

GUAM WATERWORKS AUTHORITY

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

YEARS ENDED SEPTEMBER 30, 2007 AND 2006

INDEPENDENT AUDITORS' REPORT

Consolidated Commission on Utilities:

We have audited the accompanying statements of net assets of the Guam Waterworks Authority (GWA), a component unit of the Government of Guam, as of September 30, 2007 and 2006, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of GWA's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Guam Waterworks Authority as of September 30, 2007 and 2006, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 1-5 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of GWA's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedules on pages 29-32 are presented for purposes of additional analysis and are not a required part of the basic financial statements. These accompanying schedules are the responsibility of GWA's management. The accompanying schedules on pages 29-32 have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects, in relation to the basic financial statements taken as a whole. The accompanying schedule on page 28 has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 29, 2008, on our consideration of the Guam Waterworks Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte + Touche LLP

April 29, 2008

GUAM WATERWORKS AUTHORITY

Management's Discussion and Analysis September 30, 2007 and 2006

As management of the Guam Waterworks Authority (GWA), we offer readers of GWA's financial statements this narrative overview and analysis for the fiscal year ended September 30, 2007. We encourage readers to consider the information presented here and in our basic financial statements, which begin on page 6.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the GWA's basic financial statements. GWA's basic financial statements are for a single proprietary fund and include the financial statements, notes to those financial statements and other supplementary and statistical information.

Proprietary Fund Financial Statements

GWA's operations are accounted for as a single proprietary fund using the full accrual basis of accounting. In this regard, GWA operations are accounted for in a manner similar to a private enterprise. Within this one proprietary fund, GWA segregates revenues and expenses for various purposes such as operations, debt service and capital improvements, but that segregation does not create separate proprietary funds.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements can be found beginning on page 11 of this report.

Other Information

In addition to the basic financial statements and accompanying notes, this report also presents supplementary and statistical information. Certain selected supplementary and statistical information can be found beginning on page 28 of this report.

Financial Highlights

- Total assets of GWA exceeded total liabilities at the close of the fiscal year by \$190.7 million (net assets).
- The reduction in net assets was \$6.2 million less than (or a 76% change) the net change in fiscal year 2006.
- Total net assets of GWA decreased by \$1.9 million during fiscal year 2007.
- Operating revenues increased by \$5.1 million as compared to fiscal year 2006.
- Net capital assets at September 30, 2007 increased by \$14.8 million as compared to the net balance at September 30, 2006.
- Operating and maintenance expenses increased by \$0.3 million as compared to fiscal year 2006.
- GWA experienced an operating loss of \$2.0 million for the fiscal year ended September 30, 2007 as compared to prior year's operating loss of \$6.8 million, a 71% change.

Financial Condition

The Authority's total net assets decreased by \$1.9 million during the fiscal year (see Table 1 below) due to interest expense, inventory write-down, and operating and maintenance expenses.

The decrease in long-term liabilities of \$4.5 million (see Table 1 below) is due to the payments of debt service and surcharges.

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The Authority's investment in capital assets net, of related debt, represents 110% of total net assets. The amount invested in capital assets, net of debt, decreased by \$5.9 million. The decrease was the result of capital acquisitions, net of depreciation and disposals, and 2005 revenue bonds used in fiscal 2007 to acquire capital assets.

Table 1
Summary Statement of Net Assets

	September 30, 2007	September 30, 2006	September 30, 2005	2007 to 2006 Comparison	
				Increase/ (Decrease)	% Change
Current Assets	\$ 17,483,822	\$ 15,466,932	\$ 17,465,545	\$ 2,016,890	13.04%
Property, plant and equipment, net	254,399,284	239,602,789	220,166,031	14,796,495	6.18%
Other non-current assets	<u>61,688,758</u>	<u>80,782,409</u>	<u>16,955,812</u>	<u>(19,093,651)</u>	<u>(23.64)%</u>
Total assets	<u>333,571,864</u>	<u>335,852,130</u>	<u>254,587,388</u>	<u>(2,280,266)</u>	<u>(0.68)%</u>
Current liabilities	21,165,672	17,019,403	16,047,565	4,146,269	24.36%
Long-term liabilities	<u>121,693,600</u>	<u>126,187,085</u>	<u>37,796,786</u>	<u>(4,493,485)</u>	<u>(3.56)%</u>
Total liabilities	<u>142,859,272</u>	<u>143,206,488</u>	<u>53,844,351</u>	<u>(347,216)</u>	<u>(0.24)%</u>
Net Assets:					
Invested in capital assets, net of related debt	210,517,277	216,460,775	218,981,314	(5,943,498)	(2.75)%
Restricted	975,798	3,034,766	4,145,701	(2,058,968)	(67.85)%
Unrestricted	<u>(20,780,483)</u>	<u>(26,849,899)</u>	<u>(22,383,978)</u>	<u>6,069,416</u>	<u>(22.60)%</u>
Total net assets	<u>\$190,712,592</u>	<u>\$192,645,642</u>	<u>\$200,743,037</u>	<u>\$ (1,933,050)</u>	<u>(1.00)%</u>

Total operating revenues of \$46.9 million increased by \$5.1 million for the current year and operating expenses of \$48.9 million increased by \$0.3 million, resulting in a decrease in net operating loss of \$4.8 million when compared to the prior year (see Table 2).

The major changes in net income from the prior year were from the following:

- Water and wastewater revenues increased by \$2.6 million over the prior fiscal year (see Table 3 below) due to increases in consumption (0.43%) and the number of residential customers (2.15%). The basic water and sewer charges are assessed monthly on residential customers without regard to consumption.
- Operating expenses increased by \$0.3 million. The increase in operating expenses resulted from an increase in electricity of \$1.4 million, other expenses of \$1 million, and personnel costs of \$0.1 million, which were offset by the decrease in water purchases (\$2.2 million).
- Non-operating expenses decreased by \$0.8 million which resulted from an increase in nonoperating revenues of \$1.6 million offset by increased interest expense of \$0.7 million.

Table 2
Results of Operations/Statement of Revenues, Expenses and Changes in Net Assets

	September 30, 2007	September 30, 2006	September 30, 2005	2007 to 2006 Comparison	
				Increase/ (Decrease)	% Change
Revenues:					
Water	\$ 31,705,832	\$ 29,840,570	\$ 30,315,669	\$ 1,865,262	6.25%
Wastewater	15,336,312	14,631,593	13,885,149	704,719	4.82%
Other operating revenue	653,098	474,872	273,373	178,226	37.53%
Bad debt	<u>(832,515)</u>	<u>(3,188,253)</u>	<u>(2,136,830)</u>	<u>2,355,738</u>	<u>73.89%</u>
Total operating revenue	<u>46,862,727</u>	<u>41,758,782</u>	<u>42,337,361</u>	<u>5,103,945</u>	<u>12.22%</u>

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Management's Discussion and Analysis September 30, 2007 and 2006

Table 2
Results of Operations/Statement of Revenues, Expenses and Changes in Net Assets, Continued

	September 30, 2007	September 30, 2006	September 30, 2005	2007 to 2006 Comparison Increase/ (Decrease)	% Change
Expenses:					
Power purchases	11,914,539	10,521,173	8,820,481	1,393,366	13.24%
Water purchases	2,820,954	5,017,247	6,368,221	(2,196,293)	(43.77)%
Salaries, wages and benefits	14,598,046	14,470,767	11,590,367	127,279	0.88%
Depreciation	9,748,542	9,375,635	9,425,507	372,907	3.98%
Administrative and general	5,162,451	4,697,858	4,148,100	464,593	9.89%
Contractual	4,141,397	3,956,433	2,327,605	184,964	4.68%
Supplemental annuity benefits	<u>464,620</u>	<u>473,252</u>	<u>503,822</u>	<u>(8,632)</u>	<u>(1.82)%</u>
Total operating expenses	<u>48,850,549</u>	<u>48,512,365</u>	<u>43,184,103</u>	<u>338,184</u>	<u>0.70%</u>
Net operating loss	(1,987,822)	(6,753,583)	(846,742)	4,765,761	70.56%
Non-operating revenue (expense)	4,663,991	3,084,825	(1,297,389)	1,579,166	51.19%
Less: Interest Expense	<u>6,266,080</u>	<u>5,577,844</u>	<u>353,613</u>	<u>688,236</u>	<u>12.34%</u>
Total non-operating expense	<u>(1,602,089)</u>	<u>(2,493,019)</u>	<u>(1,651,002)</u>	<u>810,930</u>	<u>32.53%</u>
Loss before capital contributions	(3,589,911)	(9,246,602)	(2,497,744)	5,656,691	61.18%
Capital contributions	<u>1,656,861</u>	<u>1,149,207</u>	<u>4,027,938</u>	<u>507,654</u>	<u>44.17%</u>
Change in net assets	(1,933,050)	(8,097,395)	1,530,194	6,164,345	76.13%
Net assets - beginning year	<u>192,645,642</u>	<u>200,743,037</u>	<u>199,212,843</u>	<u>(8,097,395)</u>	<u>(4.03)%</u>
Net assets - end of year	<u>\$190,712,592</u>	<u>\$192,645,642</u>	<u>\$200,743,037</u>	<u>\$ (1,933,050)</u>	<u>(1.00)%</u>

Table 3
Annual Water Sales

Class Type	Consumption (in gallons)			2007 to 2006 Comparison
	FY07	FY06	FY05	Increase (Decrease)
Agricultural	145,494,530	135,037,036	165,666,242	10,457,494
Golf Course	5,402,988	13,154,159	28,035,535	(7,751,171)
Comm 1	803,352,321	847,822,236	775,485,699	(44,469,915)
Comm 2	137,703,436	135,919,138	136,013,038	1,784,298
Comm 3	152,347,968	180,014,095	147,663,633	(27,666,127)
Federal	1,812,835	940,391	1,640,170	872,444
Government	512,157,762	563,437,506	421,534,812	(51,279,744)
Hotel	1,044,423,148	1,013,682,600	904,579,286	30,740,548
Irrigation	44,185,455	64,669,996	51,040,774	(20,484,541)
Residential	<u>4,125,638,707</u>	<u>3,987,420,390</u>	<u>3,984,761,111</u>	<u>138,218,317</u>
TOTAL	<u>6,972,519,150</u>	<u>6,942,097,547</u>	<u>6,616,420,300</u>	<u>30,421,603</u>

Table 4
Capital Assets, Net of Accumulated Depreciation

	September 30, 2007	September 30, 2006	September 30, 2005	2007 to 2006 Comparison Increase/ (Decrease)	% Change
Plant, buildings and equipment, net	\$ 231,668,972	\$ 212,887,711	\$ 211,392,152	\$ 18,781,261	8.82%
Construction in progress	<u>22,730,312</u>	<u>26,715,078</u>	<u>8,773,879</u>	<u>(3,984,766)</u>	<u>(14.92)%</u>
Total	<u>\$ 254,399,284</u>	<u>\$ 239,602,789</u>	<u>\$ 220,166,031</u>	<u>\$ 14,796,495</u>	<u>6.18%</u>

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Management's Discussion and Analysis September 30, 2007 and 2006

Capital Assets, Net of Accumulated Depreciation

The Authority had \$254 million (net of accumulated depreciation) invested in water utility capital assets as of September 30, 2007. The investment in capital assets includes building, improvements, water treatment plants, filter plants, water transmission and distribution mains, water storage facilities, reservoirs, pump stations, machinery and equipment. This amount represents an increase of \$14.8 million over the prior fiscal year. See note 2 to the accompanying financial statements for additional information concerning capital assets.

Table 5
Long Term Debt, Less Current Maturities

	September 30, 2007	September 30, 2006	September 30, 2005	2007 to 2006 Comparison	
				Increase/ (Decrease)	% Change
Long-term debt	\$ 102,204,246	\$ 104,679,397	\$ 15,292,641	\$ (2,475,151)	(2.36)%
Guam Power Authority	5,230,111	7,587,764	9,640,101	(2,357,653)	(31.07)%
United States Navy	<u>6,641,023</u>	<u>7,102,685</u>	<u>7,561,820</u>	<u>(461,662)</u>	<u>(6.50)%</u>
Total	<u>\$ 114,075,380</u>	<u>\$ 119,369,846</u>	<u>\$ 32,494,562</u>	<u>\$ (5,294,466)</u>	<u>(4.44)%</u>

As of September 30, 2007 the Authority had total long-term debt outstanding of \$114 million, net of unamortized costs, which is a decrease of \$5.3 million over the prior year. See note 4 to the accompanying financial statements for additional information on long-term debt.

The Authority is required by bond covenants to maintain principal, interest, and reserve funds for the bond issue outstanding. In addition, the Authority is required to set rates and charges to yield revenues equal to at least 122% of the current annual debt service requirements of the outstanding 2005 revenue bonds. The payments applied to the Guam Power Authority and United States Navy is derived from assessed surcharges from current customers.

Looking Forward

GWA continues to aggressively pursue replacing old meters with automated meter reading (AMR) meters. Approximately 24,000 (60% of active meters) meters have been replaced with the new AMR meters. The AMR program is anticipated for completion at the conclusion of FY2009.

In August 2007, the Public Utilities Commission approved a petition by GWA to implement a 14.24% increase in water and wastewater rates. The rate increase was premised on annual debt service requirements for the 2005 GWA's \$105 Million Revenue Bond. Annual debt service is approximately \$5.3 million per year.

In March 2008, the Consolidated Commission on Utilities approved a System Development Charge (SDC) for GWA. The charge is to recover costs associated with constructing, expanding, upgrading and repairing water and wastewater facilities to serve new customers. The charges range from \$3,280 for a 3/4" meter to \$1,476,000 for a 16" meter for new water users. Section 12015 of the Guam Code Annotated requires prior approval of the Public Utilities Commission (PUC) before its implementation. GWA anticipates regulatory proceedings will commence sometime in the 4th quarter of fiscal year 2008.

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Management's Discussion and Analysis
September 30, 2007 and 2006

The potential and likely increase in population as a result of the United States Department of Defense (DOD) relocation to Guam from Okinawa, Japan between 2008 and 2015 presents another challenge to GWA. Assessing the impact and the associated infrastructure requirements is predicated on population growth and DOD's partnering with GWA in meeting the needs to accommodate the growth and demand on the system. The estimated population growth associated with the impending military relocation is 46,000 people. The growth is anticipated to take place primarily in the Northern part of the island; however, some increase in activity is also anticipated in the Southern part due to the concentration of marine facilities in the vicinity.

There are several management and upgrade initiatives presently underway that affect our J.D. Edwards computerized accounting information system. They are the Fixed Assets module, the Job Cost module and Crystal Reporting software. The target implementation date for the fixed asset module is July 1st (3rd quarter, FY '08), and the remaining two is October 1, 2008 (FY '09).

As part of the financial program contained in the Water Resources Master Plan (WRMP), GWA is presently conducting a rate study to generate sufficient revenues to cover the cost of all compliance activities and deliverables required by the Stipulated Order for Preliminary Relief, as well as any other anticipated expenses, including any measures necessary to ensure compliance with the Clean Water Act and the Safe Drinking Water Act and costs related to the infrastructure improvements identified in the WRMP.

Request for Information

This financial report is to provide interested parties with a general overview of the Authority's finances. If you have any questions about this report or need additional information, you may submit a request in writing to: Chief Financial Officer, Guam Waterworks Authority, 578 N. Marine Corp Drive, Tamuning, GU 96913, or telephone (671) 647-2583.

Management's Discussion and Analysis for the years ended September 30, 2006 and 2005, is set forth in GWA's report on the audit of the financial statements, which is dated May 17, 2007, and that Discussion and Analysis explains the major factors impacting the 2006 and 2005 financial statements and can be viewed at the Office of the Public Auditor's website at www.guamopa.com.

GUAM WATERWORKS AUTHORITY

Statements of Net Assets
September 30, 2007 and 2006

<u>ASSETS</u>	<u>2007</u>	<u>2006</u>
Current assets:		
Cash:		
Unrestricted	\$ 6,286,905	\$ 2,368,633
Restricted	975,798	3,034,766
Accounts receivable, net	8,013,418	7,705,974
Materials and supplies inventory, net of allowance for obsolescence of \$339,745 and \$380,425 at September 30, 2007 and 2006, respectively	2,207,701	2,294,529
Current portion of other assets	-	63,030
Total current assets	<u>17,483,822</u>	<u>15,466,932</u>
Property, plant and equipment:		
Utility plant in service:		
Water system	232,312,800	206,765,134
Wastewater system	178,658,425	178,016,326
Non-utility property	15,511,860	15,135,570
Construction work in progress	22,730,312	26,715,078
	449,213,397	426,632,108
Less accumulated depreciation	<u>(194,814,113)</u>	<u>(187,029,319)</u>
Property, plant and equipment, net	<u>254,399,284</u>	<u>239,602,789</u>
Other noncurrent assets:		
Restricted cash	49,132,976	69,970,413
Investments	9,618,008	7,769,922
Other assets, net of current portion	2,937,774	3,042,074
Total other non current assets	<u>61,688,758</u>	<u>80,782,409</u>
	<u>\$ 333,571,864</u>	<u>\$ 335,852,130</u>

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Statements of Net Assets, Continued
September 30, 2007 and 2006

<u>LIABILITIES AND NET ASSETS</u>	2007	2006
Current liabilities:		
Current maturities of long-term debt	\$ 5,092,182	\$ 2,631,707
Accounts payable:		
United States Navy	238,020	283,213
Guam Power Authority	3,256,848	3,072,659
Trade	3,515,500	3,920,272
Accrued payroll and employee benefits	593,965	540,257
Current portion of employee annual leave	333,437	348,463
Accrued supplemental/COLA annuities	1,696,208	1,630,795
Deferred revenue	1,214,976	1,289,050
Payable to contractors	2,758,597	1,355,104
Customer deposits	1,973,100	1,805,732
Other liabilities	492,839	142,151
Total current liabilities	21,165,672	17,019,403
Long-term debt, less current maturities:		
Long-term debt	102,204,246	104,679,397
Guam Power Authority	5,230,111	7,587,764
United States Navy	6,641,023	7,102,685
Employee annual leave, less current portion	689,382	719,844
Retirement fund deferred contributions	6,226,388	5,476,855
DCRS sick leave liability	535,641	455,105
Advances for construction	166,809	165,435
Total liabilities	142,859,272	143,206,488
Commitments and contingencies		
Net assets:		
Invested in capital assets, net of related debt	210,517,277	216,460,775
Restricted	975,798	3,034,766
Unrestricted	(20,780,483)	(26,849,899)
Total net assets	190,712,592	192,645,642
	\$ 333,571,864	\$ 335,852,130

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2007 and 2006

	2007	2006
Operating revenues:		
Water:		
Private	\$ 28,926,150	\$ 28,057,921
Government	2,779,682	1,782,649
	31,705,832	29,840,570
Wastewater:		
Private	12,548,076	11,757,592
Government	2,788,236	2,874,001
	15,336,312	14,631,593
Other	653,098	474,872
Bad debt expense:		
Bad debt	(859,601)	(3,214,713)
Recovery	27,086	26,460
	(832,515)	(3,188,253)
Total operating revenues	46,862,727	41,758,782
Operating and maintenance expenses:		
Power purchases	11,914,539	10,521,173
Water purchases	2,820,954	5,017,247
	14,735,493	15,538,420
Salaries, wages and benefits	14,598,046	14,470,767
Depreciation	9,748,542	9,375,635
Administrative and general	5,162,451	4,697,858
Contractual	4,141,397	3,956,433
Supplemental annuity benefits	464,620	473,252
	48,850,549	48,512,365
Operating loss	(1,987,822)	(6,753,583)
Nonoperating revenues (expenses):		
Allowance for funds used during construction	2,136,807	1,368,485
Interest income	3,225,083	3,209,683
Interest expense	(6,266,080)	(5,577,844)
Other expense	(68,262)	(1,493,343)
Loss on asset disposal	(15,476)	-
Loss on inventory write-down	(614,161)	-
	(1,602,089)	(2,493,019)
Total nonoperating revenues (expenses), net	(1,602,089)	(2,493,019)
Loss before capital contributions	(3,589,911)	(9,246,602)
Capital contributions:		
Grants from U.S. Government	1,656,861	849,207
Other contributions	-	300,000
	1,656,861	1,149,207
Total capital contributions	1,656,861	1,149,207
Changes in net assets	(1,933,050)	(8,097,395)
Net assets at beginning of year	192,645,642	200,743,037
Net assets at end of year	\$ 190,712,592	\$ 192,645,642

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Statements of Cash Flows
Years Ended September 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
<u>Increase (decrease) in cash</u>		
Cash flows from operating activities:		
Cash received from customers	\$ 46,722,651	\$ 43,984,029
Cash payments to suppliers for goods and services	(24,492,806)	(24,624,326)
Cash payments to employees for services	(13,759,757)	(12,828,683)
Cash payments to retirees	(399,207)	(818,632)
Net cash provided by operating activities	<u>8,070,881</u>	<u>5,712,388</u>
Cash flows from noncapital financing activities:		
Principal repayment of long-term debt	(2,713,840)	(2,438,080)
Interest paid on long-term debt	(426,287)	(660,512)
Net cash used in noncapital financing activities	<u>(3,140,127)</u>	<u>(3,098,592)</u>
Cash flows from capital and related financing activities:		
Contributed capital received	1,656,861	1,149,207
Acquisition of utility plant	(21,128,630)	(26,338,594)
Proceeds from disposal of utility plant	108,417	-
Proceeds from issuance of capital debt	-	104,679,397
Principal repayment of capital debt	-	(15,385,845)
Interest paid on capital debt	(5,923,906)	(4,987,519)
Bond issuance costs	-	(3,042,074)
Net cash (used in) provided by capital and related financing activities	<u>(25,287,258)</u>	<u>56,074,572</u>
Cash flows from investing activities:		
Transfers from (to) restricted funds	21,048,319	(61,096,744)
Interest income received	3,226,457	3,210,576
Net cash provided by (used in) investing activities	<u>24,274,776</u>	<u>(57,886,168)</u>
Net change in unrestricted cash	3,918,272	802,200
Unrestricted cash at beginning of year	<u>2,368,633</u>	<u>1,566,433</u>
Unrestricted cash at end of year	\$ <u><u>6,286,905</u></u>	\$ <u><u>2,368,633</u></u>
Supplemental information on noncash activities:		
Construction work-in progress	\$ 1,403,493	\$ 1,105,314
Payable to contractors	(1,403,493)	(1,105,314)
	\$ <u><u>-</u></u>	\$ <u><u>-</u></u>

See accompanying notes to financial statements.

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Statements of Cash Flows, Continued
 Years Ended September 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (1,987,822)	\$ (6,753,583)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	9,748,542	9,375,635
Bad debt expense	859,601	3,214,713
Unfunded pension costs	749,533	1,283,136
(Increase) decrease in assets:		
Accounts receivable	(1,167,045)	(1,050,741)
Materials and supplies inventory	(527,333)	(411,064)
Other assets	63,030	(63,030)
Increase (decrease) in liabilities:		
Accounts payable	(265,776)	(628,720)
Accrued payroll and employee benefits	53,708	107,388
Employee annual leave	(45,488)	128,371
Accrued supplemental/COLA annuities	65,413	(345,380)
Deferred revenue	(74,074)	831,200
Customer deposits	167,368	61,275
Other liabilities	350,688	(160,001)
DCRS sick leave liability	80,536	123,189
Net cash provided by operating activities	<u>\$ 8,070,881</u>	<u>\$ 5,712,388</u>

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(1) Organization Summary of Significant Accounting Policies

Organization

The Guam Waterworks Authority (GWA) is a component unit of the Government of Guam (GovGuam). GWA is subject to the regulations of the Public Utility Commission of Guam (PUC). GWA became an autonomous agency in 1996 under Public Law 23-119 and derives its revenues mainly from its water and wastewater system. The water system is engaged in the production, treatment, and distribution of water to villages and communities of Guam. The wastewater system is engaged in the collection and treatment of wastewater from residences and industries in the villages of Guam. GWA is governed by a five-member Consolidated Commission on Utilities (CCU). PUC determines such matters as rates and charges for services.

The financial statements of GWA have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. Government Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Government of Guam has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

Basis of Accounting

GWA is accounted for on a “flow of economic resources management focus,” using the accrual basis of accounting. Under this method, all assets and liabilities associated with operations are included on the statement of net assets, and revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Net Assets

Net assets represent the residual interest in GWA’s assets after liabilities are deducted and consist of four sections: invested in capital assets, net of related debt; restricted expendable and nonexpendable, and unrestricted. Net assets invested in capital assets, net of debt, include capital assets, restricted and unrestricted, net of accumulated depreciation. Net assets are reported as restricted when constraints are imposed by third parties or enabling legislation. All of GWA’s restricted net assets are expendable. All other net assets are unrestricted.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(1) Organization Summary of Significant Accounting Policies, Continued

Trade Accounts Receivable

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

Materials and Supplies Inventories

Materials and supplies inventory are stated at the lower of cost or market with cost determined under the first-in, first-out method.

Other Assets

Other assets consist of the bond issuance costs associated with the bond payable. Bond issuance costs are amortized throughout the life of the bond using the straight-line method.

Property, Plant and Equipment

Plant in service amounting to \$324,988,118 is stated at estimated historical cost as determined by an independent engineering consultant at September 30, 1998. Plant in service acquired subsequent to that date is stated at cost. Non-utility property and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets (5 - 50 years for plant assets). Current policy is to capitalize items over \$5,000.

Noncurrent Restricted Cash

The purpose of the noncurrent restricted cash is for long-term capital improvements and bond related activities.

Compensated Absences

Compensated absences are accrued and reported as a liability in the period earned. Annual leave expected to be paid out within the next fiscal year is accrued and is included in current liabilities. Employees are credited with vacation leave at rates of 104, 156 or 208 hours per fiscal year, depending upon their service time with GWA. Accumulation of such vacation credits is normally limited to 480 hours at fiscal year end; however, management has exercised its authority in certain conditions to allow accumulation of up to 720 hours. All such vacation credit is convertible to pay upon termination of employment.

During the year ended September 30, 2003, Public Law 27-05 was implemented, reducing the amount of leave employees can earn in a fiscal year (either 104 or 156 hours) and the maximum accumulation amount of annual leave to 320 hours. Any annual leave earned in excess of 320 hours, but not to exceed 100 hours as of February 28, 2003 shall be credited to the employees sick leave. The remaining excess hours must be used by September 30, 2004 or will be lost. Public Law 27-106 does not allow lump sum compensation or retirement credit for annual leave in excess of three hundred twenty (320) hours.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(1) Organization Summary of Significant Accounting Policies, Continued

Revenue

Customer water meters are read on a cyclical basis throughout a monthly period depending on the route schedules of the Guam Power Authority (GPA) pursuant to a combined billing system arrangement between GWA and GPA. Revenue is recognized in the period that meters are read. Wastewater treatment is billed at a flat rate of \$22 per month for residential accounts and 80% of current water consumption for commercial and government accounts. At end of each month, unbilled revenues are accrued for each cycle based on the most recent cycle billing. Unbilled receivables at September 30, 2007 and 2006 are \$1,552,242 and \$2,131,804, respectively.

Pursuant to local law, GWA provides water to fire hydrants in Guam and classifies such service as government water revenue. Historically, however, no GovGuam agency has been tasked with paying for such service. Consequently, GWA provides an allowance for the full amount of the billings, on a monthly basis. GWA is currently pursuing the matter of billing such service with the PUC. Fire hydrant revenue was \$259,020 for the years ended September 30, 2007 and 2006. Fire hydrant receivables were \$6,287,291 and \$6,028,271 as of September 30, 2007 and 2006, respectively.

Cash

For purposes of the statements of net assets and the statements of cash flows, cash is defined as cash deposits in banks and time certificates of deposit with initial maturities of three months or less.

Capitalization of Interest

GWA capitalizes interest on construction in progress based on the weighted average interest rate. During the years ended September 30, 2007 and 2006, interest of \$2,136,807 and \$1,368,485 was capitalized.

Operating and Non-Operating Revenue and Expenses

Operating revenues and expenses generally result directly from the operation and maintenance of GWA. Non-operating revenues and expenses result from capital and financing activities, costs and related recoveries from natural disasters, surcharges and certain other non-recurring income and costs.

Grants and Contributions

Grants and contributions consist of government mandated and voluntary nonexchange transactions as defined by GASB Statement No. 33. Approved capital grants not yet received amounted to approximately \$4,358,231 and \$7,047,685 at September 30, 2007 and 2006, respectively.

Reclassifications

Certain balances in the 2006 financial statements have been reclassified to correspond with the 2007 presentation.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(2) Property, Plant and Equipment

	Beginning Balance October 1, 2006	Transfers and Additions	Transfers and Deletions	Ending Balance September 30, 2007
Utility Plant in Service – Water	\$ 206,765,134	\$ 27,635,306	\$ (2,087,640)	\$ 232,312,800
Utility Plant in Service - Wastewater	178,016,326	642,099	-	178,658,425
General Fixed Assets	15,135,570	376,290	-	15,511,860
Accumulated Depreciation	(187,029,319)	(9,748,542)	1,963,748	(194,814,113)
Construction Work in Progress	<u>26,715,078</u>	<u>24,932,713</u>	<u>(28,917,479)</u>	<u>22,730,312</u>
	<u>\$ 239,602,789</u>	<u>\$ 43,837,866</u>	<u>\$ (29,041,371)</u>	<u>\$ 254,399,284</u>
	Beginning Balance October 1, 2005	Transfers and Additions	Transfers and Deletions	Ending Balance September 30, 2006
Utility Plant in Service – Water	\$ 200,595,049	\$ 6,170,085	\$ -	\$ 206,765,134
Utility Plant in Service - Wastewater	173,861,945	4,154,381	-	178,016,326
General Fixed Assets	14,588,842	546,728	-	15,135,570
Accumulated Depreciation	(177,653,684)	(9,375,635)	-	(187,029,319)
Construction Work in Progress	<u>8,773,879</u>	<u>28,419,752</u>	<u>(10,478,553)</u>	<u>26,715,078</u>
	<u>\$ 220,166,031</u>	<u>\$ 29,915,311</u>	<u>\$ (10,478,553)</u>	<u>\$ 239,602,789</u>

In previous years, GWA has entered into a long-term agreement to purchase water. In March 2006, GWA terminated the long-term agreement through a purchase of fixed assets amounting to \$5,975,000.

(3) Accounts Receivable

Accounts receivable at September 30, 2007 and 2006, are as follows:

	2007	2006
Customers:		
Private	\$ 13,859,980	\$ 13,637,773
Government	<u>9,432,438</u>	<u>8,523,869</u>
	23,292,418	22,161,642
Federal agencies	556,136	375,406
GPA	<u>45,190</u>	<u>189,668</u>
	<u>23,893,744</u>	<u>22,726,716</u>
Less allowance for doubtful receivables:		
Private	(8,585,446)	(8,101,208)
Government	<u>(7,294,880)</u>	<u>(6,919,534)</u>
	<u>(15,880,326)</u>	<u>(15,020,742)</u>
	<u>\$ 8,013,418</u>	<u>\$ 7,705,974</u>

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(3) Accounts Receivable, Continued

	<u>2007</u>	<u>2006</u>
Allowance breakdown:		
Beginning balance	\$ (15,020,742)	\$ (11,806,029)
Less:		
Accounts written off during the year	17	-
Bad debt expense	<u>(859,601)</u>	<u>(3,214,713)</u>
Ending balance	\$ <u>(15,880,326)</u>	\$ <u>(15,020,742)</u>

Substantially all customer accounts receivable are from individuals, companies and government agencies based in Guam.

(4) Long-Term Debt

Long-term debt at September 30, 2007 and 2006 is as follows:

	<u>2007</u>	<u>2006</u>
Note payable to the U.S. Navy, interest at 1.25%, due in monthly installments of principal and interest of \$45,833 through March 2009, \$132,545 through March 2011, and \$264,853 through June 2012, collateralized by real property (see note 14).	\$ 7,103,582	\$ 7,559,502
Payable to the Guam Power Authority in settlement of previously unpaid balances, interest at 4.33%, payable in monthly principal and interest installments of \$212,899 through 2010.	7,504,734	9,762,654
Bonds:		
2005 Series, initial face value of \$101,175,000, interest at varying rates from 5.000% to 5.875% payable semiannually in January and July, principal and mandatory sinking fund payments payable in varying annual installments commencing with a payment of \$1,865,000 in July 2008, increasing to \$6,810,000 in July 2035.	<u>101,175,000</u>	<u>101,175,000</u>
Total long-term debt	115,783,316	118,497,156
Less current maturities	<u>(5,092,182)</u>	<u>(2,631,707)</u>
	110,691,134	115,865,449
Bond premium	<u>3,384,246</u>	<u>3,504,397</u>
	\$ <u>114,075,380</u>	\$ <u>119,369,846</u>

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(4) Long-Term Debt, Continued

As of September 30, 2006, future maturities of long-term debt are as follows:

<u>Year ending September 30,</u>	<u>Total</u> <u>Principal</u>	<u>Interest</u>	<u>Debt Service</u>
2008	\$ 5,092,182	\$ 6,184,084	\$ 11,276,266
2009	5,348,845	5,982,005	11,330,850
2010	6,463,616	5,722,860	12,186,476
2011	4,529,966	5,560,715	10,090,681
2012	4,078,707	5,417,200	9,495,907
2013 through 2017	12,253,750	25,149,520	37,403,270
2018 through 2022	14,621,250	21,418,794	36,040,044
2023 through 2027	19,551,250	16,481,900	36,033,150
2028 through 2032	26,047,500	9,992,934	36,040,434
2033 through 2035	<u>17,796,250</u>	<u>2,029,005</u>	<u>19,825,255</u>
	<u>\$ 115,783,316</u>	<u>\$ 103,939,017</u>	<u>\$ 219,722,333</u>

In January 2006, GWA issued a bond in the amount of \$101,175,000 for the purpose of funding capital improvements, refinancing certain outstanding obligations, and financing new water meters. Interest on the bond is payable on January 1 and July 1 of each year, commencing January 1, 2006. Interest accrues on a 360 day year, twelve 30-day months. The bond matures on July 1, 2035.

GWA fully paid a debt to Municipal Services Group, Inc. (MSG) with proceeds from the above debt issuance. MSG indicated that it may make a claim against GWA in connection with the investment earnings on the Acquisition Fund for the Certificates of Participation 2005 Services relative to financing the purchase and installation of GWA's water meters. No provision has been recorded in the accompanying financial statements for a liability, if any, that may result from the matter as it is management's position that no claim will ultimately be asserted.

Proceeds of the 2005 series bonds, are to be used for the purpose of funding capital improvements of water and wastewater systems, refinancing certain outstanding obligations and loans, finance new water meters, paying capitalized interest and paying related issuance costs.

All gross revenues of GWA have been pledged to repay the 2005 series bond principal and interest.

Total bond proceeds were \$104,779,522, including a bond premium of \$3,604,522 while GWA incurred closing costs totaling \$3,128,108. The premium, termination fees and closing costs have been deferred and amortized on a straight line basis over the average remaining life of the 2005 bond. The closing costs, net of amortization, are reflected as other assets in the accompanying statements of net assets. The current year amortization of the deferred revenue and the deferred asset is reflected as other expense in the accompanying statements of revenues, expenses and changes in net assets.

Management is of the opinion that compliance with applicable debt covenants occurred during the year ended September 30, 2007.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(4) Long-Term Debt, Continued

The following summarizes movements in GWA's non-current liabilities for the years ended September 30, 2007 and 2006:

	Outstanding September 30, <u>2006</u>	<u>Increases</u>	<u>Decreases</u>	Outstanding September 30, <u>2007</u>	<u>Current</u>
Long-term debt	\$ 101,175,000	\$ -	\$ -	\$ 101,175,000	\$ 2,355,000
Premium on bonds	3,504,397	-	120,151	3,384,246	-
Guam Power Authority	9,762,654	-	2,257,920	7,504,734	2,274,623
U.S. Navy	7,559,502	-	455,920	7,103,582	462,559
Employee annual leave	1,068,307	-	45,488	1,022,819	333,437
Retirement fund deferred contributions	5,476,855	749,533	-	6,226,388	-
DCRS sick leave liability	455,105	80,536	-	535,641	-
Other liabilities	<u>165,435</u>	<u>1,374</u>	<u>-</u>	<u>166,809</u>	<u>-</u>
	<u>\$ 129,167,255</u>	<u>\$ 831,443</u>	<u>\$ 2,879,479</u>	<u>\$ 127,119,219</u>	<u>\$ 5,425,619</u>

	Outstanding September 30, <u>2005</u>	<u>Increases</u>	<u>Decreases</u>	Outstanding September 30, <u>2006</u>	<u>Current</u>
Long-term debt	\$ 15,385,845	\$ 101,175,000	\$ 15,385,845	\$ 101,175,000	\$ -
Premium on bonds	-	3,604,522	100,125	3,504,397	-
Guam Power Authority	11,747,272	-	1,984,618	9,762,654	2,174,890
U.S. Navy	8,012,964	-	453,462	7,559,502	456,817
Employee annual leave	939,936	128,371	-	1,068,307	348,463
Retirement fund deferred contributions	4,193,719	1,283,136	-	5,476,855	-
DCRS sick leave liability	331,916	123,189	-	455,105	-
Other liabilities	<u>164,542</u>	<u>893</u>	<u>-</u>	<u>165,435</u>	<u>-</u>
	<u>\$ 40,776,194</u>	<u>\$ 106,315,111</u>	<u>\$ 17,924,050</u>	<u>\$ 129,167,255</u>	<u>\$ 2,980,170</u>

(5) Employees' Retirement Plan

Employees of GWA hired before September 30, 1995 are under the Government of Guam Employees' Retirement System (a defined benefit, contributory pension plan). Employees hired after September 30, 1995, are members of the Defined Contribution Retirement System (DCRS). Until December 31, 1999, those employees who are members of the defined benefit plan with less than 20 years of service at September 30, 1995, had the option to switch to the Defined Contribution Retirement System.

The Defined Benefit Plan and the DCRS are administered by the Government of Guam Retirement Fund, to which GWA contributes based upon a fixed percentage of the payroll for those employees who are members of the Plan. Statutory contribution rates are established by the Guam Legislature.

Defined Benefit Plan

As a result of actuarial valuations performed as of September 30, 2005, 2004 and 2003 (applicable to fiscal year 2007, 2006 and 2005, respectively), contribution rates to fully fund the Retirement Fund liability as required by Guam Law, for the years ended September 30, 2007, 2006 and 2005, respectively, have been determined as follows:

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(5) Employees' Retirement Plan, Continued

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Normal costs (% of DB Plan payroll)	18.21%	17.83%	18.30%
Employee contributions (DB Plan employees)	<u>9.50%</u>	<u>9.50%</u>	<u>9.50%</u>
Employer portion of normal cost (% of DB Plan payroll)	<u>8.71%</u>	<u>8.33%</u>	<u>8.80%</u>
Employer portion of normal cost (% of total payroll)	4.26%	4.64%	4.96%
Unfunded liability cost (% of total payroll)	<u>20.66%</u>	<u>21.36%</u>	<u>19.93%</u>
Government contribution as a % of total payroll	<u>24.92%</u>	<u>26.00%</u>	<u>24.89%</u>

The statutory contribution as a % of DB payroll is as follows:

Employer	<u>22.94%</u>	<u>21.81%</u>	<u>20.81%</u>
Employee	<u>9.50%</u>	<u>9.50%</u>	<u>9.50%</u>

The plan utilized the actuarial cost method termed "entry age normal". Significant actuarial assumptions for the 2005, 2004, and 2003 actuarial valuations were:

Interest rate and rate of return	7.0%
Payroll increases	3.5%
Salary increases	4.0%-8.5%

The unfunded liability is being amortized as a level percentage of total payroll through May 1, 2031.

The actuarial valuation performed as of September 30, 2005, 2004 and 2003, did not provide a breakdown of actuarial present value of vested and non-vested accumulated plan benefits by sponsor or net assets available for benefits by sponsor. If the actuarial valuation were performed for GWA as a separate sponsor, the accrued unfunded liability at September 30, 2007 and 2006 may be materially different than that recorded in the accompanying financial statements.

The actuarial valuations and contribution rates are based on estimates and assumptions. Changes in estimates and actuarial assumptions may result in revisions in actuarial valuations and contributions rates. The effects of such revisions are recognized in the period in which the revisions are determined.

Defined Contribution Plan

Contributions into the DCRS by members are based on an automatic deduction of 5% of the member's regular base pay. The contribution is periodically deposited into an individual annuity account within the DCRS. Employees are afforded the opportunity to select from different annuity accounts available under the DCRS.

Statutory employer contributions into the DCRS for the years ended September 30, 2007 and 2006 are determined using the same rate as the DB plan. Of the amount contributed by the employer, only 5% of the member's regular base pay is deposited into the member's individual annuity account. The remaining amount is contributed towards the unfunded liability of the defined benefit plan.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(5) Employees' Retirement Plan, Continued

Members of the DCRS who have completed five years of government service, have a vested balance of 100% of both member and employer contributions plus any earnings thereon.

Public Law 26-86 allows members of the Defined Contribution Retirement System to receive a lump sum payment of one-half of their accumulated sick leave upon retirement. Management recorded an estimated liability of \$535,641 and \$455,105 at September 30, 2007 and 2006, respectively, for benefits to be payable under Public Law 26-86. The Public Law can be viewed at the Guam Legislature's website at www.guamlegislature.com.

Retirement Expense

Retirement expense for the years ended September 30, 2007, 2006 and 2005 is as follows:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Cash contributions and accruals	\$ 3,258,198	\$ 3,135,488	\$ 3,091,775
Increase (decrease) in accrued unfunded liability to the retirement fund	<u>749,533</u>	<u>1,283,136</u>	<u>(183,164)</u>
	<u>\$ 4,007,731</u>	<u>\$ 4,418,624</u>	<u>\$ 2,908,611</u>

For additional information on the Government of Guam Retirement Fund, inquiries may be addressed to the Director of the Government of Guam Retirement Fund, 424 A Route 8, Maite, Guam 96910.

(6) Real Estate Properties Transferred by Government of Guam

The Government of Guam, pursuant to Public Law 23-119, assigned to GWA various real estate properties under GWA's administration. As of September 30, 2007 and 2006, the properties have not been recognized in the financial statements pending completion of formal transfer proceedings.

(7) Agreements with the United States Navy

Pursuant to a Memorandum of Agreement, the United States Navy supplies water through its water system to GWA for distribution and resale to non-military customers. Total purchases from the U.S. Navy for the years ended September 30, 2007 and 2006 are \$2,810,612 and \$4,135,573, respectively.

(8) Commitments and Contingencies

Claims

Due to the nature of its operations, GWA is subject to various claims by private and governmental customers and vendors for various alleged losses. Because an estimate of the amount or range of potential loss cannot be determined at this time, no provision for any liability that may result from such claims has been made in the financial statements.

Self Insurance

GWA has adopted a policy of self-insuring potential risks relative to its property, plant and equipment. GWA has not purchased insurance relative to its property, plant and equipment, and no other risks are insured. GWA is of the opinion that it has suffered no material losses in the past three years related to damages to its utility plant-in-service.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(8) Commitments and Contingencies, Continued

Contract Commitments

Contract commitments in connection with projects currently in construction approximate \$28,987,615 at September 30, 2007.

Project Management Contracts

On December 5, 2006, GWA entered into Performance Management Contracts (PMC) with a Company for the operation and maintenance of its Wastewater Treatment Plants, Collection System, and Lift Stations. PMC contracts are for a period of 3 years.

At September 30, 2007, the minimum management fees for the PMC above are as follows:

Year ending September 30,	Amount
2008	\$ 991,605
2009	1,019,370
2010	<u>256,590</u>
	<u>\$ 2,267,565</u>

The above fees are subject to certain incentives and penalties, as agreed by both parties.

Medicare

The Government of Guam and its component units, including GWA, began withholding and remitting funds to the U.S. Social Security System for the health insurance component of its salaries and wages effective October 1998. Prior to that date, the Government of Guam did not withhold or remit Medicare payments to the U.S. Social Security System. If the Government is found to be liable for Medicare payments on salaries and wages prior to October 1998, an indeterminate liability could result. It has been the practice of GWA and all other component units of the Government of Guam that payment of this health insurance component is optional prior to October 1998. Therefore, no liability for any amount which may ultimately arise from this matter has been recorded in the accompanying financial statements.

Single Audit Questioned Costs

GWA undergoes annual compliance audits to satisfy federal grantor requirements. Cumulative questioned costs of \$445,931 exist from these audits as of September 30, 2007. The questioned costs will be resolved by the applicable grantor and due to GWA's inability to predict the ultimate outcome of this matter, no provision for any liability, if any, that may result from this matter has been made in the accompanying financial statements.

Stipulated Order

In or about December 2002, the United States Government filed a complaint against the Guam Waterworks Authority and the Government of Guam for alleged violations under the Federal Clean Water Act (CWA) and the Safe Drinking Water Act (SDWA). Because of GWA's non-compliance with the National Primary Drinking Water Regulations, the U.S. Government is seeking both civil penalties and injunctive relief to address such non-compliance. Both GWA and the U.S. Government of Justice, Environmental and Natural Resources Division mutually agreed in the form of Stipulated Order to resolve the violation issues.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(8) Commitments and Contingencies, Continued

Stipulated Order, Continued

On June 5, 2003, Stipulated Order for Preliminary Relief was filed before the District Court of Guam. The Stipulation requires implementation of short-term projects and initial planning measures by GWA. GWA is required to submit a final financial plan in the Master Plan that generates sufficient revenue to cover the cost of all compliance activities and deliverables required by the Stipulated Order for Preliminary Relief, as well as any other anticipated expenses, including any measures necessary to ensure compliance with the CWA and the SDWA and costs related to the infrastructure improvements identified in the Master Plan.

(9) Cash and Cash Equivalents and Investments

The bond indenture agreements for the 2005 series revenue bonds (note 4) require the establishment of special funds to be held and administered by trustees and by GWA. In addition, proceeds from borrowings to fund capital improvements are maintained by GWA in construction accounts. Funds in these accounts are required by loan agreement or public law to be used to fund capital improvements.

At September 30, 2007 and 2006, investments and cash held by trustees and by GWA in these funds and accounts are as follows:

	2007		Total
	Held By Trustee	Held By GWA	
	Bond Indenture Funds	Bond Indenture Funds	
Unrestricted:			
Revenue funds	\$ -	\$ 3,627,054	\$ 3,627,054
Operations and maintenance funds	-	24,196	24,196
Restricted:			
Operations, maintenance renewal and replacement funds	-	1,320,290	1,320,290
Rate stabilization fund	-	888,441	888,441
Cost of issuance fund	-	37,413	37,413
Construction fund	-	46,886,832	46,886,832
Investment:			
Reserve fund	7,685,596	-	7,685,596
Debt service fund	<u>1,932,412</u>	<u>-</u>	<u>1,932,412</u>
	<u>\$ 9,618,008</u>	<u>\$ 52,784,226</u>	<u>\$ 62,402,234</u>

	2006		Total
	Held By Trustee	Held By GWA	
	Bond Indenture Funds	Bond Indenture Funds	
Unrestricted:			
Revenue funds	\$ -	\$ 1,315,923	\$ 1,315,923
Operations and maintenance funds	-	133,222	133,222
Restricted:			
Operations, maintenance renewal and replacement funds	-	1,136,357	1,136,357
Rate stabilization fund	-	902,246	902,246
Cost of issuance fund	-	35,641	35,641
Construction fund	-	67,896,169	67,896,169

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(9) Cash and Cash Equivalents and Investments, Continued

	2006		<u>Total</u>
	Held By Trustee	Held By GWA	
	Bond Indenture Funds	Bond Indenture Funds	
Investment:			
Reserve fund	7,768,966	-	7,768,966
Debt service fund	956	-	956
	<u>\$ 7,769,922</u>	<u>\$ 71,419,558</u>	<u>\$ 79,189,480</u>

At September 30, 2007 and 2006, investments in debt securities are carried at cost or amortized cost which approximates market value including accrued interest for debt securities.

The deposits and investment policies of GWA are governed by 14 GCA 12, *Investments and Deposits* in conjunction with applicable bond indentures. Authorized investments include obligations issued or guaranteed by the U.S. government or agencies of the U.S. government; bonds, notes or other indebtedness rated in the highest rating by Moody's Investors Service (Moody's) or Standard & Poor's Corporation (S&P); obligations issued by the Federated Government obligations Fund SS or the Transamerica Accidental Life Insurance Company with remaining maturities of not more than three years; any bonds or other obligations of any state of the U.S. or any agency, instrumentality or local government unit of such state which are rated in the highest rating category of either Moody's or S&P; demand and time deposits in or certificates of deposit or bankers acceptances with U.S. domestic banks which have a rating of their short term certificates of deposit of A-1 or better by S&P and P-1 by Moody's and mature no more than 360 days after purchase; commercial paper which is rating in the highest classification by S&P and Moody's; and money market funds rated AAAM or better by S&P.

A. Cash

GASB Statement No. 3 requires government entities to categorize investments to give an indication of the level of credit risk assumed by the entity at year-end. The three categories are described below:

Category 1 Insured or registered, or securities held by GWA or its agent in GWA's name;

Category 2 Uninsured and unregistered, with securities held by the broker's or dealer's trust department or agent in GWA's name; or

Category 3 Uninsured and unregistered, with securities held by the broker or dealer, or by its trust department or agent but not in GWA's name.

GASB Statement No. 40 amended GASB Statement No. 3 to eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, GWA'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. GWA does not have a deposit policy for custodial credit risk.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(9) Cash and Cash Equivalents and Investments, Continued

A. Cash, Continued

Bank balances of demand and time deposit accounts held in the name of GWA totaled \$56,224,739 and \$75,202,871 as of September 30, 2007 and 2006, respectively, of which \$242,547 and \$437,590 were insured by the Federal Deposit Insurance Corporation and the remaining balances were uninsured and uncollateralized. Restricted cash on hand consists of cash received for specific capital projects and for bond indenture related accounts.

Current restricted cash amounted to \$975,798 and \$3,034,766 as of September 30, 2007 and 2006, respectively. The noncurrent restricted cash amounted to \$49,132,976 and \$69,970,413 as of September 30, 2007 and 2006, respectively.

The composition of current and noncurrent restricted cash is as follows:

	<u>2007</u>	<u>2006</u>
Current restricted:		
Capital projects	\$ 169,557	\$ 167,440
Operation and maintenance	394,534	1,641,717
PUC surcharge	56,401	56,120
Navy surcharge	355,306	188,280
Meter reserve	-	6,877
TCD	-	974,332
	<u>975,798</u>	<u>3,034,766</u>
Noncurrent restricted:		
Operations, maintenance, renewal and replacement	1,320,290	1,136,357
Rate stabilization	888,441	902,246
Cost of issuance	37,413	35,640
Construction fund	<u>46,886,832</u>	<u>67,896,170</u>
	<u>49,132,976</u>	<u>69,970,413</u>
Total restricted cash	\$ <u>50,108,774</u>	\$ <u>73,005,179</u>

B. Investments

GASB Statement No. 3 previously required government entities to present investment risks in terms of whether the investments fell into the following categories:

- Category 1 Investments that are insured or registered, or securities held by GWA or its agent in GWA's name;
- Category 2 Investments that are uninsured and unregistered for which the securities are held by the counterparty's trust department or agent in GWA's name; or
- Category 3 Investments that are uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in GWA's name.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(9) Cash and Cash Equivalents and Investments, Continued

B. Investments, Continued

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No. 3.

As of September 30, 2007 and 2006, the GWA's fixed income securities had the following maturities:

<u>Investment Type</u>	<u>2007</u>		
	<u>Investment Maturities (in years)</u>		
	<u>Fair Value</u>	<u>Less than 1</u>	<u>1-5</u>
U.S. Treasury obligations	\$ <u>9,618,008</u>	\$ <u>7,087,058</u>	\$ <u>2,530,950</u>

<u>Investment Type</u>	<u>2006</u>		
	<u>Investment Maturities (in years)</u>		
	<u>Fair Value</u>	<u>Less than 1</u>	<u>1-5</u>
U.S. Treasury obligations	\$ <u>7,769,922</u>	\$ <u>2,708,370</u>	\$ <u>5,061,552</u>

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

GWA's exposure to credit risk at September 30, 2007 and 2006 as follow:

<u>Moody's Rating</u>	<u>2007</u>		
	<u>Total</u>	<u>Domestic</u>	<u>International</u>
Aaa	\$ <u>9,618,008</u>	\$ <u>9,618,008</u>	\$ <u>-</u>
Total credit risk debt securities	\$ <u>9,618,008</u>	\$ <u>9,618,008</u>	\$ <u>-</u>

<u>Moody's Rating</u>	<u>2006</u>		
	<u>Total</u>	<u>Domestic</u>	<u>International</u>
Aaa	\$ <u>7,769,922</u>	\$ <u>7,769,922</u>	\$ <u>-</u>
Total credit risk debt securities	\$ <u>7,769,922</u>	\$ <u>7,769,922</u>	\$ <u>-</u>

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(9) Cash and Cash Equivalents and Investments, Continued

B. Investments, Continued

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, GWA will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. GWA's investments are held and administered by trustees. Accordingly, these investments are exposed to custodial credit risk. Based on negotiated trust and custody contracts, all of these investments were held in GWA's name by GWA's custodial financial institutions at September 30, 2007 and 2006.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for GWA. As of September 30, 2007 and 2006, GWA's investment in agency obligations of US Treasury agency obligations constituted 53% and 98%, respectively, of its total investments.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. GWA does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

(10) Other Matters

On December 31, 1989, the Government of Guam issued general obligation Water System Revenue Bonds, Series 1989, in the amount of \$49,190,000. The bonds have been issued for the purpose of expanding and improving the existing water system of the Government operated by GWA. The bond obligation is recognized on the books of the Government of Guam and is not reflected as a liability of GWA.

(11) New Accounting Principles

During fiscal year 2007, the Authority implemented GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. GASB Statement No. 43 establishes uniform financial reporting for other postemployment benefit plans by state and local governments. The implementation of this Statement did not have a material effect on the financial statements of GWA.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. GASB Statement No. 45 establishes standards for the measurement, recognition, and display of other postemployment benefit expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. The provisions of this Statement are effective for periods beginning after December 15, 2006. The effect, if any, of the implementation of this Statement on the financial statements of GWA has not been determined.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(11) New Accounting Principles, Continued

In September 2006, GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfer of Assets and Future Revenues*. GASB Statement No. 48 establishes criteria that governments will use to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing. The Statement also includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. The provisions of this Statement are effective for periods beginning after December 15, 2006. Management does not believe that the implementation of this Statement will have a material effect on the financial statements of GWA.

In December 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. GASB Statement No. 49 provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation. The provisions of this Statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this Statement will have a material effect on the financial statements of GWA.

In May 2007, GASB issued Statement No. 50, *Pension Disclosures an Amendment of GASB Statements No. 25 and 27*. GASB Statement No. 50 more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits. The provisions of this Statement are effective for periods beginning after June 15, 2007. Management does not believe that the implementation of this Statement will have a material effect on the financial statements of GWA.

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. GASB Statement No. 51 addresses whether and when intangible assets should be considered capital assets for financial reporting purposes. The provisions of this Statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this Statement will have a material effect on the financial statements of GWA.

(12) Contributions Received

Contributions received by GWA during the years ended September 30, 2007 and 2006, are as follows:

	<u>2007</u>	<u>2006</u>
Grants from U.S. Government:		
Received from the U.S. Environmental Protection Agency	\$ 1,656,861	\$ 903,874
Received from the U.S. Federal Emergency Management Agency, net of returns	<u> -</u>	<u>(54,667)</u>
	<u>\$ 1,656,861</u>	<u>\$ 849,207</u>
Other contributions:		
Proceeds received through refinancing of Government of Guam's Water Bond	<u>\$ -</u>	<u>\$ 300,000</u>

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2007 and 2006

(13) Accrued Supplemental/COLA Annuities

As required by Public Law 26-35, as amended by Public Law 26-49 and 27-29 thereafter, GWA must pay to the Government of Guam Retirement Fund certain supplemental benefits paid to retirees. The supplemental benefits derive from an annual appropriation by the Guam Legislature and do not relate to covered Plan benefits. GWA's regulator has determined that payment of this liability will not be a recoverable cost. GWA has not been able to initiate litigation to resolve this matter. Therefore, GWA is currently unable to predict when the accrued balance will be paid.

The accrued balance at September 30, 2007 and 2006 is \$1,696,208 and \$1,630,795, respectively.

(14) PUC Surcharge

The Public Utilities Commission ordered an 11.5% regulatory surcharge effective for meters read after October 1, 2001, to enable GWA to retire its obligations to both Guam Power Authority (GPA) and the Guam Telephone Authority (GTA). The order stipulated that monthly payments be made to both GPA and GTA. Payments to GPA should be no less than \$75,000 per month, after the required \$50,000 payment to GTA, payment of the PUC's annual administrative assessments and payment of PUC invoices in excess of 60 days.

On May 9, 2002, the Guam Legislature passed Public Law 26-81. The Law established a one-year moratorium of the 11.5% surcharge, wherein GWA was prohibited for the moratorium period from any further billings of the surcharge. Additionally, in order for GWA to pay its debt to GPA, the law appropriated \$2.75 million to GWA from a bond re-financing. In May 2003, the one year moratorium expired and proceeds from the renewed surcharge of 8.03% have gone toward GWA's obligation to GPA and effective October 2003, also to the obligation to the U.S. Navy. In addition, proceeds from a surcharge of 3.49% are earmarked to pay benefits for GWA's supplemental annuity for retirees.

(15) Related Party Transactions

GWA receives electrical and administrative services from Guam Power Authority (GPA), a component unit of the Government of Guam also governed by the CCU. Electricity purchases from GPA for the years ended September 30, 2007 and 2006 were \$11,914,539 and \$10,521,173, respectively, and GWA was also charged \$529,442 and \$336,626, respectively, for administrative services provided by GPA. In addition, GWA has long-term debt of \$7,504,734 and \$9,762,654 due to GPA at September 30, 2007 and 2006, respectively (see note 4).

(16) Subsequent Events

GWA was engaged in a dispute with a customer concerning a water connection. The disputed charges could not be determined as of September 30, 2007, thus no adjustment has been recorded in the accompanying financial statements. On October 31, 2007, GWA negotiated and settled the dispute for receipts of \$1,110,300.

GUAM WATERWORKS AUTHORITY

Schedule 1
 Schedule of Equalization of Net (Income) Loss
 Years Ended September 30, 1991 through 2007

	2007	2006	2005	2004	2003 (As Restated)	2002	2001	2000	1999	1998 (1)	1997 (1)	1996 (1)	1995 (1)	1994 (1)	1993 (1)	1992 (1)	1991 (1)
Net (income) loss	\$ 1,933,050	\$ 8,097,395	\$ (1,530,194)	\$ 1,809,232	\$ 7,402,223	\$ 14,712,887	\$ 639,033	\$ 9,930,509	\$ 9,756,403	\$ 20,589,668	\$ 12,002,404	\$ 2,486,481	\$ 7,293,467	\$ 10,920,041	\$ 3,069,762	\$ 4,394,359	\$ 1,744,519
Less transfers from GovGuam	-	300,000	1,110,561	578,754	748,109	2,859,524	2,800,388	-	-	-	-	18,538,800	22,743,010	16,136,274	24,959,972	27,447,270	22,064,351
Less other operating revenues recognized in 1999 attributable to prior years	-	-	-	-	-	-	-	-	4,282,966	-	-	-	-	-	-	-	-
Effect of unfunded pension liability	(749,533)	(1,283,136)	183,164	(1,900,563)	(1,263,158)	77,489	(52,940)	(155,899)	927,990	437,109	(3,516,573)	3,926,422	5,053	(278,750)	(784,801)	(1,478,412)	(1,389,512)
Equalization of net (income) loss	\$ 1,183,517	\$ 7,114,259	\$ (236,469)	\$ 487,423	\$ 6,887,174	\$ 17,649,900	\$ 3,386,481	\$ 9,774,610	\$ 14,967,359	\$ 21,026,777	\$ 8,485,831	\$ 24,951,703	\$ 30,041,530	\$ 26,777,565	\$ 27,244,933	\$ 30,363,217	\$ 22,419,358

(1) This information is extracted from prior Government of Guam general-purpose financial statements.

See accompanying independent auditors' report.

GUAM WATERWORKS AUTHORITY

Schedule 2

Schedule of Certain Operating and Maintenance Expenses
Years Ended September 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Salaries, wages and benefits:		
Regular, differential and hazardous pay	\$ 9,411,521	\$ 8,988,945
Pension costs	4,007,731	4,418,624
Overtime pay	867,270	940,009
Sick leave	311,524	123,189
	<u>14,598,046</u>	<u>14,470,767</u>
Total salaries, wages and benefits	\$ 14,598,046	\$ 14,470,767
Employees at end of year	251	245
Administrative and general:		
Materials and supplies	\$ 2,288,907	\$ 2,601,892
Chemicals	1,000,799	581,654
Transportation	539,045	440,001
Public Utility Commission	199,186	291,397
Training	279,265	241,368
Violation fees	40,000	144,000
Communications	170,864	105,008
Liability claims	266,577	101,879
Advertising	171,550	65,389
Miscellaneous	206,258	125,270
	<u>5,162,451</u>	<u>4,697,858</u>
Total administrative and general	\$ 5,162,451	\$ 4,697,858
Contractual:		
Labor, materials and others	\$ 1,733,461	\$ 2,165,523
Equipment rental	743,860	1,029,483
Accounting	809,615	473,223
Testing	126,054	287,232
PMC management	728,407	-
Legal	-	972
	<u>4,141,397</u>	<u>3,956,433</u>
Total contractual	\$ 4,141,397	\$ 3,956,433
Other expense:		
Privatization	\$ -	\$ 895
Loss on inventory write-down	614,161	-
Loss on asset disposal	15,476	-
Interest expense	6,266,080	5,577,844
Supplemental annuity benefits	464,620	473,252
Other	68,262	1,492,448
	<u>7,428,599</u>	<u>7,544,439</u>
Total other expense	\$ 7,428,599	\$ 7,544,439

See accompanying independent auditors' report.

GUAM WATERWORKS AUTHORITY

Schedule 3

Schedule of Cash Flows Indicating Financing Method
Year Ended September 30, 2007

Cash flows provided by operating activities	\$ 8,070,881
Cash flows used for acquisition of utility plant, net of contributed capital received	<u>(19,471,769)</u>
Cash flows if GPA were fully paid and if utility plant were built, net of contributed capital received	<u>\$ (11,400,888)</u>

See accompanying independent auditors' report.

GUAM WATERWORKS AUTHORITY

Schedule 4
 Schedule of Construction Work in Progress
 Year Ended September 30, 2007

Project Title	Type	Ending Balance 2006	Additions and Transfers	Closed out during FY2007	Ending Balance 2007
Agat/Santa Rita Sewer System	Wastewater	\$ 418,504	\$ 888,158	\$ (327,724)	\$ 978,938
Ordot/Chalan Pago 2B	Wastewater	622,342	-	-	622,342
Watershed Master Plan	Water	6,152,488	810,634	(6,963,122)	-
Automated Meter Reading	Water	8,662,553	7,020,563	(8,095,089)	7,588,027
Distribution Line Replacement	Water	1,617,510	2,428,554	-	4,046,064
Hagatna Sewage Treatment Plant	Wastewater	5,003,377	6,107,528	(11,110,905)	-
Hagatna and Northern District	Wastewater	-	5,585,642	-	5,585,642
All Others	Water/Wastewater	4,238,304	2,091,634	(2,420,639)	3,909,299
		<u>\$ 26,715,078</u>	<u>\$ 24,932,713</u>	<u>\$ (28,917,479)</u>	<u>\$ 22,730,312</u>

See accompanying independent auditors' report.

GUAM WATERWORKS AUTHORITY

Schedule 5

Schedule of Employee and Other Data

Year Ended September 30, 2007

Department	PL 28-150 Sec 45:a Full-Time Employees	PL 28-150 Sec 45:b Category Personnel Services	Contractual Services	Materials and Supplies	Total
Board	-	\$ -	\$ 37,550	\$ 849	\$ 38,399
Administration	72	4,985,648	967,003	177,976	6,130,627
Accounting	17	755,717	176,053	227,000	1,158,770
Engineering	10	630,443	126,026	22,106	778,575
Collection and Distribution	93	5,622,427	2,519,201	1,238,402	9,380,030
Production and Treatment	59	3,068,431	315,564	622,574	4,006,569
Total	<u>251</u>	<u>\$ 15,062,666</u>	<u>\$ 4,141,397</u>	<u>\$ 2,288,907</u>	<u>\$ 21,492,970</u>