

GUAM WATERWORKS AUTHORITY

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

YEARS ENDED SEPTEMBER 30, 2006 AND 2005

INDEPENDENT AUDITORS' REPORT

Consolidated Commission on Utilities:

We have audited the accompanying statements of net assets of Guam Waterworks Authority (GWA), a component unit of the Government of Guam, as of September 30, 2006 and 2005, and the related statements of revenues, expenses and changes in net assets and 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.

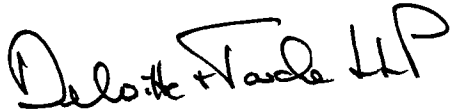
We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan 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 Guam Waterworks Authority as of September 30, 2006 and 2005, 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 1-3 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 measurements and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audits of the financial statements for the years ended September 30, 2006 and 2005, were made for the purpose of expressing our opinion on the basic financial statements taken as a whole. The accompanying schedules on pages 25-29 are presented for purposes of additional analysis. These schedules are the responsibility of GWA's management. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and in our opinion, except for the information presented in Schedule 1 (page 25) upon which we express no assurance, is fairly stated in all material respects, in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 17, 2007, on our consideration of the Guam Waterworks Authority's internal control over financial reporting and 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.

A handwritten signature in black ink that reads "Deloitte Touche LLP". The signature is written in a cursive, stylized font.

May 17, 2007

GUAM WATERWORKS AUTHORITY

Management's Discussion and Analysis
September 30, 2006 and 2005

Management Discussion & Analysis

The major accomplishment for Guam Waterworks Authority (GWA) was the receipt of a Ba2 bond rating from Moody's Investors Service, Inc. and BB rating from Fitch, Inc. Although not investment grade ratings, they represent the acknowledgement from credit agencies of the substantial improvements that have been made at the utility in the last few years. This also marked the first time that GWA received a bond rating from a nationally recognized credit rating agency. These ratings enabled GWA to be in a position to issue bonds. In December 2005, GWA completed an issuance of \$101,175,000 in bonds.

The utility has gone right to work at spending the proceeds of the bond issuance. At present, nearly 75% of the bond funds are encumbered and 50% of the funds have been spent.

Master Plan

During the year, GWA's master plan was completed. The purpose of the master plan is to serve as a roadmap for the GWA's capital program for the next 20 years. The master plan identified nearly \$900 million in capital improvements being recommended at the utility. GWA will continue to study and evaluate the recommendations of the master plan and will work to determine the best way to move forward in improving service to GWA's customers.

Rate Increases

Shortly after the bond issuance, GWA entered into a stipulation for a 3% rate increase with the Public Utilities Commission (PUC). GWA had originally petitioned for an 8% increase, however, because the master plan (including the final financial plan) was so near completion and so much more information would be available in the near future, the parties agreed that a smaller increase should be sought immediately. GWA currently has a petition before the PUC for a 14.24% rate increase. The petition should be heard in May 2007.

Performance Management Contract

During the year the Consolidated Commission on Utilities determined that GWA may need an additional resource to meet all of the challenges ahead. There are a great number of capital improvements to be constructed, troubleshooting of system deficiencies, creation of standard operating procedures and substantial employee training that needs to take place. In order to assist GWA in meeting these requirements, the CCU authorized the issuance of a bid for a wastewater operator to enter into a performance management contract with the Authority. On January 1, 2007, Veolia Guam LLC assumed responsibility for the management of GWA's wastewater system. The contract term is three years with an option to extend for one additional three year period.

Automated Meter Reading Project

GWA is continuing with the project to install radio read meters for all its customers. The purpose of the project was to help GWA correct some long standing problems with its revenue control including the ability to obtain consistent readings and problems in locating meters in areas that have become overgrown with vegetation. Additionally, GWA also believed that the incremental revenues gained from more accurate readings would offset the costs of the program. To date, the incremental revenues have not materialized. GWA is projecting the completion of the installation to occur in early 2008.

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Management's Discussion and Analysis
September 30, 2006 and 2005

Well Acquisition

During the year, GWA was able to successfully negotiate the buyout of 10 wells which had been operated by a private operator. GWA determined that the wells could be operated at less cost by in-house staff. This change has resulted in a decreased cost of purchased water during the last year.

Summary of Financial Condition-Comparative Analysis

	<u>FY2006</u>	<u>FY2005</u>	<u>FY2004</u>
Assets:			
Cash	\$ 83,143,734	\$ 21,244,790	\$ 4,231,807
Receivables, net	7,705,974	9,869,946	8,404,461
Other assets	5,399,633	3,306,621	2,195,576
Plant in service, net	<u>239,602,789</u>	<u>220,166,031</u>	<u>221,668,469</u>
Total Assets	\$ <u>335,852,130</u>	\$ <u>254,587,388</u>	\$ <u>236,500,313</u>
Liabilities:			
Current liabilities	\$ 16,877,252	\$ 15,745,413	\$ 12,291,754
Long term liabilities	<u>126,329,236</u>	<u>38,098,938</u>	<u>24,995,716</u>
	<u>143,206,488</u>	<u>53,844,351</u>	<u>37,287,470</u>
Net Assets	<u>192,645,642</u>	<u>200,743,037</u>	<u>199,212,843</u>
Total Liabilities and Net Assets	\$ <u>335,852,130</u>	\$ <u>254,587,388</u>	\$ <u>236,500,313</u>
Operating revenues	\$ 41,413,300	\$ 42,269,166	\$ 38,840,590
Operating expenses	48,039,113	42,680,281	42,248,398
Non-operating revenues, net	<u>(1,471,582)</u>	<u>1,941,309</u>	<u>1,598,576</u>
(Decrease) increase in net assets	\$ <u>(8,097,395)</u>	\$ <u>1,530,194</u>	\$ <u>(1,809,232)</u>

Analysis of Changes

The change in cash is primarily explained by the acquisition fund for the meter financing in FY2005 and the bond construction fund and other related funds in FY2006.

The change in receivables is mostly explained by a meter reading problem that was occurring at the end of FY2006.

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Management's Discussion and Analysis September 30, 2006 and 2005

Other assets increased as a result of the amortization of certain bond related costs.

The growth in plant in service is the result of the construction that is taking place at the utility.

Current liabilities are growing as a result of the increased construction activity taking place.

Long term liability growth is explained by the increased debt taken on by GWA in the last two years.

The changes in revenues are resulting from a combination of the impact of rate increases, GWA's continued efforts to improve the accuracy of the accounting for its revenues, and possibly some efforts by some of GWA's customers to fix leaks now that GWA is installing meters that track daily water usage.

The changes in expenses are due to a nearly \$2 million increase in power costs resulting from higher oil prices, a \$1.5 million increase in salaries and wages as GWA has been bringing in some additional highly skilled employees, and nearly \$3.5 million in increases to contracts and administrative and general expenses which result from the improved performance of the utility. An example of this last item is that GWA is improving its ability to respond to customer complaints of water leaks, wastewater leaks, etc. However, the increased responsiveness means that GWA must utilize more contractors to complete road repairs after the fix is made.

Management's Discussion and Analysis for the years ended September 30, 2005 and 2004, is set forth in GWA's report on the audit of the financial statements, which is dated April 13, 2006, and that Discussion and Analysis explains the major factors impacting the 2005 and 2004 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, 2006 and 2005

<u>ASSETS</u>	<u>2006</u>	<u>2005</u>
Current assets:		
Cash:		
Unrestricted	\$ 2,368,633	\$ 1,566,433
Restricted	3,034,766	4,145,701
Accounts receivable, net	7,705,974	9,869,946
Materials and supplies inventory, net of allowance for obsolescence of \$380,425 at September 30, 2006 and 2005	2,294,529	1,883,465
Current portion of other assets	63,030	-
Total current assets	<u>15,466,932</u>	<u>17,465,545</u>
Property, plant and equipment:		
Utility plant in service:		
Water system	206,765,134	200,595,049
Wastewater system	178,016,326	173,861,945
Non-utility property	15,135,570	14,588,842
Construction work in progress	26,715,078	8,773,879
	426,632,108	397,819,715
Less accumulated depreciation	<u>(187,029,319)</u>	<u>(177,653,684)</u>
Property, plant and equipment, net	<u>239,602,789</u>	<u>220,166,031</u>
Other noncurrent assets:		
Restricted cash	69,970,413	15,532,656
Investments	7,769,922	-
Other assets, net of current portion	3,042,074	1,423,156
Total other non current assets	<u>80,782,409</u>	<u>16,955,812</u>
	<u>\$ 335,852,130</u>	<u>\$ 254,587,388</u>

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Statements of Net Assets, Continued
September 30, 2006 and 2005

<u>LIABILITIES AND NET ASSETS</u>	<u>2006</u>	<u>2005</u>
Current liabilities:		
Current maturities of long-term debt	\$ 2,631,707	\$ 2,651,519
Accounts payable:		
United States Navy	283,213	446,389
Guam Power Authority	3,072,659	2,633,062
Trade	3,920,272	4,825,413
Accrued payroll and employee benefits	540,257	432,869
Current portion of employee annual leave	348,463	327,889
Accrued supplemental/COLA annuities	1,630,795	1,976,175
Deferred revenue	1,289,050	457,850
Payable to contractors	1,355,104	249,790
Customer deposits	1,805,732	1,744,457
Total current liabilities	<u>16,877,252</u>	<u>15,745,413</u>
Long-term debt, less current maturities:		
Long-term debt	104,679,397	15,292,641
Guam Power Authority	7,587,764	9,640,101
United States Navy	7,102,685	7,561,820
Employee annual leave, less current portion	719,844	612,047
Retirement fund deferred contributions	5,476,855	4,193,719
DCRS sick leave liability	455,105	331,916
Advances for construction	165,435	164,542
Other liabilities	142,151	302,152
Total liabilities	<u>143,206,488</u>	<u>53,844,351</u>
Commitments and contingencies		
Net assets:		
Invested in capital assets, net of related debt	216,460,775	218,981,314
Restricted	3,034,766	4,145,701
Unrestricted	<u>(26,849,899)</u>	<u>(22,383,978)</u>
Total net assets	<u>192,645,642</u>	<u>200,743,037</u>
	<u>\$ 335,852,130</u>	<u>\$ 254,587,388</u>

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Operating revenues:		
Water:		
Private	\$ 27,712,439	\$ 28,413,600
Government	1,782,649	1,833,874
	<u>29,495,088</u>	<u>30,247,474</u>
Wastewater:		
Private	11,757,592	10,729,420
Government	2,874,001	3,155,729
	<u>14,631,593</u>	<u>13,885,149</u>
Other	<u>474,872</u>	<u>273,373</u>
Bad debt expense:		
Bad debt	(3,214,713)	(3,282,341)
Recovery	26,460	1,145,511
	<u>(3,188,253)</u>	<u>(2,136,830)</u>
Total operating revenues	<u>41,413,300</u>	<u>42,269,166</u>
Operating and maintenance expenses:		
Power purchases	10,521,173	8,820,481
Water purchases	5,017,247	6,368,221
	<u>15,538,420</u>	<u>15,188,702</u>
Salaries and wages	14,470,767	11,590,367
Depreciation	9,375,635	9,425,507
Administrative and general	4,697,858	4,148,100
Contractual	3,956,433	2,327,605
	<u>48,039,113</u>	<u>42,680,281</u>
Total operating and maintenance expenses	<u>48,039,113</u>	<u>42,680,281</u>
Operating loss	<u>(6,625,813)</u>	<u>(411,115)</u>
Other income (expense):		
Allowance for funds used during construction	1,368,485	222,250
Interest income	3,209,683	29,668
Interest expense	(5,577,844)	(353,613)
Other expense	(1,493,343)	(1,549,307)
Other income	345,482	68,195
Supplemental/COLA annuities	(473,252)	(503,822)
	<u>(2,620,789)</u>	<u>(2,086,629)</u>
Total other expense, net	<u>(2,620,789)</u>	<u>(2,086,629)</u>
Loss before capital contributions	<u>(9,246,602)</u>	<u>(2,497,744)</u>
Capital contributions:		
Grants from U.S. Government	849,207	2,917,377
Other contributions	300,000	1,110,561
	<u>1,149,207</u>	<u>4,027,938</u>
Total capital contributions	<u>1,149,207</u>	<u>4,027,938</u>
Changes in net assets	<u>(8,097,395)</u>	<u>1,530,194</u>
Net assets at beginning of year	<u>200,743,037</u>	<u>199,212,843</u>
Net assets at end of year	\$ <u>192,645,642</u>	\$ <u>200,743,037</u>

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Statements of Cash Flows
Years Ended September 30, 2006 and 2005

	2006	2005
<u>Increase (decrease) in cash</u>		
Cash flows from operating activities:		
Cash received from customers	\$ 43,103,178	\$ 41,349,501
Cash payments to suppliers for goods and services	(22,313,116)	(21,099,168)
Cash payments to employees for services	(13,174,063)	(11,023,621)
Net cash provided by operating activities	7,615,999	9,226,712
Cash flows from capital and related financing activities:		
Contributed capital received	1,649,208	4,027,938
Acquisition of utility plant	(28,811,499)	(7,922,444)
Proceeds from long-term debt	104,679,397	15,385,845
Repayments of long-term debt	(17,823,926)	(2,180,217)
Interest paid	(5,577,844)	(353,613)
Bond issuance cost	(3,042,074)	(1,423,156)
Net cash provided by capital and related financing activities	51,073,262	7,534,353
Cash flows from investing activities:		
Transfers to restricted funds	(61,096,744)	(19,513,228)
Interest income received	3,209,683	251,918
Net cash used in investing activities	(57,887,061)	(19,261,310)
Net change in unrestricted cash	802,200	(2,500,245)
Unrestricted cash at beginning of year	1,566,433	4,066,678
Unrestricted cash at end of year	\$ 2,368,633	\$ 1,566,433
Supplemental information on noncash financing activities:		
Reduction of other assets and increase in other expense	\$ 1,423,156	\$ -

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Statements of Cash Flows, Continued
Years Ended September 30, 2006 and 2005

	2006	2005
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (6,625,813)	\$ (411,115)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	9,375,635	9,425,507
Bad debt expense	3,214,713	3,282,341
Other expense	670,528	(1,984,934)
(Increase) decrease in assets:		
Accounts receivable	(1,050,741)	(4,747,827)
Materials and supplies inventory	(411,064)	258,381
Other assets	(63,030)	53,730
Increase (decrease) in liabilities:		
Accounts payable	1,307,794	2,248,021
Accrued payroll	424,457	840,784
Employees' annual leave	(188,697)	(609,545)
Accrued supplemental/COLA annuities	(345,381)	503,822
Customer deposits	61,275	233,711
Other liabilities	(160,002)	302,152
Retirement fund deferred contributions	1,283,136	(183,164)
DCRS sick leave liability	123,189	14,848
Net cash provided by operating activities	\$ 7,615,999	\$ 9,226,712

See accompanying notes to financial statements.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(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 statements 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, reduced by outstanding debt net of debt service reserve. 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, 2006 and 2005

(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.

Accrued Annual Leave

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, 2006 and 2005

(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, 2006 and 2005 are \$2,131,804 and \$1,454,696, 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 and \$755,245 for the years ended September 30, 2006 and 2005, respectively. Fire hydrant receivables were \$6,028,271 and \$5,769,251 as of September 30, 2006 and 2005, 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, 2006 and 2005, interest of \$1,368,485 and \$308,476 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, surcharge 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 \$7,047,685 and \$1,951,738 at September 30, 2006 and 2005, respectively.

Reclassifications

Certain balances in the 2005 financial statements have been reclassified to correspond with the 2006 presentation.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(2) Property, Plant and Equipment

	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>
	Beginning Balance October 1, 2004	Transfers and Additions	Transfers and Deletions	Ending Balance September 30, 2005
Utility Plant in Service – Water	\$ 194,823,853	\$ 5,771,196	\$ -	\$ 200,595,049
Utility Plant in Service - Wastewater	174,628,020	363,631	(1,129,706)	173,861,945
General Fixed Assets	16,999,915	829,317	(3,240,390)	14,588,842
Accumulated Depreciation	(168,228,177)	(9,425,507)	-	(177,653,684)
Construction Work in Progress	<u>3,444,858</u>	<u>7,095,858</u>	<u>(1,766,837)</u>	<u>8,773,879</u>
	<u>\$ 221,668,469</u>	<u>\$ 4,634,495</u>	<u>\$ (6,136,933)</u>	<u>\$ 220,166,031</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, 2006 and 2005, are as follows:

	2006	2005
Customers:		
Private	\$ 13,637,773	\$ 12,654,327
Government	<u>8,523,869</u>	<u>8,309,060</u>
	22,161,642	20,963,387
Federal agencies	375,406	451,888
GPA	<u>189,668</u>	<u>260,700</u>
	<u>22,726,716</u>	<u>21,675,975</u>
Less allowance for doubtful receivables:		
Private	(8,101,208)	(5,171,595)
Government	<u>(6,919,534)</u>	<u>(6,634,434)</u>
	<u>(15,020,742)</u>	<u>(11,806,029)</u>
	<u>\$ 7,705,974</u>	<u>\$ 9,869,946</u>

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(3) Accounts Receivable, Continued

Allowance breakdown:		
Beginning balance	\$ (11,806,029)	\$ (18,128,905)
Less:		
Accounts written off during the year	-	8,459,706
Recoveries of bad debts	-	1,145,511
Bad debt expense	<u>(3,214,713)</u>	<u>(3,282,341)</u>
Ending balance	\$ <u>(15,020,742)</u>	\$ <u>(11,806,029)</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, 2006 and 2005 is as follows:

	<u>2006</u>	<u>2005</u>
Note payable to Municipal Services Group, Inc., interest at 5.18%, due in semi-annual installments of principal and interest of \$444,499 through July 15, 2007, \$1,172,054 through July 15, 2015.	\$ -	\$ 15,385,845
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).	7,559,502	8,012,964
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.	9,762,654	11,747,272
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>-</u>
Total long-term debt	118,497,156	35,146,081
Less current maturities	<u>(2,631,707)</u>	<u>(2,651,519)</u>
	115,865,449	32,494,562
Bond premium	<u>3,504,397</u>	<u>-</u>
	\$ <u>119,369,846</u>	\$ <u>32,494,562</u>

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(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 Principal</u>	<u>Interest</u>	<u>Debt Service</u>
2007	\$ 2,631,707	\$ 6,312,871	\$ 8,944,578
2008	5,088,514	6,187,751	11,276,265
2009	5,345,016	5,985,834	11,330,850
2010	6,554,142	5,731,867	12,286,009
2011	4,529,966	5,560,716	10,090,682
2012 through 2016	13,885,311	25,805,872	39,691,183
2017 through 2021	13,793,750	22,246,419	36,040,169
2022 through 2026	18,451,250	17,582,541	36,033,791
2027 through 2031	24,601,250	11,438,258	36,039,508
2032 through 2035	<u>23,616,250</u>	<u>3,416,459</u>	<u>27,032,709</u>
	<u>\$ 118,497,156</u>	<u>\$ 110,268,588</u>	<u>\$ 228,765,744</u>

In January 2006, GWA issued a bond in the amount of \$101,175,000 for the purpose of funding capital improvements to GWA's water and wastewater systems, refinancing certain outstanding obligations of GWA, and financing new water meters. Interest on the bond is payable on January 1 and July 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 the debt to Municipal Services Group, Inc. (MSG) with proceeds from the above debt issuance. As a result, MSG has 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 components of interest income and interest expense, respectively, 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, 2006.

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Notes to Financial Statements September 30, 2006 and 2005

(4) Long-Term Debt, Continued

The following summarizes movements in GWA's non-current liabilities for the years ended September 30, 2006 and 2005:

	Outstanding September 30, <u>2005</u>	<u>Increases</u>	<u>Decreases</u>	Outstanding September 30, <u>2006</u>	<u>Current</u>	<u>Noncurrent</u>
Long-term debt	\$ 15,385,845	\$ 101,175,000	\$ 15,385,845	\$ 101,175,000	\$ -	\$ 101,175,000
Premium on bonds	-	3,604,522	100,125	3,504,397	-	3,504,397
Guam Power Authority	11,747,272	-	1,984,618	9,762,654	2,174,890	7,587,764
U.S. Navy	8,012,964	-	453,462	7,559,502	456,817	7,102,685
Employee annual leave	939,936	128,371	-	1,068,307	348,463	719,844
Retirement fund deferred contributions	4,193,719	1,283,136	-	5,476,855	-	5,476,855
DCRS sick leave liability	331,916	123,189	-	455,105	-	455,105
Other liabilities	<u>466,694</u>	<u>-</u>	<u>159,108</u>	<u>307,586</u>	<u>-</u>	<u>307,586</u>
	<u>\$ 41,078,346</u>	<u>\$ 106,314,218</u>	<u>\$ 18,083,158</u>	<u>\$ 129,309,406</u>	<u>\$ 2,980,170</u>	<u>\$ 126,329,236</u>

	Outstanding September 30, <u>2004</u>	<u>Increases</u>	<u>Decreases</u>	Outstanding September 30, <u>2005</u>	<u>Current</u>	<u>Noncurrent</u>
Long-term debt	\$ -	\$ 15,385,845	\$ -	\$ 15,385,845	\$ 93,204	\$ 15,292,641
Guam Power Authority	13,313,861	-	1,566,589	11,747,272	2,107,171	9,640,101
U.S. Navy	8,626,591	-	613,627	8,012,964	451,144	7,561,820
Employee annual leave	1,045,659	-	105,723	939,936	327,889	612,047
Retirement fund deferred contributions	4,376,883	-	183,164	4,193,719	-	4,193,719
DCRS sick leave liability	317,068	14,848	-	331,916	-	331,916
Other liabilities	<u>163,922</u>	<u>302,772</u>	<u>-</u>	<u>466,694</u>	<u>-</u>	<u>466,694</u>
	<u>\$ 27,843,984</u>	<u>\$ 15,703,465</u>	<u>\$ 2,469,103</u>	<u>\$ 41,078,346</u>	<u>\$ 2,979,408</u>	<u>\$ 38,098,938</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.

As a result of actuarial valuations performed as of September 30, 2004, 2003 and 2002 (applicable to fiscal year 2006, 2005 and 2004, respectively), contribution rates for the years ended September 30, 2006, 2005 and 2004, respectively, have been determined as follows:

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Notes to Financial Statements
September 30, 2006 and 2005

(5) Employees' Retirement Plan, Continued

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Normal costs (% of DB Plan payroll)	17.83%	18.30%	17.66%
Unfunded liability costs (% of total payroll)	<u>21.36%</u>	<u>19.93%</u>	<u>16.23%</u>
	39.19%	38.23%	33.89%
Employee contributions (DB Plan employees)	<u>9.50%</u>	<u>9.50%</u>	<u>9.50%</u>
Government contribution as a % of DB Plan payroll	<u>29.69%</u>	<u>28.73%</u>	<u>24.39%</u>
Government contribution as a % of total payroll	<u>26.00%</u>	<u>24.89%</u>	<u>20.81%</u>

Statutory contribution rates for employer and employee contributions were 21.81% and 9.5% and 20.81% and 9.5%, respectively, of qualifying payroll for the years ended September 30, 2006 and 2005.

The plan utilized the actuarial cost method termed "entry age normal". Significant actuarial assumptions are as follows:

	<u>2004</u> <u>Actuarial Valuation</u>	<u>2003</u> <u>Actuarial Valuation</u>
Interest rate and rate of return	7.0%	7.0%
Payroll increases	3.5%	3.5%
Salary increases	4.0%-8.5%	4.0% - 8.5%

The actuarial valuation performed as of September 30, 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, 2006 and 2005 may be materially different than that recorded in the accompanying financial statements.

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, 2006 and 2005 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.

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 \$455,105 and \$331,916 at September 30, 2006 and 2005, 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.

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Notes to Financial Statements
September 30, 2006 and 2005

(5) Employees' Retirement Plan, Continued

Retirement expense for the years ended September 30, 2006, 2005 and 2004 is as follows:

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Cash contributions and accruals	\$ 3,135,488	\$ 3,091,775	\$ 2,835,588
Increase (decrease) in accrued unfunded liability to the retirement fund	<u>1,283,136</u>	<u>(183,164)</u>	<u>1,900,563</u>
	<u>\$ 4,418,624</u>	<u>\$ 2,908,611</u>	<u>\$ 4,736,151</u>

(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, 2006 and 2005, 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, 2006 and 2005 are \$4,135,573 and \$4,531,722, 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.

Contract Commitments

Contract commitments in connection with projects currently in construction amount to approximately \$7,047,685 at September 30, 2006.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(8) Commitments and Contingencies, Continued

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, 2006. 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.

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 for fund capital improvements.

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Notes to Financial Statements
September 30, 2006 and 2005

(9) Cash and Cash Equivalents and Investments, Continued

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

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

Investments in debt securities are carried at cost or amortized cost which approximates market value at September 30, 2006 include 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

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Notes to Financial Statements
September 30, 2006 and 2005

9) Cash and Cash Equivalents and Investments, Continued

A. Cash, Continued

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.

Bank balances of demand and time deposit accounts held in the name of GWA totaled \$75,202,871 and \$21,010,527 as of September 30, 2006 and 2005, respectively, of which \$437,590 and \$452,570 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 \$3,034,766 and \$4,145,701 as of September 30, 2006 and 2005, respectively. The noncurrent restricted cash amounted to \$69,970,412 and \$15,532,656 as of September 30, 2006 and 2005, respectively.

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

	<u>2006</u>	<u>2005</u>
Current restricted:		
Capital projects	\$ 167,440	\$ 166,067
Operation and maintenance	1,641,717	1,240,985
PUC surcharge	56,120	2,025,482
Navy surcharge	188,280	404,089
Earth Tech	-	252,012
Meter reserve	6,877	6,832
Escrow account	-	50,234
TCD	<u>974,332</u>	<u>-</u>
	<u>3,034,766</u>	<u>4,145,701</u>
Noncurrent restricted:		
Debt service related	-	1,342,087
Capital acquisition related	-	13,246,501
CIP reserve fund	-	944,068
Operations, maintenance, renewal and replacement	1,136,357	-
Rate stabilization	902,246	-
Cost of issuance	35,640	-
Construction fund	<u>67,896,170</u>	<u>-</u>
	<u>69,970,413</u>	<u>15,532,656</u>
Total restricted cash	<u>\$ 73,005,179</u>	<u>\$ 19,678,357</u>

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Notes to Financial Statements
September 30, 2006 and 2005

(9) Cash and Cash Equivalents and Investments, Continued

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 the Administration 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.

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, 2006, the GWA's fixed income securities had the following maturities:

<u>Investment Type</u>	<u>Investment Maturities (in years)</u>		
	<u>Fair Value</u>	<u>Less than 1</u>	<u>1-5</u>
First America Treasury obligation	\$ 176,204	\$ 176,204	\$ -
U.S. Treasury agency obligations	<u>7,593,718</u>	<u>2,532,166</u>	<u>5,061,552</u>
	\$ <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, 2006 as follow:

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

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, 2006.

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Notes to Financial Statements
September 30, 2006 and 2005

(9) Cash and Cash Equivalents and Investments, Continued

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, 2006, GWA's investment in agency obligations of US Treasury agency obligations constituted 98% 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 2006, GWA implemented the following pronouncements:

- GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, which establishes standards for impairment of capital assets when service utility has declined significantly and unexpectedly.
- GASB Statement No. 44, *Economic Condition Reporting: The Statistical Section, an amendment to NCGA Statement 1*, which improves the understandability and usefulness of statistical section information and adds information from the new financial reporting model for state and local governments required by GASB Statement No. 34.
- GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation (an amendment to GASB Statement No. 34)*, which requires that limitations on the use of net assets imposed by enabling legislation be reported as restricted net assets.
- GASB Statement No. 47, *Accounting for Termination of Benefits*, which establishes guidance for state and local governmental employers on accounting and financial reporting for termination of benefits.
- GASB Technical Bulletin No. 2004-2, *Recognition of Pension and Other Postemployment Benefits Expenditures/Expense and Liabilities by Cost-Sharing Employers*, which clarifies the requirements of GASB Statement Nos. 27 and 45 for recognition of pension and other postemployment benefit expenditures/expense and liabilities by cost-sharing employers.

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

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Notes to Financial Statements
September 30, 2006 and 2005

(11) New Accounting Principles, Continued

In April 2004, GASB issued 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 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 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. Management does not believe that the implementation of this Statement will have a material effect on the financial statements of GWA.

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.

(12) Contributions Received

Contributions received by GWA during the years ended September 30, 2006 and 2005, are as follows:

	<u>2006</u>	<u>2005</u>
Grants from U.S. Government:		
Received from the Environmental Protection Agency	\$ 903,874	\$ 2,836,249
Received from the Federal Emergency Management Agency, net of returns	<u>(54,667)</u>	<u>81,128</u>
	\$ <u>849,207</u>	\$ <u>2,917,377</u>
Other contributions:		
Proceeds received through refinancing of Government of Guam's Water Bond	\$ <u>300,000</u>	\$ <u>1,110,561</u>

(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.

GUAM WATERWORKS AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(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 have gone toward GWA's obligation to GPA and effective October 2003, also to the obligation to the U.S. Navy.

(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, 2006 and 2005 were \$10,521,173 and \$8,820,481, respectively, and GWA was also charged \$336,626 and \$116,871, respectively, for administrative services provided by GPA. In addition, GWA has long-term debt of \$9,762,654 and \$11,747,272 due to GPA at September 30, 2006 and 2005, respectively (see note 4).

(16) Subsequent Event

On December 6, 2006, GWA signed a performance management contract to manage GWA's wastewater system. The contract term is for three years with an option to extend for an additional three year period.

GUAM WATERWORKS AUTHORITY

Schedule 1
Schedule of Equalization of Net (Income) Loss
Years Ended September 30, 1991 through 2006

	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	\$ 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	(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	\$ 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, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Salaries and wages:		
Regular, differential and hazardous pay	\$ 8,988,945	\$ 8,188,675
Pension costs	4,418,624	2,908,611
Overtime pay	940,009	478,233
Sick leave	123,189	14,848
	<u>14,470,767</u>	<u>11,590,367</u>
Total salaries and wages	<u>\$ 14,470,767</u>	<u>\$ 11,590,367</u>
Employees at end of year	245	235
Administrative and general:		
Materials and supplies	\$ 2,601,892	\$ 2,033,352
Chemicals	581,654	542,074
Transportation	440,001	459,021
Public Utility Commission	291,397	350,403
Training	241,368	-
Violation fees	144,000	22,750
Communications	105,008	85,449
Liability claims	101,879	274,070
Advertising	65,389	46,735
Miscellaneous	125,270	334,246
	<u>4,697,858</u>	<u>4,148,100</u>
Total administrative and general	<u>\$ 4,697,858</u>	<u>\$ 4,148,100</u>
Contractual:		
Labor, materials and others	\$ 2,165,523	\$ 941,426
Equipment rental	1,029,483	994,720
Accounting	473,223	121,137
Testing	287,232	282,257
Legal	972	(11,935)
Engineering	-	-
	<u>3,956,433</u>	<u>2,327,605</u>
Total contractual	<u>\$ 3,956,433</u>	<u>\$ 2,327,605</u>
Other expense:		
Privatization	\$ 895	\$ 1,212,984
Other	1,492,448	336,323
	<u>1,493,343</u>	<u>1,549,307</u>

See accompanying independent auditors' report.

GUAM WATERWORKS AUTHORITY

Schedule 3

Schedule of Cash Flows Indicating Financing Method
Year Ended September 30, 2006

Cash flows provided by operating activities	\$ 7,615,999
Less nonpayment to GPA for 2006 expenses	<u>-</u>
Cash flows if all GPA expenses for 2006 were paid	7,615,999
Cash flows used for acquisition of utility plant, net of contributed capital received	<u>(27,162,291)</u>
Cash flows if GPA were fully paid and if utility plant were built, net of contributed capital received	<u>\$ (19,546,292)</u>

See accompanying independent auditors' report.

GUAM WATERWORKS AUTHORITY

Schedule 4
 Schedule of Construction Work in Progress
 Year Ended September 30, 2006

Project Title	Type	Ending Balance 2005	Additions and Transfers	Closed out during FY2006	Ending Balance 2006
Agat/Santa Rita Sewer System	Wastewater	\$ 418,456	\$ 48	\$ -	\$ 418,504
Layang South Barrigada	Wastewater	2,279,371	960,553	(3,239,924)	-
Ordot/Chalan Pago 2B	Wastewater	622,342	-	-	622,342
Watershed Master Plan	Water	2,939,293	3,213,195	-	6,152,488
Automated Meter Reading	Water	521,166	8,141,387	-	8,662,553
Distribution Line Replacement	Water	15,360	1,602,150	-	1,617,510
Hagatna Sewage Treatment Plant	Wastewater	-	4,744,209	-	4,744,209
All Others	Water/Wastewater	1,977,891	9,758,210	(7,238,629)	4,497,472
		<u>\$ 8,773,879</u>	<u>\$ 28,419,752</u>	<u>\$ (10,478,553)</u>	<u>\$ 26,715,078</u>

See accompanying independent auditors' report.

GUAM WATERWORKS AUTHORITY

Schedule 5
 Schedule of Employee Data
 Year Ended September 30, 2006

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	-	-	\$ 12,598	\$ 1,613	\$ 14,211
Administration	69	4,649,836	664,437	171,680	5,485,953
Accounting	14	743,277	343,859	223,074	1,310,210
Engineering	7	474,477	6,161	4,766	485,404
Collection and Distribution	98	5,919,289	2,563,279	1,642,867	10,125,435
Production and Treatment	57	3,157,140	366,099	557,892	4,081,131
Total	<u>245</u>	<u>\$ 14,944,019</u>	<u>\$ 3,956,433</u>	<u>\$ 2,601,892</u>	<u>\$ 21,502,344</u>