a component unit of the Republic of the Marshall Islands (RepMar), was created under Public Law 2005-41, the Marshall Islands Shipping Corporation Act, 2004. MISC was established to manage and operate RepMar's shipping vessels including the MV Aemman, the MV Enen Kio, the MV Kwajalein, the MV Ribuuk Ae, the MV Ribuuk Meto, the MV Tobolar, and the SV Kwai. In 2020, the MV Ribuuk Ae and the MV Tobolar were decommissioned and taken out of service. MISC's principal line of business is to provide sea transportation services; to carry on business as ship owners; and to build and maintain ships and vessels.

MISC is governed by an eight-member Board of Directors appointed by the Cabinet of RepMar.

MISC's financial statements are incorporated into the financial statements of RepMar as a component unit.

## (2) Summary of Significant Accounting Policies

The accounting policies of MISC conform to accounting principles generally accepted in the United States of America (GAAP), as applicable to governmental entities, specifically proprietary funds. The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for establishing governmental accounting and financial reporting principles.

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.

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: net position whose use by MISC is subject to externally imposed stipulations that can be fulfilled by actions of MISC pursuant to those stipulations or that expire with the passage of time. As of September 30, 2021 and 2020, MISC has restricted net position for unexpended contributions from RepMar as follows:

| | 2021 | 2020 |
|---|---|---|
| Repairs and maintenance | $ 158,000 | $ 158,000 |
| Vessel delivery | 125,626 | 37,388 |
| | $ 283,626 | $ 195,388 |

- 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 MISC's policy to use unrestricted resources first, then restricted resources as they are needed.

(2) Summary of Significant Accounting Policies, Continued

Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and 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

MISC's revenues are derived primarily from the operation of shipping vessels. Capital grants, financing or investing related transactions are reported as non-operating revenues. Revenue is recognized on the accrual basis and is recorded upon billing when services have been completed. Specifically, cargo, charter and passenger revenue are recognized when the transportation is provided. Other components of other operating revenue are recognized as revenue when the related goods and services are provided. All expenses related to operating MISC are reported as operating expenses. Interest income or federal program revenues are the primary components of non-operating expenses and revenues.

Cash

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

For purposes of the statements of net position and cash flows, cash is defined as cash on hand and cash held in demand accounts. As of September 30, 2021 and 2020, the carrying amount of cash was $243,607 and $132,716, respectively, and the corresponding bank balances were $271,723 and $154,821, respectively. Of the bank balance amounts, $215,244 and $108,827, respectively, were maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance with the remaining amounts of $56,479 and $45,994, respectively, being maintained in a financial institution not subject to depository insurance. As of September 30, 2021 and 2020, bank deposits in the amount of $215,244 and $108,827, respectively, were FDIC insured. MISC does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

Receivables

All receivables are uncollateralized and are due from affiliates or customers, located within the Republic of the Marshall Islands. The allowance for 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.

(2) Summary of Significant Accounting Policies, Continued

Inventory

Inventory consists of items purchased for resale (on the ships) during outer islands voyages. Inventory is valued at the lower of cost (moving average) or market value (net realized value).

Deferred Dry-dock Expenditures

Dry dock expenditures have been recognized as an asset when the recognition criteria were met. The recognition is made when the dry docking has been performed and is amortized over the period until the next scheduled dry docking, usually two to three years. Any remaining carrying amount of the cost of the previous inspection is derecognized. Ordinary repairs and maintenance expenses are charged to the income statement during the financial period in which they are incurred.

Equipment

MISC has not adopted a formal capitalization policy for equipment; however, items with a cost that equals or exceeds $1,000 and have an estimated life of more than one year are generally capitalized. Such assets are stated at cost. Depreciation is calculated on the straight-line method based on the estimated useful lives of the respective assets. The estimated useful lives of these assets are as follows:

| | |
|---|---|
| Equipment | 5 - 10 years |
| Vehicles | 5 years |
| Vessels | 25 years |
| Motor boats | 5 years |

Deferred Outflows of Resources

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

Deferred Inflows of Resources

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

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits. As of September 30, 2021 and 2020, the accumulated vacation leave liability totals $96,321 and $86,866, respectively, and is included within the statements of net position as accruals and other liabilities.

Unearned Revenue

Unearned revenue represents cash received in advance for revenue to be earned in a future period.

(2) Summary of Significant Accounting Policies, Continued

Taxes

Corporate profits are not subject to income tax in the Republic of the Marshall Islands. The Government of the Republic of the Marshall Islands imposes a gross receipts tax of 3% on revenues. MISC is specifically exempt from this tax.

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 Statements 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.

During the year ended September 30, 2021, MISC implemented the following pronouncements:

- GASB Statement No. 84, *Fiduciary Activities*, which improves guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported.
- GASB Statement No. 90, *Majority Equity Interests – An Amendment of GASB Statements No. 14 and 61*, which improves 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.
- GASB Statement No. 93, *Replacement of Interbank Offered Rates*, which establishes accounting and reporting requirements related to the replacement of Interbank Offered Rates such as the London Interbank Offered Rate (LIBOR) for hedging derivative instruments. The provision removing LIBOR as an appropriate benchmark interest rate for the evaluation of the effectiveness of derivative instruments is effective for the year ending September 30, 2022.

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

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 the 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 the fiscal year ending September 30, 2022.

(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 the 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. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. 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 are effective for the fiscal year ending 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 the 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 the fiscal year ending September 30, 2023.

(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. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 97 will be effective for the 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 disclosures 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) Prepaid Drydocking

In 2019, MISC incurred dry-dock costs of $338,220 for MV Aemman in Fiji, which is to be amortized over 3 years. Furthermore, Tobolar Copra Processing Authority (TCPA) transferred dry-dock costs of $457,125 relating to the transfer of MV Tobolar. During the year ended September 30, 2020, MV Ribuuk Ae sank resulting in related prepaid dry-dock costs of $106,816 being written off. In addition, MV Tobolar was considered impaired resulting in related prepaid dry-dock costs of $199,071 being written off. As of September 30, 2021 and 2020, prepaid dry-dock costs amounted to $84,555 and $198,833, respectively.

An analysis of the change in prepaid dry-dock costs during the years ended September 30, 2021 and 2020 is as follows:

| | 2021 | 2020 |
|---|---|---|
| Beginning balance | $ 198,833 | $ 806,812 |
| Drydock costs written off | - | (305,887) |
| Amortized drydock expense | (114,278) | (302,092) |
| Ending balance | $ 84,555 | $ 198,833 |
| Disclosed as follows: | | |
| Current | $ 84,555 | $ 114,278 |
| Noncurrent | - | 84,555 |
| | $ 84,555 | $ 198,833 |

## (4) Capital Assets

Capital asset activity for the years ended September 30, 2021 and 2020 is as follows:

| | 2021 | | | | |
|---|---|---|---|---|---|
| | October 1, 2020 | Additions | Transfers | Disposals/ Impairment/ Reclassifications | September 30, 2021 |
| Equipment | $ 397,586 | $ 66,848 | $ - | $ (119,306) | $ 345,128 |
| Vehicles | 502,870 | 30,000 | - | (24,000) | 508,870 |
| Vessels | 8,239,074 | 300,000 | 1,339,787 | - | 9,878,861 |
| Motor boats | 223,924 | 12,500 | - | (12,950) | 223,474 |
| | 9,363,454 | 409,348 | 1,339,787 | (156,256) | 10,956,333 |
| Less accumulated depreciation | (1,680,911) | (621,394) | - | 120,412 | (2,181,893) |
| | 7,682,543 | (212,046) | 1,339,787 | (35,844) | 8,774,440 |
| Vessels under construction | 970,000 | 369,787 | (1,339,787) | - | - |
| | $ 8,652,543 | $ 157,741 | $ - | $ (35,844) | $ 8,774,440 |

| | 2020 | | | | |
|---|---|---|---|---|---|
| | October 1, 2019 | Additions | Transfers | Disposals/ Impairment/ Reclassifications | September 30, 2020 |
| Equipment | $ 387,023 | $ 61,600 | $ - | $ (51,037) | $ 397,586 |
| Vehicles | 457,070 | 49,500 | - | (3,700) | 502,870 |
| Vessels | 6,792,253 | 262,212 | 1,900,500 | (715,891) | 8,239,074 |
| Motor boats | 221,229 | 28,595 | - | (25,900) | 223,924 |
| | 7,857,575 | 401,907 | 1,900,500 | (796,528) | 9,363,454 |
| Less accumulated depreciation | (1,437,025) | (593,673) | - | 349,787 | (1,680,911) |
| | 6,420,550 | (191,766) | 1,900,500 | (446,741) | 7,682,543 |
| Vessels under construction | 1,900,500 | 970,000 | (1,900,500) | - | 970,000 |
| | $ 8,321,050 | $ 778,234 | $ - | $ (446,741) | $ 8,652,543 |

On December 28, 2019, MV Ribuuk Ae ran aground on Ujae Atoll. Subsequent recovery efforts failed resulting in the vessel sinking and the recognition of an impairment loss of $386,978 together with prepaid dry-dock costs of $106,816 being written off. On August 19, 2020, MISC determined that MV Tobolar was impaired resulting in the recognition of an impairment loss of $51,363 together with prepaid dry-dock costs of $199,071 being written off.

## (5) Related Party Transactions

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

A summary of related party transactions as of September 30, 2021 and 2020 and for the years then ended are as follows:

| | 2021 | | | |
|---|---|---|---|---|
| | Revenues | Expenses | Receivables | Payables |
| Tobolar Copra Processing Authority | $ 389,881 | $ - | $ 389,220 | $ - |
| Marshall Islands Social Security Administration | - | 297,256 | - | 85,876 |
| Marshalls Energy Company, Inc. | 1,099 | 101,144 | 84 | 62,516 |
| RMI Ports Authority | - | 46,526 | - | 98,046 |
| Republic of the Marshall Islands | 199,418 | 157,621 | 296,137 | 24,072 |
| Other | 2,425 | 84,084 | 2,961 | 22,695 |
| | $ 592,823 | $ 686,631 | $ 688,402 | $ 293,205 |

| | 2020 | | | |
|---|---|---|---|---|
| | Revenues | Expenses | Receivables | Payables |
| Tobolar Copra Processing Authority | $ 434,405 | $ - | $ 288,918 | $ 588,069 |
| Marshall Islands Social Security Administration | 2,314 | 291,519 | - | 72,972 |
| Marshalls Energy Company, Inc. | 39 | 352,598 | 3,585 | 6,989 |
| RMI Ports Authority | - | 50,237 | - | 89,462 |
| Republic of the Marshall Islands | 354,088 | 146,017 | 363,335 | 5,015 |
| Other | 106,523 | 67,153 | 44,658 | 5,747 |
| | $ 897,369 | $ 907,524 | $ 700,496 | $ 768,254 |

During the years ended September 30, 2021 and 2020, the operations of MISC were funded by appropriations from the Nitijela of RepMar of $1,814,824 and $2,348,075, respectively. As of September 30, 2020, $23,845 relating to operating subsidies is due from RepMar.

On December 2, 2020, the Board of Directors approved the acquisition of SV Kwai for $300,000. MISC financed the acquisition through a $450,000 loan from the Marshall Islands Development Bank. On April 28, 2021, the $450,000 loan was paid on behalf of MISC by RepMar and has been recognized by MISC as a capital contribution from RepMar.

During the years ended September 30, 2021 and 2020, the acquisition of certain vessels was funded by capital contributions from the Nitijela of RepMar of $369,787 and $993,845, respectively. As of September 30, 2020, $154,825 relating to capital contributions is due from RepMar.

In 2018, MISC entered into an agreement with the Ministry of Works, Infrastructure and Utilities (MWIU) whereby the MV Majuro vessel was transferred to MWIU. In return, MWIU agreed to operate the MV Majuro vessel and that any revenue generated by MWIU from MV Majuro in excess of $300,000 per annum would be remitted to MISC. During the years ended September 30, 2021 and 2020, MV Majuro revenues did not exceed the $300,000 threshold.

In 2018, the Cabinet of RepMar authorized and approved the transfer of MV Tobolar, with a net book value of $130,944, from TCPA to MISC. On February 28, 2019, the net book value of MV Tobolar amounting to $130,944 and related deferred dry-dock costs of $457,125 were transferred from TCPA to MISC resulting in a payable to TCPA of $588,069. On March 17, 2022, TCPA entered into an agreement with MISC to write-off the $588,069 payable. MISC has recognized this forgiveness of debt during the year ended September 30, 2021.

(5) Related Party Transactions, Continued

MISC occupies certain RepMar office space at no cost. No lease agreement has been executed to formalize this arrangement. However, management is of the opinion that no rental payment for the use of this property is anticipated. The fair value of this contribution is presently not determinable. Accordingly, the contributed facility use has not been recognized as revenue and expenses in the accompanying financial statements.

As described in note 7, MISC leases space from RMI Ports Authority.

(6) Risk Management

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

(7) Commitments and Contingencies

Commitments

MISC leased a warehouse for $2,557 per month, effective August 1, 2015, from the RMI Ports Authority, which lease expired on July 31, 2020. On August 1, 2020, the lease was renewed for an additional 5 year term, expiring on July 31, 2025 for $2,297 per month. During the years ended September 30, 2021 and 2020, MISC recorded associated rent expense of $27,558 and $30,158, respectively. Total minimum future rental payments for this non-cancelable lease agreement for the years ending September 30, are as follows:

| Year ending September 30, | |
|---|---|
| 2022 | $ 27,558 |
| 2023 | 27,558 |
| 2024 | 27,558 |
| 2025 | 22,965 |
| | $ 105,639 |

Going Concern

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 MISC as a going concern. During the years ended September 30, 2021 and 2020, MISC incurred losses from operations of $2,609,320 and $3,429,266, respectively. During the years ended September 30, 2021 and 2020, the operations of MISC were funded by appropriations from the Nitijela of RepMar of $1,814,824 and $2,348,075, respectively. In addition, during the years ended September 30, 2021 and 2020, MISC received $819,787 and $993,845, respectively, for the purpose of funding the acquisition of certain vessels. Management acknowledges that it is currently dependent on RepMar for cash funding in order to maintain MISC as a going concern. Although RepMar has provided funding in the past, MISC does not have a formal agreement with RepMar to provide future funding. Management believes that the continuation of MISC's operations is dependent upon the future financial support of RepMar, deferment of payment of certain liabilities, and/or significant improvements in operations.

## (7) Commitments and Contingencies, Continued

### Going Concern, Continued

In view of these matters, realization of the related assets in the accompanying statement of net position as of September 30, 2021, is dependent upon continued operations of MISC, which, in turn, is dependent upon MISC's ability to provide service to its customers and the success of future operations. Management believes that actions presently being undertaken to revise MISC's operating requirements, including the generation of positive cash flows from operations by increasing the number of field trips and operation of the new MV Ribuuk Meto and SV Kwai vessels, provide the opportunity for MISC to continue as a going concern. For the year ending September 30, 2022, RepMar has appropriated $1,579,750 to fund MISC operations, including $450,000 to fund drydocking costs.

## (8) 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. During the year ended September 30, 2021, four confirmed cases were identified in the Marshall Islands that were isolated and contained. On August 8, 2022, community transmission was identified and MISC has determined that such may negatively impact MISC's business, results of operations, and financial position and MISC may become more 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 MISC 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.

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# INDEPENDENT AUDITOR'S 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*

Chairman
Board of Directors
Marshall Islands Shipping Corporation:

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 Marshall Islands Shipping Corporation (MISC), which comprise the statement of net position as September 30, 2021, 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 December 29, 2022.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered MISC'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 MISC's internal control. Accordingly, we do not express an opinion on the effectiveness of MISC'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 and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses as item 2021-001 that we consider to be a material weakness.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether MISC's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the 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 item 2021-002.

**MISC's Responses to Findings**

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

Deloitte & Touche LLP

December 29, 2022

## MARSHALL ISLANDS SHIPPING CORPORATION

Schedule of Findings and Responses
Year Ended September 30, 2021

Finding No. 2021-001

Inventory

Criteria: Generally accepted accounting principles (GAAP) requires inventories on hand consisting of items purchased for resale be valued at the lower of cost (moving average) or market value (net realized value).

Condition: As of September 30, 2021, MISC did not observe and perform a physical inventory count. Ship inventories on hand and held by MISC were expensed as cost of goods sold during the year ended September 30, 2021. A supporting $60,000 inventory on hand schedule was subsequently provided on December 9, 2022, which was not considered material to the financial statements.

Cause: The cause of the above condition is the lack of internal control policies and procedures over the observation and performance of a physical year-end inventory count.

Effect: The effect of the above condition is a departure from GAAP resulting in a potential opinion modification.

Recommendation: We recommend management establish internal control policies and procedures over the observation and performance of a physical year-end inventory count.

Auditee Response and Corrective Action Plan: MISC physical inventory of ship inventories is counted upon the respective ship's arrival. These are then stored and added to new inventories for the next voyage. Similarly, at the end of the last voyage of a particular or end of a fiscal year, the inventories are also counted and added to the new inventories for the next voyage at the beginning of the new fiscal year. As a matter of policy and procedure, all such inventory data is recorded in MISC's accounting system and be ready to be authorized by the GM. It a normal practice on any material decisions, orders, rules and regulations relating to the financial operations of MISC be made by resolution of the Board of Directors and be recorded in the minutes of such meeting as a Policies and Procedures for Inventory. MISC has subsequently reconciled and corrected the General Ledger (GL) inventory account balances. Moving forward, MISC has hired a new Merchant supervisor to help with the inventory records and to timely reconcile the GL inventory accounts to prevent and detect any similar problem in the future.

Finding No. 2021-002

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 competition when it is determined in writing that there is only one source for the required supply, service, or construction item.

Condition: Supporting documentation was inadequate to evidence the procurement process utilized for the purchase of the following:

1. Purchase of $17,459 in parts for MV Ribuuk Meto.

2. Contract totaling $12,000 for international marine consultant.

3. Purchase of a $30,000 truck.

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

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

Recommendation: We recommend management establish adequate internal control policies and procedures requiring compliance with RepMar's Procurement Code. We recommend management complete documentation of the procurement process, from request 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.

Finding No. 2021-002, Continued

Local Noncompliance

Auditee Response and Corrective Action Plan: MISC at the outset expresses appreciation for the recent completion of the FY2021 audit as follows:

1. Purchase of $17,459 in parts for MV Ribuuk Meto, the purchase of the vessel was under special circumstance. The Cabinet established a Maritime Working Committee to look for and identify and negotiate with due diligence for the acquisition of a vessel in response to the COVID-19 anticipated transport needs. The Committee sent invitations for quotations from a number of sources, undergoing a short-listing process until they eventually selected what is currently the MV Ribuuk Meto. At the early stages of COVID-19 established protocols worldwide, the Committee was unable or in no position to send anyone to inspect the vessel. The owner of the vessel and its broker entered into an agreement to provide assistance relating to and including dry-docking, refitting, maritime related services, such as flagging, registration, clearances, crewing for the delivery of the vessel, etc. The physical condition of the vessel was good; however, there were structural, electrical, machinery works that needed to be undertaken. Accordingly, the owner indicated that the vessel could use its shipyard facility in Malaysia. This offer was accepted; however, the RMI needed an agent to inspect the daily or regular refitting works. The RMI was in no position to send anyone, so it also accepted the owner's offer in identifying one. The agent selected was never at the dry-dock for fear of the COVID pandemic. Unable to be there physically, the RMI had to rely on working closely with the dry-dock. There were parts that needed to be acquired and obviously were mostly available in Malaysia. At the completion of the dry-dock, the owner determined that the ship was safe for the voyage. After arrival, the ship was put to test and no problems were encountered. However, at a later time, mechanical problems became more frequent. The shipyard was able to find the parts, but not all. MISC decided to go to its regular supplier of parts, Japan Marine Engineer, which stocks marine engine parts including the Japanese engine parts. This is the same company that MISC gets parts for the MV Kwajelein, MV Aemman, and MV Majuro, all are Japanese made. Because of our working relationship with Japan Marine Engineer, and because of the urgency of the acquisition of the parts, the best choice to provide prompt and timely service, and reasonable prices as have been, Japan Maritime Engineer was approached to provide the parts. On an important note, Japan Maritime Engineer was also approached because of their professionalism and reliability. Accordingly, because of reliability to provide such service in a timely manner and considering the urgency to get the parts, they were approached.

2. Contracting an International Maritime Consultant: At the time of the COVID-19 outbreak and when the Government was exploring and considering possible options and alternative preparations for the arrival of the virus, the Government was in urgent, dire need to buy a vessel or vessels to supplement or support the then limited fleet size. The limitation was not only to respond to the ever increasing transport needs to the Neighboring Islands (NI) because of the anticipated coming of the virus, but also increasing needs by the NI and to deliver COVID related supplies, including foods (food baskets, etc.). While the huge transport needs were urgent and needed to be readily available, the MV Enen Kio was at anchorage in port because of a suspected design problem, physically unusual high vibrations and rattling noises when the speed went over 4 knots. MISC was advised by maritime experts to stop operating the vessel until the problem was fixed, otherwise the problem would worsen.

Finding No. 2021-002, Continued

Local Noncompliance

Auditee Response and Corrective Action Plan, Continued:

The Cabinet established a Maritime Working Committee to look for the vessels, as well as to address the problem encountered by the MV Enen Kio. In regards the MV Enen Kio, the Committee approached the GIZ maritime engineers and naval architect for assistance. The assistance was provided in the form of providing the naval architect involved in the German assisted Transitioning to Sustainable Sea Transport and Reduction of Gas Emission. Through said assistance, a maritime expert was identified in New Zealand, namely Mark Oxley. He was selected because, in addition to his previous association with MISC in maritime works, he also knew a number of naval architects from on-going and past associations.

Because of the highly urgent circumstances surrounding timely need to fix the MV Enen Kio problem, Mr. Oxley was selected. Through him and his close association with a naval architect, the problem was determined as faulty design. Legal settlement would have been costly as advised by the AG's Office. Mr. Oxley and his colleague helped design a device that, to date, has helped the vessel return to normal expected service. It is made out of wood, so it is temporary. The Board has agreed to send the ship to Kiribati to replace it with a long-term steel device. This option is the cheapest as there were considerations to send her to Fiji or back to China, to have the builder correct the problem.

3. Purchase of $30,000 truck. The old MISC white truck was encountering frequent break-down, with regular mechanical problems. In order to avoid disruptions in preparation for the vessels to turn around and resume their expected transport services as timely as possible to the Northern Islands and back to Majuro, and to maintain timey unloading of copra, and in view of the availability of the truck at such a reasonable price, and the unreliability of the old white truck, the Board approved the purchase of the new truck. It was noted and was a big concern to the public and the Government that the turn around time of vessels was slow, so MISC needed to responsibly respond to such concerns. Accordingly, the purchase of the truck at such a reasonable price, was justified in view of the Board and others within MISC.

MISC utilizes the approval by the Board of Directors as evidenced in the minutes of meetings which become a policy and regulation for the Company. MISC uses or follows the Government's policy in terms of purchasing with three (3) available quotes. If one or two quotes are entertained with no other vendors having the available stock on hand or the right kind of parts in stock, MISC will ensure more complete supporting documentation on file for sole source. Such will include a Memo to File justifying the reason for such urgent purchase or any other purchasing to be approved by Management or Board, especially during disaster season time, such as COVID-19, and to avoid and prevent this from happening in the future. MISC will also need to have a document on file supporting competitive bidding, including advertisement to the general public, for such purchases more than $25,000.

Unresolved Prior Year Findings
Year Ended September 30, 2021

There are no unresolved audit findings from prior year audits of MISC.