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COMMONWEALTH PORTS AUTHORITY
(A COMPONENT UNIT OF THE COMMONWEALTH
OF THE NORTHERN MARIANA ISLANDS)

REPORT ON THE AUDIT OF FINANCIAL
STATEMENTS IN ACCORDANCE
WITH OMB CIRCULAR A-133

YEAR ENDED SEPTEMBER 30, 2008

COMMONWEALTH PORTS AUTHORITY
(A COMPONENT UNIT OF THE COMMONWEALTH
OF THE NORTHERN MARIANA ISLANDS)

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2008 AND 2007

INDEPENDENT AUDITORS' REPORT

Board of Directors
Commonwealth Ports Authority:

We have audited the accompanying statements of net assets of the Commonwealth Ports Authority (CPA), a component unit of the Commonwealth of the Northern Mariana Islands, as of September 30, 2008 and 2007, 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 CPA'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 CPA'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, such financial statements present fairly, in all material respects, the financial position of the Commonwealth Ports Authority as of September 30, 2008 and 2007, 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.

As discussed in note 14 to the financial statements, operations receivable, net, passenger facility charge revenues and beginning net assets as of and for the year ended September 30, 2007 have been restated.

The Management's Discussion and Analysis on pages 3 through 10 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 the Commonwealth Ports Authority's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

Our audits were conducted for the purpose of forming an opinion on the Commonwealth Ports Authority's basic financial statements. The Combining Schedule of Net Assets, Combining Schedule of Revenues, Expenses and Changes in Net Assets and Combining Schedule of Cash Flows as of and for the year ended September 30, 2008 (pages 35 through 37) are presented for purposes of additional analysis and are not a required part of the basic financial statements. This supplementary information is the responsibility of the Commonwealth Ports Authority's management. This supplementary information has been subjected to the auditing procedures applied by us in the audit of the basic financial statements and, in our opinion, 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 March 3, 2010, on our consideration of 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 LLC

March 3, 2010



COMMONWEALTH PORTS AUTHORITY

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MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

This section of the Commonwealth Ports Authority's (herein referred to as "CPA") audit report presents our discussion and analysis of CPA's financial performance during the fiscal year ended September 30, 2008. Please read it in conjunction with the more detailed information contained within the accompanying financial statements. The nationally recognized accounting firm of Deloitte & Touche LLC issued an unqualified audit opinion.

INTRODUCTION

CPA is a component unit of the Government of the Commonwealth of the Northern Marianas Islands (CNMI) and was established as a public corporation on November 8, 1981 by CNMI Public Law 2-48. A seven-member Board of Directors appointed by the Governor to serve four-year terms governs CPA. CPA is a self-supporting organization and generates revenues from port users to fund operating expenses and debt service requirements.

CPA is tasked with the responsibility to operate, maintain, and improve all airports and seaports within the CNMI. Airport and seaport facilities currently exist on the islands of Saipan, Tinian and Rota and have 138 employees on Saipan, 26 employees on Rota and 24 employees on Tinian.

The following discussion and analysis of CPA's activities and financial performance provides an introduction to the financial statements for the fiscal year ended September 30, 2008, with selected comparative information for the fiscal years ended September 30, 2007 and 2006.

The notes to the financial statements are essential to a full understanding of the data contained in the financial statements. This report also presents certain required supplementary information regarding capital assets and long-term debt activity during the year, including commitments made for capital expenditures.

OVERVIEW OF FINANCIAL STATEMENTS

CPA's financial transactions and subsequent statements are prepared in accordance with accounting principles generally accepted in the United States of America and standards mandated by the Governmental Accounting Standards Board, as applicable to governmental entities.

CPA operates on an accrual basis wherein revenues are recognized when earned, not when received and expenses are recorded when incurred, not when paid. Capital assets, except for land, are capitalized and depreciated over their useful lives. Further information is provided in the footnotes of the accompanying audited financial statements.

The financial statements of this annual report consist of three parts: the MD&A, the basic financial statements, and notes to the financial statements. The basic financial statements consist of the Statement of Net Assets, the Statement of Revenues, Expenses and Changes in Net Assets, and the Statement of Cash Flows.

The Statement of Net Assets presents information on all CPA's assets and liabilities, with the difference between the two reported as net assets. Net assets consist of restricted net assets, unrestricted net assets and invested in capital assets, net of related debt.

The Statement of Revenues, Expenses and Changes in Net Assets presents information showing how net assets changed during the most recent three fiscal years. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future periods.

The Statement of Cash Flows presents information about the cash receipts and cash payments of CPA during the most recent three fiscal years and its ability to generate net cash flows, its ability to meet its obligations as they come due and its needs for external financing.

FINANCIAL HIGHLIGHTS

Total assets for the airport and seaport operations combined in FY2008 decreased by 2% or \$4,442,578 from \$227,602,011 in FY2007 to \$223,159,433.

Net assets for the airport and seaport operations combined in FY2008 increased by 1% or \$1,760,583 from \$154,290,063 in FY2007 to \$156,050,646. Net assets represent the amount that total assets exceed total liabilities.

Enplanement (air passenger departures) declined by 3% and deplanement (air passenger arrivals) declined by 2% during FY2008 from the prior year due to reduction in passenger arrivals to the CNMI.

Seaport inbound cargo decreased by 13% and outbound cargo decreased by 52% in FY2008 from the prior year due to the closure of several garment factories and a decline in orders and inbound commodities from existing factories.

Operating revenues for the airport and seaport operations combined in FY2008 decreased by 9% or \$1,353,443 from \$15,152,900 in FY2007 to \$13,799,457. Airport operating revenues decreased by 12% or \$1,175,007 from \$9,805,327 in FY2007 to \$8,630,320. Seaport operating revenues decreased by 3% or \$178,436 from \$5,347,573 in FY2007 to \$5,169,137.

Operating expenses (excluding depreciation and amortization) for the airport and seaport operations combined in FY2008 decreased by 4% or \$561,389 from \$13,348,829 in FY2007 to \$12,787,440, due to reduction in operating costs.

Due to a revenue shortfall of \$3.4 million for the Airport Division and \$1.3 million for the Seaport Division at September 30, 2008 or a combined shortfall of \$4.7 million, CPA was not in compliance with its 1998 Bond Indenture Agreement (the Agreement). CPA hired a bond consultant to conduct an Airport/Seaport rate study to comply with the Agreement. Currently, both the Airport and Seaport Divisions increased their fees to comply with the Agreement.

Statement of Net Assets

| Assets | 2008 | 2007 | Variance | % | 2006 |
|---|------------------------------|------------------------------|------------------------------|-------------|------------------------------|
| Current assets | \$ <u>10,168,093</u> | \$ <u>19,299,165</u> | \$ <u>(9,131,072)</u> | -47% | \$ <u>16,784,712</u> |
| Investments, restricted for construction and debt service purposes | <u>17,122,945</u> | <u>18,729,555</u> | <u>(1,606,610)</u> | -9% | <u>22,572,954</u> |
| Noncurrent assets: | | | | | |
| Deferred bond issue cost | 1,461,297 | 1,528,232 | (66,935) | -4% | 1,595,167 |
| Receivable from related party, net | 3,659,613 | 4,700,947 | (1,041,334) | -22% | 4,700,947 |
| Capital assets, net | <u>190,747,485</u> | <u>183,344,112</u> | <u>7,403,373</u> | 4% | <u>156,386,112</u> |
| Total noncurrent assets | <u>195,868,395</u> | <u>189,573,291</u> | <u>6,295,104</u> | 3% | <u>162,682,226</u> |
| | \$ <u>223,159,433</u> | \$ <u>227,602,011</u> | \$ <u>(4,442,578)</u> | -2% | \$ <u>202,039,892</u> |

Statement of Net Assets, Continued

| Liabilities and Net Assets | 2008 | 2007 | Variance | % | 2006 |
|---|---------------------------|---------------------------|---------------------------|-------------|---------------------------|
| Current liabilities: | | | | | |
| Revenue bonds payable, current portion | \$ 2,330,000 | \$ 1,265,000 | \$ 1,065,000 | 84% | \$ 1,050,000 |
| Note payable to related party, current portion | - | 1,281,659 | (1,281,659) | -100% | 1,244,439 |
| Contractors payable | 3,549,673 | 9,029,167 | (5,479,494) | -61% | 4,217,463 |
| Trade and other payables | 278,657 | 224,700 | 53,957 | 24% | 138,812 |
| Due to related parties | 2,184,935 | 2,524,210 | (339,275) | -13% | 2,229,182 |
| Accrued expenses | 3,273,680 | 2,362,501 | 911,179 | 39% | 2,490,901 |
| Deferred income | 5,625 | 5,625 | - | 0% | 10,333 |
| Compensated absences, current portion | <u>275,621</u> | <u>242,557</u> | <u>33,064</u> | 14% | <u>284,386</u> |
| Total current liabilities | 11,898,191 | 16,935,419 | (5,037,228) | -30% | 11,665,516 |
| Accrued interest payable | 304,994 | - | 304,994 | 100% | - |
| Compensated absences, net of current portion | 262,334 | 505,246 | (242,912) | -48% | 356,566 |
| Revenue bonds payable, net of current portion | 48,839,658 | 51,126,227 | (2,286,569) | -4% | 52,349,570 |
| Note payable to related party, net of current portion | <u>5,803,610</u> | <u>4,745,056</u> | <u>1,058,554</u> | 22% | <u>5,432,114</u> |
| Total liabilities | <u>67,108,787</u> | <u>73,311,948</u> | <u>(6,203,161)</u> | -8% | <u>69,803,766</u> |
| Net assets: | | | | | |
| Invested in capital assets, net of related debt | 135,235,514 | 126,454,402 | 8,781,112 | 7% | 97,905,156 |
| Restricted | 17,122,945 | 18,729,555 | (1,606,610) | -9% | 22,572,954 |
| Unrestricted | <u>3,692,187</u> | <u>9,106,106</u> | <u>(5,413,919)</u> | -59% | <u>11,758,016</u> |
| Total net assets | <u>156,050,646</u> | <u>154,290,063</u> | <u>1,760,583</u> | 1% | <u>132,236,126</u> |
| | \$ 223,159,433 | \$ 227,602,011 | \$ (4,442,578) | -2% | \$ 202,039,892 |

Statement of Revenues, Expenses and Changes in Net Assets

| | 2008 | 2007 | Variance | % | 2006 |
|--|------------------------------|------------------------------|-------------------------------|-------------|------------------------------|
| Operating revenues, net | \$ 13,348,228 | \$ 15,045,048 | \$ (1,696,820) | -11% | \$ 19,426,102 |
| Maintenance and operations expenses | <u>12,787,440</u> | <u>13,348,829</u> | <u>(561,389)</u> | -4% | <u>13,963,912</u> |
| Income before depreciation | 560,788 | 1,696,219 | (1,135,431) | -67% | 5,462,190 |
| Depreciation | <u>9,690,222</u> | <u>10,607,952</u> | <u>(917,730)</u> | -9% | <u>9,614,293</u> |
| Loss after depreciation | (9,129,434) | (8,911,733) | (217,701) | 2% | (4,152,103) |
| Non-operating revenues (expenses), net | <u>(1,635,583)</u> | <u>(721,079)</u> | <u>(914,504)</u> | 127% | <u>(244,758)</u> |
| Loss before capital contributions | (10,765,017) | (9,632,812) | (1,132,205) | 12% | (4,396,861) |
| Capital contributions | <u>12,525,600</u> | <u>31,686,749</u> | <u>(19,161,149)</u> | -60% | <u>18,284,820</u> |
| Change in net assets | \$ <u>1,760,583</u> | \$ <u>22,053,937</u> | \$ <u>(20,293,354)</u> | -92% | \$ <u>13,887,959</u> |
| Net assets - beginning | \$ 154,290,063 | \$ 132,236,126 | \$ 22,053,937 | 17% | \$ 118,348,167 |
| Change in net assets | <u>1,760,583</u> | <u>22,053,937</u> | <u>(20,293,354)</u> | -92% | <u>13,887,959</u> |
| Net assets - ending | \$ <u>156,050,646</u> | \$ <u>154,290,063</u> | \$ <u>1,760,583</u> | 1% | \$ <u>132,236,126</u> |

In FY2008, airport operating revenues decreased by 12% or \$1,175,007 compared to FY2007 levels mainly due to decreases in airline passengers, new airline incentive program (100% discount) and concession revenues resulting from the reduction of flights to the CNMI. Seaport operating revenues decreased by 3% due to the reduction in consumer cargoes and the closure of the garment factories.

Statements of Cash Flows

| | 2008 | 2007 | Variance | % | 2006 |
|--|----------------------------|----------------------------|------------------------------|-------------|-----------------------------|
| Cash flows from operating activities | \$ 2,738,495 | \$ (578,367) | \$ 3,316,862 | -573% | \$ 5,140,015 |
| Cash flows from capital and related financing activities | (10,606,114) | (6,134,427) | (4,471,687) | 73% | (1,623,868) |
| Cash flows from investing activities | <u>2,100,007</u> | <u>4,933,030</u> | <u>(2,833,023)</u> | -57% | <u>(1,003,757)</u> |
| Net change in cash | (5,767,612) | (1,779,764) | (3,987,848) | 224% | 2,512,390 |
| Cash and cash equivalents at beginning of year | <u>9,678,551</u> | <u>11,458,315</u> | <u>(1,779,764)</u> | -16% | <u>8,945,925</u> |
| Cash and cash equivalents at end of year | \$ <u>3,910,939</u> | \$ <u>9,678,551</u> | \$ <u>(5,767,612)</u> | -60% | \$ <u>11,458,315</u> |

Capital Assets

At September 30, 2008, CPA had \$190,747,485 invested in capital assets, net of depreciation where applicable, including land, runway, terminal and harbor facilities and equipment, fire and rescue equipment, general transportation, other machinery and equipment and numerous projects under construction. This represents a net increase of \$7,403,373 or 4% over last year.

| | 2008 | 2007 | 2006 |
|--|-----------------------|-----------------------|-----------------------|
| Runway and improvements | \$ 92,331,622 | \$ 69,076,791 | \$ 69,076,791 |
| Other improvements | 16,258,401 | 16,215,774 | 16,197,486 |
| Terminal facilities and equipment | 100,721,909 | 79,202,607 | 78,675,814 |
| Harbor facilities | 62,101,850 | 62,101,850 | 61,997,300 |
| Grounds maintenance and shop equipment | 509,692 | 509,692 | 506,735 |
| Fire and rescue equipment | 11,506,180 | 11,477,584 | 10,481,756 |
| Office furniture and fixtures | 905,497 | 871,010 | 824,171 |
| General transportation | 1,010,798 | 929,612 | 879,641 |
| Other | <u>2,394,591</u> | <u>2,392,367</u> | <u>871,469</u> |
| | 287,740,540 | 242,777,287 | 239,511,163 |
| Less accumulated depreciation | <u>(127,547,389)</u> | <u>(117,828,380)</u> | <u>(107,254,453)</u> |
| Total capital assets being depreciated | 160,193,151 | 124,948,907 | 132,256,710 |
| Construction in progress | 30,089,905 | 57,930,776 | 23,664,973 |
| Land | <u>464,429</u> | <u>464,429</u> | <u>464,429</u> |
| Total capital assets, net | <u>\$ 190,747,485</u> | <u>\$ 183,344,112</u> | <u>\$ 156,386,112</u> |

Please refer to note 6 to the financial statements for additional information regarding capital asset activity.

1998 Airport Revenue Bonds

On March 26, 1998, CPA issued a 1998 Series A \$20,050,000 tax-exempt revenue bond. Interest is 6.25%, payable semi-annually on March 15 and September 15 of each year, commencing September 1998 and ending in the year 2028.

Payments for the Airport bond are current. The current portion of the Airport bond principal is \$1,435,000. The long-term portion of the bond balance as of September 30, 2008 is \$15,375,000.

This 1998 bond was partly used to refund an outstanding \$8,250,000 1987 Series B tax-exempt bonds. The bond refunding consolidated the existing bonds with new bonds to finance various airport projects and to reduce total future debt service payments from lower interest rates. The reacquisition price exceeded the net carrying amount of the old debt by \$503,906 that was netted out against the new debt and amortized over the refunded debt's life, which is shorter than the life of the new debt. The transaction also resulted in an economic gain of \$688,620 and an increase of \$7,616,151 in debt service payments in the future.

Airport Restricted Investments

Restricted investments for airport construction and debt service purposes represent the unused proceeds of the 1998 Airport Revenue Bonds deposited with the Trustee. The balances as of September 30, 2008 are:

| | |
|---------------------------|---------------------|
| Bond Reserve Fund | \$ 1,555,389 |
| Construction Fund | 998,519 |
| Bond Fund | 284,982 |
| Maintenance and Operation | 464,713 |
| Reserve Fund | <u>448,588</u> |
| Total | <u>\$ 3,752,191</u> |

1998 Seaport Revenue Bonds

On March 26, 1998, CPA issued a 1998 Series A \$33,775,000 tax-exempt revenue bond. Interest on the bond is payable at 6.6% on March 15 and September 15 of each year, commencing September 1998 and ending in the year 2028.

Payments for the 1998 Seaport bond are current. The current portion of the 1998 Seaport bond principal is \$740,000. The long-term portion of the bond balance as of September 30, 2008 is \$27,685,000.

The seaport bond proceeds were partly used for a current refunding of \$22,470,000 of 1995 Series A tax-exempt seaport revenue bonds. The refunding consolidated existing debt with new debt issued to finance various seaport projects and to reduce total debt service payments in the future. The reacquisition price exceeded the net carrying amount of the old debt by \$1,345,593 that was netted out against the new debt and amortized over the refunded debt's life, which is shorter than the life of the new debt. The transaction also resulted in an economic gain of \$1,724,777 and a decrease of \$6,983,345 in debt service payments in the future.

2005 Seaport Revenue Bonds

On September 21, 2005, CPA issued another Senior Series A tax-exempt revenue bond in the amount of \$7,225,000 for the purpose of financing primarily the paving of the container yard area of the seaport. Pursuant to Section 2.04 (A)(9) of the 1998 Senior Series A Seaport Revenue Bond Indenture Agreement, CPA entered into a Second Supplemental Indenture for the above 2005 Senior Series A bonds payable at a semi-annual interest rate of 5.5% on March 15 and September 15 of each year. Payments commenced on March 15, 2008.

Payments for the 2005 Seaport bond are current. The current portion of the 2005 Seaport bond principal is \$155,000. The long-term portion of the bond balance as of September 30, 2008 is \$6,920,000.

Seaport Restricted Investments

| | |
|---------------------------|----------------------|
| Bond Reserve Fund | \$ 3,478,814 |
| Supplemental Reserve Fund | 8,038,346 |
| Reimbursement Fund | 5,806 |
| Bond Fund | 489,094 |
| Maintenance and Operation | 493,610 |
| Construction Fund | 557,219 |
| Interest Fund | 69,468 |
| Revenue Fund | <u>238,397</u> |
| Total | \$ <u>13,370,754</u> |

FY2008 Bond/Debt Ratio Noncompliance

| | Airport | Seaport |
|---------------------------------------|-----------------------|-----------------------|
| Required revenues for bond compliance | \$ 12,287,723 | \$ 6,727,176 |
| Actual revenues collected | <u>9,264,470</u> | <u>5,474,433</u> |
| Variance (noncompliance) | \$ <u>(3,023,253)</u> | \$ <u>(1,252,743)</u> |

The drop in revenue in FY2008 resulted in noncompliance with the revenue requirements imposed by the Airport and Seaport Bond Indentures. CPA was cited for noncompliance with the Airport and Seaport Bond Indentures.

In accordance with the Bond Indentures, CPA hired a bond consultant to conduct an airport and seaport rate study to comply with the revenue requirements for the Airport and Seaport Divisions.

Notes Payable to Commonwealth Development Authority

CPA signed a promissory note with the Commonwealth Development Authority (CDA) with interest at 2.5% per annum. Payments are due quarterly and the note matures on November 16, 2014. The balance is \$5,803,610 as of September 30, 2008. The CDA promissory note is subordinate to CPA's Seaport bond obligations. Beginning January 2008, Principle and interest payments have been deferred for five years and two years, respectively.

Please refer to notes 7 and 8 to the financial statements for additional information regarding revenue bonds payable and notes payable to related party.

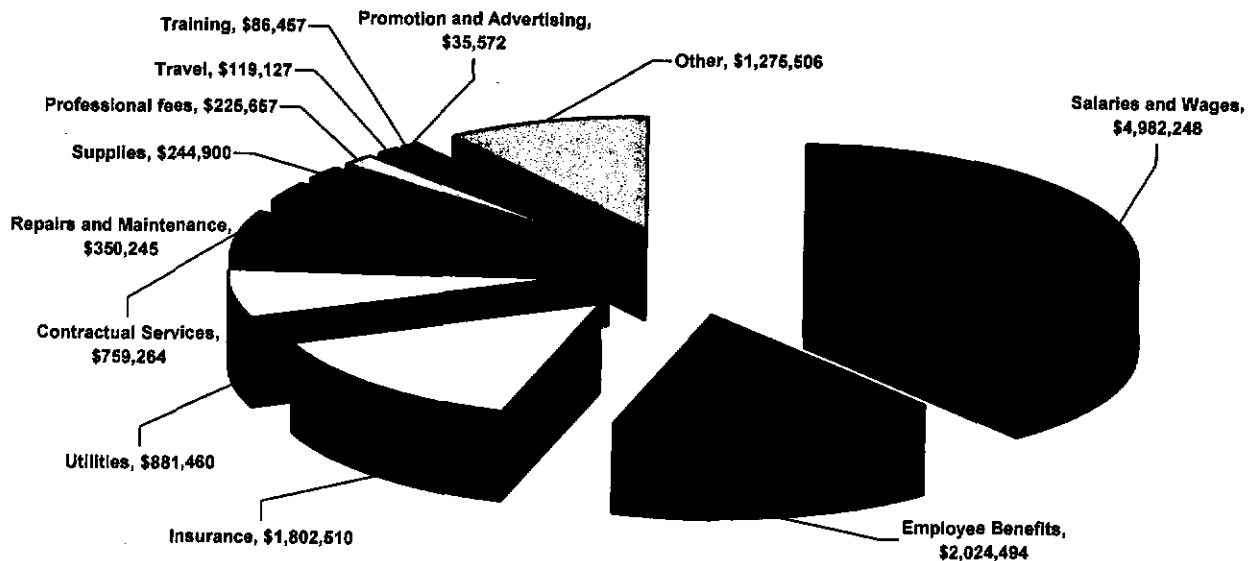
Operating Revenues (Combined)

| | FY2008 Audited | FY2007 Audited | Change | % | FY2006 Audited |
|---------------------------------|-----------------------------|-----------------------------|------------------------------|------------|-----------------------------|
| Airport revenues | \$ 8,630,320 | \$ 9,805,327 | \$ (1,175,007) | -12% | \$ 10,951,105 |
| Seaport revenues | <u>5,169,137</u> | <u>5,347,573</u> | <u>(178,436)</u> | -3% | <u>9,005,950</u> |
| Total operating revenues | \$ <u>13,799,457</u> | \$ <u>15,152,900</u> | \$ <u>(1,353,443)</u> | -9% | \$ <u>19,957,055</u> |

Airport revenues declined by 12% or \$1,175,007 overall when compared to FY2007 mainly due to a drastic drop in air passenger revenues, new airline incentive program (100% discount) and reduction of flights to the CNMI. Seaport revenues decreased by 3% or \$178,436 overall when compared to FY2007. The decrease is due to a reduction in consumer cargo and the pull out of the garment industry.

Operating Expenses (Combined)

| | FY2008 Audited | FY2007 Audited | Change | % | FY2006 Audited |
|-------------------------------------|-----------------------------|-----------------------------|----------------------------|------------|-----------------------------|
| Personnel costs | \$ 7,006,742 | \$ 7,812,531 | \$ (805,789) | -10% | \$ 7,853,859 |
| Maintenance and operations expenses | <u>5,780,698</u> | <u>5,536,298</u> | <u>244,400</u> | 4% | <u>6,110,053</u> |
| Total operating expenses | \$ <u>12,787,440</u> | \$ <u>13,348,829</u> | \$ <u>(561,389)</u> | -4% | \$ <u>13,963,912</u> |



| | | | |
|------------------------|---------------------------|-----------------------------|---------------------|
| ■ Salaries and Wages | ■ Employee Benefits | □ Insurance | □ Utilities |
| ■ Contractual Services | ■ Repairs and Maintenance | ■ Supplies | □ Professional fees |
| ■ Travel | ■ Training | □ Promotion and advertising | □ Other |

Operating expenses (excluding depreciation and amortization), for the airport and seaport operations combined in FY 2008 decreased by 4% or \$561,389 from \$13,348,829 in FY2007 to \$12,787,440 due to reduction in operating costs.

Airport Deplanement or Arrivals (Number of Passengers) for Each Airport

| | FY2008 | FY2007 | Change | % | FY2006 |
|--------------|-----------------------|-----------------------|-----------------------|------------|-----------------------|
| Saipan | 460,437 | 470,013 | -9,576 | -2% | 511,720 |
| Rota | 18,589 | 19,409 | -820 | -4% | 28,963 |
| Tinian | <u>29,263</u> | <u>30,258</u> | <u>-995</u> | -3% | <u>37,495</u> |
| Total | <u>508,289</u> | <u>519,680</u> | <u>-11,391</u> | -2% | <u>578,178</u> |

Deplanement or passenger arrivals dropped by 2% or 11,391 passengers in FY2008 as compared to 2007 due to the reduction of flights to the CNMI.

Airport Enplanement or Departures (Number of Passengers) for Each Airport

| | FY2008 | FY2007 | Change | % | FY2006 |
|--------------|-----------------------|-----------------------|-----------------------|------------|-----------------------|
| Saipan | 460,933 | 473,249 | -12,316 | -3% | 516,366 |
| Rota | 19,048 | 20,326 | -1,278 | -6% | 29,544 |
| Tinian | <u>31,020</u> | <u>35,427</u> | <u>-4,407</u> | -12% | <u>44,597</u> |
| Total | <u>511,001</u> | <u>529,002</u> | <u>-18,001</u> | -3% | <u>590,507</u> |

Enplanement or passenger departures dropped by 3% or 18,001 passengers in FY 2008 as compared to FY2007 due to the reduction of flights to the CNMI.

Seaport Inbound Cargo Revenue Tons

| | FY2008 | FY2007 | Change | % | FY2006 |
|--------------|-----------------------|-----------------------|-----------------------|-------------|-----------------------|
| Saipan | 389,338 | 462,233 | -72,895 | -16% | 553,267 |
| Rota | 10,406 | 12,090 | -1,684 | -14% | 13,000 |
| Tinian | <u>33,790</u> | <u>23,174</u> | <u>10,616</u> | 46% | <u>28,584</u> |
| Total | <u>433,534</u> | <u>497,497</u> | <u>-63,963</u> | -13% | <u>594,851</u> |

Seaport inbound cargo in terms of revenue tonnage dropped by 13% or 63,963 revenue tons due to the closure of several garment factories and a decline in orders and inbound commodities from existing factories.

Seaport Outbound Cargo Revenue Tons

| | FY2008 | FY2007 | Change | % | FY2006 |
|--------------|----------------------|-----------------------|-----------------------|-------------|-----------------------|
| Saipan | 44,834 | 99,855 | -55,021 | -55% | 115,555 |
| Rota | 1,761 | 1,103 | 658 | 60% | 665 |
| Tinian | <u>3,448</u> | <u>2,373</u> | <u>1,075</u> | 45% | <u>3,101</u> |
| Total | <u>50,043</u> | <u>103,331</u> | <u>-53,288</u> | -52% | <u>119,321</u> |

Seaport outbound cargo in terms of revenue tonnage dropped by 52% or 53,288 revenue tons due to the closure of several garment factories and a decline in orders from existing factories.

ECONOMIC OUTLOOK

Subsequent to fiscal year 2008, the world economy suffered a serious recession, which was further exacerbated by a swine flu pandemic which had a major impact on air travel. The effect and length of these two factors are unknown at this time. Further, the closure of the CNMI's last garment factory had a major impact on CPA's seaport activity. Saipan's seaport activity for the first five months of fiscal year 2009 indicates a 23% decrease in inbound freight and a 45% decrease in outbound freight over the prior year.

This decline in activity has been very noticeable. However, the financial impact of this decline has been offset by two major policy changes, as follows:

1. Port charges were substantially increased (90%) at the beginning of 2009. This increase has gradually been absorbed by the community and appears sustainable.
2. The previously initiated Airlines Rebate Program has been discontinued. This program refunded 100% of the airline landing fees to the airlines. Developed as an incentive to promote additional tourism, the program was a failure. Canceling the program will greatly aid the revenue and the cash flow of the airport division.

Other economic factors which can impact CPA include the federalization of CNMI's immigration and the enforcement of U.S. minimum wage standards.

Currently, the CNMI enjoys niche tourism markets in Russia and China due to the application of local immigration standards. Beginning in fiscal year 2010, when the U.S. takes over, both Chinese and Russian tourists will be required to obtain U.S. visas before entering the CNMI. CPA's major markets in Japan and Korea will not be affected.

While the U.S. minimum wage application will not impact CPA's direct payroll, it will impact many of the service suppliers to CPA, so increases in operating costs can be anticipated.

The long-term outlook indicates some optimism with the expansion of the military presence in Guam and the announced intention to use Tinian as a training center. This would possibly increase air traffic as Saipan would be seen as an inexpensive weekend getaway vacation for military personnel. Further, construction and supply demands for the Tinian training center could greatly increase seaport activity.

CONTACTING CPA'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of CPA's finances and to demonstrate its accountability for the monies received. The Management's Discussion and Analysis for the year ended September 30, 2007 is set forth in the report on the audit of CPA's financial statements which is dated August 5, 2008. That Discussion and Analysis explains the major factors impacting the 2007 financial statements. If you have questions about this report or need additional financial information, contact Ms. Frances C. Mafnas, Comptroller, P.O. Box 501055, Saipan, MP 96950-1055, or call (670) 237-6500 or email at cpa.plantacct@pticom.com.

COMMONWEALTH PORTS AUTHORITY

Statements of Net Assets
September 30, 2008 and 2007

| <u>ASSETS</u> | <u>2008</u> | <u>2007</u> <u>(As Restated)</u> |
|--|-----------------------|-------------------------------------|
| Current assets: | | |
| Cash and cash equivalents | \$ 3,910,939 | \$ 9,678,551 |
| Receivables: | | |
| Grantor agencies | 1,522,401 | 4,470,495 |
| Operations, net | 3,730,575 | 4,944,500 |
| Related parties | 855,878 | 53,181 |
| Officers and employees | 60,927 | 55,069 |
| Prepaid expenses | 87,373 | 97,369 |
| Investments, restricted for construction and debt service purposes | <u>17,122,945</u> | <u>18,729,555</u> |
| Total current assets | <u>27,291,038</u> | <u>38,028,720</u> |
| Noncurrent assets: | | |
| Deferred bond issue costs | 1,461,297 | 1,528,232 |
| Receivable from related party, net | 3,659,613 | 4,700,947 |
| Capital assets, net | <u>190,747,485</u> | <u>183,344,112</u> |
| Total noncurrent assets | <u>195,868,395</u> | <u>189,573,291</u> |
| | <u>\$ 223,159,433</u> | <u>\$ 227,602,011</u> |
| <u>LIABILITIES AND NET ASSETS</u> | | |
| Current liabilities: | | |
| Revenue bonds payable, current portion | \$ 2,330,000 | \$ 1,265,000 |
| Note payable to related party, current portion | - | 1,281,659 |
| Contractors payable | 3,549,673 | 9,029,167 |
| Trade and other payables | 278,657 | 224,700 |
| Due to related parties | 2,184,935 | 2,524,210 |
| Accrued expenses | 3,273,680 | 2,362,501 |
| Deferred income | 5,625 | 5,625 |
| Compensated absences, current portion | <u>275,621</u> | <u>242,557</u> |
| Total current liabilities | 11,898,191 | 16,935,419 |
| Accrued interest payable | 304,994 | - |
| Compensated absences, net of current portion | 262,334 | 505,246 |
| Revenue bonds payable, net of current portion | 48,839,658 | 51,126,227 |
| Note payable to related party, net of current portion | <u>5,803,610</u> | <u>4,745,056</u> |
| Total liabilities | <u>67,108,787</u> | <u>73,311,948</u> |
| Commitment and contingencies | | |
| Net assets: | | |
| Invested in capital assets, net of related debt | 135,235,514 | 126,454,402 |
| Restricted | 17,122,945 | 18,729,555 |
| Unrestricted | <u>3,692,187</u> | <u>9,106,106</u> |
| Total net assets | <u>156,050,646</u> | <u>154,290,063</u> |
| | <u>\$ 223,159,433</u> | <u>\$ 227,602,011</u> |

See accompanying notes to financial statements.

COMMONWEALTH PORTS AUTHORITY

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2008 and 2007

| | <u>2008</u> | <u>2007</u> (As Restated) |
|--|-----------------------|------------------------------|
| Operating revenues: | | |
| Concession and lease income | \$ 4,476,494 | \$ 4,213,807 |
| Aviation fees | 4,120,192 | 5,866,390 |
| Seaport fees | 3,532,991 | 3,870,641 |
| Other | <u>1,669,780</u> | <u>1,202,062</u> |
| | 13,799,457 | 15,152,900 |
| Less bad debts | <u>(451,229)</u> | <u>(107,852)</u> |
| Operating revenues, net | <u>13,348,228</u> | <u>15,045,048</u> |
| Operating expenses: | | |
| Depreciation and amortization | 9,690,222 | 10,607,952 |
| Salaries and wages | 4,982,248 | 5,372,951 |
| Employee benefits | 2,024,494 | 2,439,580 |
| Insurance | 1,802,510 | 2,036,874 |
| Utilities | 881,460 | 597,068 |
| Contractual services | 759,264 | 736,042 |
| Repairs and maintenance | 350,245 | 247,852 |
| Supplies | 244,900 | 358,138 |
| Professional fees | 225,657 | 344,622 |
| Travel | 119,127 | 176,011 |
| Training | 86,457 | 112,987 |
| Promotion and advertising | 35,572 | 38,546 |
| Other | <u>1,275,506</u> | <u>888,158</u> |
| Total operating expenses | <u>22,477,662</u> | <u>23,956,781</u> |
| Operating loss | <u>(9,129,434)</u> | <u>(8,911,733)</u> |
| Non-operating revenues (expenses): | | |
| Passenger facility charges | 2,160,681 | 1,925,589 |
| Interest income | 493,397 | 1,089,631 |
| Interest expense | (2,974,460) | (3,669,364) |
| Other expense | (1,248,266) | - |
| Amortization of bond issue costs | <u>(66,935)</u> | <u>(66,935)</u> |
| Total non-operating revenues (expenses), net | <u>(1,635,583)</u> | <u>(721,079)</u> |
| Loss before capital contributions | (10,765,017) | (9,632,812) |
| Capital contributions | <u>12,525,600</u> | <u>31,686,749</u> |
| Change in net assets | 1,760,583 | 22,053,937 |
| Net assets at beginning of year, as restated | <u>154,290,063</u> | <u>132,236,126</u> |
| Net assets at end of year | <u>\$ 156,050,646</u> | <u>\$ 154,290,063</u> |

See accompanying notes to financial statements.

COMMONWEALTH PORTS AUTHORITY

Statements of Cash Flows
Years Ended September 30, 2008 and 2007

| | 2008 | 2007 (As Restated) |
|--|---------------------|-----------------------|
| Cash flows from operating activities: | | |
| Cash received from customers | \$ 14,777,981 | \$ 12,435,374 |
| Cash payments to suppliers for goods and services | (4,822,896) | (5,308,061) |
| Cash payments to employees for services | (7,216,590) | (7,705,680) |
| Net cash provided by (used for) operating activities | <u>2,738,495</u> | <u>(578,367)</u> |
| Cash flows from capital and related financing activities: | | |
| Acquisition of capital assets | (22,041,522) | (32,754,248) |
| Capital contributions received | 14,225,428 | 30,021,777 |
| Passenger facility charge receipts | 2,160,681 | 1,925,589 |
| Principal paid on revenue bond maturities | (1,265,000) | (1,050,000) |
| Payments on note payable to related party | (223,105) | (649,838) |
| Interest paid on revenue bonds and note payable to related party | (3,462,596) | (3,627,707) |
| Net cash used for capital and related financing activities | <u>(10,606,114)</u> | <u>(6,134,427)</u> |
| Cash flows from investing activities: | | |
| Net change in restricted investments | 1,606,610 | 3,843,399 |
| Interest income | 493,397 | 1,089,631 |
| Net cash provided by investing activities | <u>2,100,007</u> | <u>4,933,030</u> |
| Net change in cash and cash equivalents | (5,767,612) | (1,779,764) |
| Cash and cash equivalents at beginning of year | 9,678,551 | 11,458,315 |
| Cash and cash equivalents at end of year | <u>\$ 3,910,939</u> | <u>\$ 9,678,551</u> |
| Reconciliation of operating loss to net cash provided by (used for) operating activities: | | |
| Operating loss | \$ (9,129,434) | \$ (8,911,733) |
| Adjustments to reconcile operating loss to net cash provided by (used for) operating activities: | | |
| Depreciation and amortization | 9,690,222 | 10,607,952 |
| Bad debts | 451,229 | 107,852 |
| (Increase) decrease in assets: | | |
| Receivables - operations | 762,696 | (2,692,953) |
| Receivables - officers and employees | (5,858) | (16,819) |
| Prepaid expenses | 9,996 | (19,760) |
| Receivables - related parties | 238,637 | (7,565) |
| Increase (decrease) in liabilities: | | |
| Accounts payable - trade and other | 53,957 | 85,888 |
| Accounts payable - related parties | (339,275) | 295,028 |
| Accrued expenses | 1,216,173 | (128,400) |
| Deferred income | - | (4,708) |
| Compensated absences | (209,848) | 106,851 |
| Net cash provided by (used for) operating activities | <u>\$ 2,738,495</u> | <u>\$ (578,367)</u> |

See accompanying notes to financial statements.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(1) Organization

The Commonwealth Ports Authority (CPA), a component unit of the Commonwealth of the Northern Mariana Islands (CNMI), was established as a public corporation by CNMI Public Law 2-48, effective November 8, 1981. CPA was given responsibility for operations, maintenance and improvement of all airports and seaports within the CNMI. Both airports and seaports currently exist on the islands of Saipan, Tinian and Rota. CPA is governed by a seven-member Board of Directors, appointed for terms of four years by the Governor of the CNMI.

(2) Summary of Significant Accounting Policies

The accounting policies of CPA conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities, specifically proprietary funds. Governmental 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. CPA has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

Basis of Accounting

All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of this fund are included in the statements of net assets. Proprietary fund operating statements present increases (e.g. revenues) and decreases (e.g. expenses) in net assets. The accrual basis of accounting is utilized for proprietary funds. Under this method, revenues are recorded when earned and expenses recorded at the time liabilities are incurred.

Budgets

In accordance with CNMI Public Law 3-68, the Planning and Budgeting Act of 1983, CPA is required to submit annual budgets to the CNMI Office of the Governor.

Concentrations of Credit Risk

Financial instruments which potentially subject CPA to concentrations of credit risk consist principally of cash demand deposits, investments, receivables and receivables from related party.

At September 30, 2008 and 2007, CPA has cash deposits and investments in bank accounts that exceed federal depository insurance limits. CPA has not experienced any losses on such accounts.

As of September 30, 2008 and 2007, concentrations of credit risk result from receivables from significant customers and receivable from a related party which represent 62% and 42%, respectively, of total receivables. Management assesses the risk of loss and provides an allowance for doubtful accounts to compensate for known credit risk.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(2) Summary of Significant Accounting Policies, Continued

Cash and Cash Equivalents

For the purposes of the statements of net assets and the statements of cash flows, cash and cash equivalents is defined as cash on hand, demand deposits, savings and unrestricted short-term investments in U.S. Treasury obligations with maturity dates within three months of the date acquired. Short-term investment accounts established and set aside for construction and debt service purposes are separately classified as investments in the accompanying financial statements.

Capitalization of Interest

CPA capitalizes interest in order to recognize all costs associated with the non-contributed airport and seaport construction projects based on CPA's weighted average borrowing rate. The amount of interest eligible for capitalization was \$531,567 at September 30, 2008. During the year ended September 30, 2007, management of CPA determined that the amount of interest eligible for capitalization was not material. No interest is capitalized for projects financed with grant proceeds or Passenger Facility Charges.

Investments

CPA values its investments based on fair values in accordance with GASB Statement No. 31. CNMI Public Law 2-48, Section 31, requires that all CPA investments be guaranteed by the CNMI Government or U.S. Government, or be invested in direct obligations, or participation certificates, guaranteed by the U.S. Government.

Allowance for Doubtful Accounts

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

Capital Assets

Property, plant and equipment and construction-in-progress are recorded at cost. Depreciation is provided by using the straight-line method over the estimated useful lives of the assets. CPA's current policy is to capitalize items with costs in excess of \$1,000.

Bond Discounts and Issuance Costs

Bond discounts and issuance costs are deferred and amortized over the term of the related bond using the straight-line method. Bonds payable are reported net of bond discounts. Bond issuance costs are reported as deferred charges.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(2) Summary of Significant Accounting Policies, Continued

Passenger Facility Charges

Passenger Facility Charges (PFCs) generate revenue to be expended by CPA for eligible projects and the payment of debt service on the General Revenue Bonds as determined by applicable federal legislation. PFC revenues are recorded as nonoperating income in the statements of revenues, expenses and changes in net assets.

Retirement Plan

CPA contributes to the Northern Mariana Islands Retirement Fund (the Fund), a cost-sharing multiple employer defined benefit pension plan administered by the CNMI. The Fund provides retirement, security and other benefits to employees, and their spouses and dependents, of the CNMI Government and CNMI agencies, instrumentalities, and public corporations. CNMI Public Law 6-17, the Northern Mariana Retirement Fund Act of 1988 assigns the authority to establish and amend benefit provisions to the Fund's Board of Trustees. The Fund issues a publicly available financial report that includes financial statements and required supplementary information for the Fund. That report may be obtained by writing to the Northern Mariana Islands Retirement Fund, P.O. Box 501247, Saipan, MP, 96950-1247.

Plan members are required to contribute 6.5% and 9.0% of their annual covered salary for Class I and Class II members, respectively, and CPA is required to contribute at an actuarially determined rate. The current rate is 36.77% of annual covered payroll. The contribution requirements of plan members and CPA are established and may be amended by the Fund's Board of Trustees. CPA's recorded contributions to the Fund for the years ended September 30, 2008, 2007 and 2006 were \$1,818,905, \$1,976,243, \$2,084,913, respectively, equal to the required contributions for each year.

GASB Statement No. 45 requires employers to record other postemployment benefits (OPEB) expense for their contractually required contributions to the OPEB plan. CPA has complied with GASB Statement No. 45 by recording OPEB expense based on the statutory determined contribution rate of the Fund. It is the understanding of the management of CPA that the statutory determined contribution rate of the Fund incorporates both the pension liability and OPEB liability. GASB Statement No. 45 also requires detailed disclosure of information related to the OPEB plan and CPA management was unable to obtain this information from the Fund financial report. CPA management is unable to obtain the required disclosures and is of the opinion that such information must be obtained from the Fund. It is the position of the management of CPA that the Fund is solely responsible for disclosure of OPEB information.

Net Assets

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, requires CPA to establish net asset categories as follows:

- Invested in capital assets net of related debt; capital assets, net of accumulated depreciation, plus deferred bond issuance cost, less outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(2) Summary of Significant Accounting Policies, Continued

Net Assets, Continued

- Restricted:
 - Nonexpendable - Net assets subject to externally imposed stipulations that CPA maintain them permanently. For the years ended September 30, 2008 and 2007, CPA does not have nonexpendable restricted net assets.
 - Expendable - Net assets whose use by CPA is subject to externally imposed stipulations that can be fulfilled by actions of CPA pursuant to those stipulations or that expire by the passage of time.
- Unrestricted; Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. No liability is recorded for nonvesting accumulating rights to receive sick pay benefits. The accumulated vacation leave liability as of September 30, 2008 and 2007 is \$537,955 and \$747,803, respectively.

Operating and Non-Operating Revenues and Expenses

Operating revenues and expenses generally result directly from the operation and maintenance of all airports and seaports within the CNMI. Non-operating revenues and expenses result from capital and financing activities, Passenger Facility Charges and certain recurring income and costs.

New Accounting Standards

During fiscal year 2008, CPA implemented GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Post employment Benefits Other Than Pensions*, GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfer of Assets and Future Revenues* and GASB Statement No. 50, *Pension Disclosures an amendment of GASB Statements No. 25 and 27*. GASB Statement No. 45 establishes standards for the measurement, recognition, and display of other post employment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. 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 and includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. GASB Statement No. 50 more closely aligns the financial reporting requirements for pensions with those for other post-employment benefits. The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

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 CPA.

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 CPA.

In November 2007, GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*. GASB Statement No. 52 improves the quality of financial reporting by requiring endowments to report their land and other real estate investments at fair value, creating consistency in reporting among similar entities that exist to invest resources for the purpose of generating income. The provisions of this statement are effective for periods beginning after June 15, 2008. Management does not believe that the implementation of this statement will have a material effect on the financial statements of CPA.

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. GASB Statement No. 53 is intended to improve how state and local governments report information about derivative instruments - financial arrangements used by governments to manage specific risks or make investments - in their financial statements. 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 CPA.

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 disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(3) Deposits and Investments

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(3) Deposits and Investments, Continued

Deposits

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

- Category 1 Deposits that are federally insured or collateralized with securities held by CPA or its agent in CPA's name;
- Category 2 Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in CPA's name; or
- Category 3 Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in CPA's name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect 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, CPA'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 but not in CPA's name. CPA does not have a deposit policy for custodial credit risk.

As of September 30, 2008 and 2007, total cash and cash equivalents were \$3,910,939 and \$9,678,551, respectively, and the corresponding bank balances were \$4,507,931 and \$9,968,110, respectively. Of the bank balance amounts, \$3,411,380 and \$8,849,729, respectively, are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. The remaining amounts of \$1,096,551 and \$1,118,381, respectively, represent short-term investments held and administered by CPA's trustees in accordance with various trust agreements. Based on negotiated trust and custody contracts, all of these deposits were held in CPA's name by CPA's custodial financial institutions at September 30, 2008 and 2007. As of September 30, 2008 and 2007, bank deposits in the amount of \$100,000 were FDIC insured. CNMI law does not require component unit funds to be collateralized and thus CPA's funds, in excess of FDIC insurance, are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

Investments

Investments in U.S. Treasury obligations restricted for construction and debt service purposes represent the unused proceeds of the Airport Revenue Bonds and the Seaport Revenue Bonds. These investments are summarized as follows:

| <u>Airport Division</u> | <u>2008</u> | <u>2007</u> |
|---------------------------|------------------|------------------|
| Bond Reserve Fund | \$ 1,555,389 | \$ 1,525,233 |
| Construction Fund | 998,519 | 979,159 |
| Bond Fund | 284,982 | 262,205 |
| Maintenance and Operation | 464,713 | 404,586 |
| Revenue Fund | 448,588 | - |
| | <u>3,752,191</u> | <u>3,171,183</u> |

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(3) Deposits and Investments, Continued

Investments, Continued

| | <u>2008</u> | <u>2007</u> |
|---------------------------|----------------------|----------------------|
| <u>Seaport Division</u> | | |
| Bond Reserve Fund | 3,478,814 | 3,489,728 |
| Supplemental Reserve Fund | 8,038,346 | 8,059,119 |
| Reimbursement Fund | 5,806 | 5,693 |
| Bond Fund | 489,094 | 448,539 |
| Maintenance and Operation | 493,610 | 344,926 |
| Construction Fund | 557,219 | 3,101,624 |
| Interest Fund | 69,468 | 108,743 |
| Revenue Fund | 238,397 | - |
| | <u>13,370,754</u> | <u>15,558,372</u> |
| | <u>\$ 17,122,945</u> | <u>\$ 18,729,555</u> |

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 CPA or its agent in CPA'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 CPA'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 CPA'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.

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. With the exception of investments in U.S. government securities, which are explicitly or implicitly guaranteed by the United States government, all other investments must be rated in accordance with CPA's investment policy.

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, CPA will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. CPA's investments are held and administered by CPA's trustees in accordance with various trustee agreements and bond indentures. Based on negotiated trust and custody contracts, all of these investments were held by the counterparty, or by its trust department or agent but not in CPA's name by CPA's custodial financial institutions at September 30, 2008 and 2007. Accordingly, these investments are exposed to custodial credit risk.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(3) Deposits and Investments, Continued

Investments, Continued

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. CPA's investment policy limits investment maturities to one year to manage its exposure to fair value losses arising from increasing interest rates.

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 CPA. As of September 30, 2008 and 2007, there were no investments in any one issuer that exceeded 5% of total investments.

As of September 30, 2008 and 2007, investments at fair value consist of investments in U.S. Government money market placements.

(4) Receivables From Federal Grantor Agencies

Receivables from federal grantor agencies as of September 30, 2008 and 2007, are as follows:

| | <u>2008</u> | <u>2007</u> |
|---|--------------|----------------|
| <u>U.S. Department of Transportation</u> | | |
| <u>Federal Aviation Administration</u> | | |
| Saipan International Airport, AIP Project No. 3-69-0002-31/32/50/53 | \$ 425,924 | \$ 192,186 |
| Saipan International Airport, AIP Project No. 3-69-0002-37 | (50,079) | (50,079) |
| Saipan International Airport, AIP Project No. 3-69-0002-38/41/52/55 | - | 1,423,088 |
| Saipan International Airport, AIP Project No. 3-69-0002-43/56 | - | 322,246 |
| Saipan International Airport, AIP Project No. 3-69-0002-45/49 | (32,592) | (186,640) |
| Saipan International Airport, AIP Project No. 3-69-0002-48 | 21,341 | - |
| Saipan International Airport, AIP Project No. 3-69-0002-51 | - | 131,775 |
| Saipan International Airport, AIP Project No. 3-69-0002-54 | - | 17,692 |
| Saipan International Airport, AIP Project No. 3-69-0002-57 | 4,081 | - |
| Saipan International Airport, AIP Project No. 3-69-0002-58 | 580 | - |
| Rota International Airport, AIP Project No. 3-69-0003-19/20 | 30,741 | - |
| Master Plan Study (Pagan), AIP Project No. 3-69-0004-01 | - | 7,768 |
| Tinian International Airport, AIP Project No. 3-69-0011-15/17/19/20 | 463,090 | 675,502 |
| Tinian International Airport, AIP Project No. 3-69-0011-18 | <u>6,623</u> | <u>148,381</u> |
| | 869,709 | 2,681,919 |
| <u>Transportation Security Administration</u> | | |
| Homeland Security | 275,956 | - |
| Security reimbursement | 62,994 | 205,351 |
| National Explosives Detection Canine Team Program | 150,500 | - |
| <u>U.S. Department of the Interior</u> | | |
| OMIP | - | 110,436 |
| Rota Extension Runway | - | 332,041 |
| Tinian Terminal Building Expansion | - | 392,789 |
| <u>U.S. Department of Homeland Security</u> | | |
| Disaster Grants - Public Assistance (Presidentially Declared Disasters) | 108,201 | 147,274 |
| Law Enforcement Terrorist Prevention Program | - | 23,263 |

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(4) Receivables From Federal Grantor Agencies, Continued

| | <u>2008</u> | <u>2007</u> |
|--|---------------------|---------------------|
| <u>Passed Through from CNMI Government</u> | | |
| Rota Charter Flight | 54,112 | - |
| Tinian Harbor | <u>929</u> | <u>577,422</u> |
| | <u>\$ 1,522,401</u> | <u>\$ 4,470,495</u> |

Amounts due from the above agencies represent reimbursements due under grants for costs incurred for improvements of the CNMI airports and public assistance. Generally, under the grant agreements, the grantor agency funds a portion of the allowable costs incurred, ranging from 80% to 100%, with the remainder of project costs, if any, funded by CPA or other sources.

(5) Accounts Receivable from Operations

CPA extends credit to organizations and individuals, substantially all of whom are located in the CNMI, Japan, the United States and Korea. CPA's accounts receivable from operations as of September 30, 2008 and 2007, are as follows:

| | <u>2008</u> | <u>2007</u> |
|--------------------------------------|---------------------|---------------------|
| Accounts receivable | \$ 5,386,770 | \$ 6,183,222 |
| Less allowance for doubtful accounts | <u>(1,656,195)</u> | <u>(1,238,722)</u> |
| | <u>\$ 3,730,575</u> | <u>\$ 4,944,500</u> |

(6) Capital Assets

Capital asset balances consist of the following as of September 30, 2008 and 2007:

| | <u>Estimated Useful Lives</u> | <u>Balance October 1, 2007</u> | <u>Increases</u> | <u>Decreases</u> | <u>Balance September 30, 2008</u> |
|--|-----------------------------------|--|----------------------|------------------------|---|
| Assets not being depreciated: | | | | | |
| Construction in progress | | \$ 57,930,776 | \$ 16,671,609 | \$ (44,512,480) | \$ 30,089,905 |
| Land | | <u>464,429</u> | <u>-</u> | <u>-</u> | <u>464,429</u> |
| Total capital assets not being depreciated | | <u>58,395,205</u> | <u>16,671,609</u> | <u>(44,512,480)</u> | <u>30,554,334</u> |
| Capital assets being depreciated: | | | | | |
| Runway and improvements | 20 years | 69,076,791 | 23,254,831 | - | 92,331,622 |
| Other improvements | 3 - 10 years | 16,215,774 | 42,627 | - | 16,258,401 |
| Terminal facilities | 20 years | 69,581,642 | 21,299,911 | - | 90,881,553 |
| Terminal equipment | 2 - 10 years | 9,620,965 | 219,391 | - | 9,840,356 |
| Harbor facilities | 20 years | 62,101,850 | - | - | 62,101,850 |
| Grounds maintenance and shop equipment | 2 - 5 years | 509,692 | - | - | 509,692 |
| Fire and rescue equipment | 2 - 8 years | 11,477,584 | 32,138 | (3,542) | 11,506,180 |
| Office furniture and fixtures | 2 - 10 years | 871,010 | 34,487 | - | 905,497 |
| General transportation | 3 - 5 years | 929,612 | 81,186 | - | 1,010,798 |
| Other | 3 - 5 years | <u>2,392,367</u> | <u>2,224</u> | <u>-</u> | <u>2,394,591</u> |
| | | 242,777,287 | 44,966,795 | (3,542) | 287,740,540 |
| Less accumulated depreciation | | <u>(117,828,380)</u> | <u>(9,690,222)</u> | <u>(28,787)</u> | <u>(127,547,389)</u> |
| Total capital assets being depreciated | | <u>124,948,907</u> | <u>35,276,573</u> | <u>(32,329)</u> | <u>160,193,151</u> |
| Total capital assets, net | | <u>\$ 183,344,112</u> | <u>\$ 51,948,182</u> | <u>\$ (44,544,809)</u> | <u>\$ 190,747,485</u> |

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(6) Capital Assets, Continued

| | Estimated Useful Lives | Balance October 1, 2006 | Increases | Decreases | Balance September 30, 2007 |
|--|---------------------------|-------------------------------|----------------------|-----------------------|----------------------------------|
| Assets not being depreciated: | | | | | |
| Construction in progress | | \$ 23,664,973 | \$ 37,159,576 | \$ (2,893,773) | \$ 57,930,776 |
| Land | | 464,429 | - | - | 464,429 |
| Total capital assets not being depreciated | | <u>24,129,402</u> | <u>37,159,576</u> | <u>(2,893,773)</u> | <u>58,395,205</u> |
| Capital assets being depreciated: | | | | | |
| Runway and improvements | 20 years | 69,076,791 | - | - | 69,076,791 |
| Other improvements | 3 - 10 years | 16,197,486 | 28,340 | (10,052) | 16,215,774 |
| Terminal facilities | 20 years | 69,083,593 | 498,049 | - | 69,581,642 |
| Terminal equipment | 2 - 10 years | 9,592,221 | 31,569 | (2,825) | 9,620,965 |
| Harbor facilities | 20 years | 61,997,300 | 104,550 | - | 62,101,850 |
| Grounds maintenance and shop equipment | 2 - 5 years | 506,735 | 2,957 | - | 509,692 |
| Fire and rescue equipment | 2 - 8 years | 10,481,756 | 995,828 | - | 11,477,584 |
| Office furniture and fixtures | 2 - 10 years | 824,171 | 46,839 | - | 871,010 |
| General transportation | 3 - 5 years | 879,641 | 83,990 | (34,019) | 929,612 |
| Other | 3 - 5 years | 871,469 | 1,520,898 | - | 2,392,367 |
| | | 239,511,163 | 3,313,020 | (46,896) | 242,777,287 |
| Less accumulated depreciation | | (107,254,453) | (10,607,952) | 34,025 | (117,828,380) |
| Total capital assets being depreciated | | <u>132,256,710</u> | <u>(7,294,932)</u> | <u>(12,871)</u> | <u>124,948,907</u> |
| Total capital assets, net | | \$ <u>156,386,112</u> | \$ <u>29,864,644</u> | \$ <u>(2,906,644)</u> | \$ <u>183,344,112</u> |

CPA leases significant portions of airport terminal facilities and certain grounds and improvements to concessionaires, airlines, and other lessees. CPA additionally holds title to 13,646,163 square meters of land on the islands of Saipan, Tinian and Rota for seaport and airport operations. No value for this land has been recorded on CPA's books as an appraisal has not been performed.

Land acquired by CPA on the islands of Saipan and Rota from the former Marianas Public Land Corporation for seaport improvement and use has been recorded on CPA's books at its estimated fair market value. This estimated value is based on a land valuation established by Article VIII of the Marianas Political Status Commission as contained in the Section-by-Section Analysis of the Covenant to Establish a Commonwealth of the Northern Mariana Islands, dated February 15, 1975, for land of a similar nature leased by the CNMI to the U.S. Government.

(7) Revenue Bonds Payable

Airport Division

On March 26, 1998, CPA issued \$20,050,000 of tax-exempt airport revenue bonds which in part were used for a current refunding of \$8,250,000 of 1987 Series B tax-exempt airport revenue bonds. The refunding was undertaken to consolidate existing bonds with new bonds issued for the purpose of financing various airport projects and to reduce total future debt service payments. The reacquisition price exceeded the net carrying amount of the old debt by \$503,906. This amount was netted against the new debt and is being amortized over the refunded debt's life, which is shorter than the life of the new debt. The transaction also resulted in an economic gain of \$688,620 and an increase of \$7,616,151 in future debt service payments. Interest on the bonds is payable semi-annually at 6.25% on March 15 and September 15 of each year.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(7) Revenue Bonds Payable, Continued

Airport Division, Continued

Revenue bonds payable as of September 30, 2008 and 2007, consist of the following:

| | <u>2008</u> | <u>2007</u> |
|---|----------------------|----------------------|
| Special Revenue Bonds, tax exempt, 1998 Senior Series A: interest and annual installments payable to the Bond Trustee between 2009 and 2028 are listed below. | \$ 16,810,000 | \$ 17,230,000 |
| Current portion | <u>1,435,000</u> | <u>420,000</u> |
| Long-term portion | <u>\$ 15,375,000</u> | <u>\$ 16,810,000</u> |

Principal installments payable by CPA to the Bond Trustee through the life of the 1998 Series A, Airport Revenue Bonds, are due on March 15.

Principal and interest payments for subsequent years ending September 30, are as follows:

| <u>Year ending September 30,</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|--------------------------------------|----------------------|----------------------|----------------------|
| 2009 | \$ 1,435,000 | \$ 1,036,719 | \$ 2,471,719 |
| 2010 | 445,000 | 947,031 | 1,392,031 |
| 2011 | 470,000 | 918,438 | 1,388,438 |
| 2012 | 505,000 | 887,969 | 1,392,969 |
| 2013 | 530,000 | 855,625 | 1,385,625 |
| 2014 - 2018 | 3,210,000 | 3,719,063 | 6,929,063 |
| 2019 - 2023 | 4,335,000 | 2,547,969 | 6,882,969 |
| 2024 - 2028 | <u>5,880,000</u> | <u>963,750</u> | <u>6,843,750</u> |
| | <u>\$ 16,810,000</u> | <u>\$ 11,876,564</u> | <u>\$ 28,686,564</u> |

Seaport Division

On March 26, 1998, CPA issued \$33,775,000 of Senior Series A tax-exempt seaport revenue bonds which in part were used for a current refunding of \$22,470,000 of 1995 Series A tax-exempt seaport revenue bonds. The refunding was undertaken to consolidate existing debt with new debt issued for the purpose of financing various seaport projects and to reduce total future debt service payments. The reacquisition price exceeded the net carrying amount of the old debt by \$1,345,593. This amount was netted against the new debt and is being amortized over the refunded debt's life, which is shorter than the life of the new debt. The transaction also resulted in an economic gain of \$1,724,777 and a decrease of \$6,983,345 in future debt service payments. Interest on the bonds is payable semi-annually at 6.6% on March 15 and September 15 of each year.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(7) Revenue Bonds Payable, Continued

Seaport Division, Continued

On September 21, 2005, CPA issued \$7,225,000 of Senior Series A tax-exempt seaport revenue bonds for the purpose of financing (including reimbursing itself for) the purchase, acquisition, construction, reconstruction, repair, renovation, improvement or expansion of CPA's seaports. Pursuant to Section 2.04(A)(9) of the 1998 Senior Series A Seaport Revenue Bonds Indenture Agreement dated March 1, 1998 and as supplemented by a First Supplemental Indenture dated March 1, 2000, CPA entered into a Second Supplemental Indenture for the issuance of the 2005 Senior Series A bonds. Interest on the bonds is payable semi-annually at 5.5% on March 15 and September 15 of each year.

Revenue bonds payable as of September 30, 2008 and 2007, consist of the following:

| | <u>2008</u> | <u>2007</u> |
|---|----------------------|----------------------|
| Special Revenue Bonds, tax exempt, 1998 Senior Series A: interest and annual installments payable to the Bond Trustee between 2009 and 2028 are listed below. | \$ 28,425,000 | \$ 29,120,000 |
| Special Revenue Bonds, tax exempt, 2005 Senior Series A: interest and annual installments payable to the Bond Trustee between 2009 and 2031 are listed below. | 7,075,000 | 7,225,000 |
| Deferred costs of debt refunding on 1998 Senior Series A bonds | (1,030,410) | (1,069,062) |
| Discount on 2005 Senior Series A bonds | <u>(109,932)</u> | <u>(114,711)</u> |
| | 34,359,658 | 35,161,227 |
| Current portion | <u>895,000</u> | <u>845,000</u> |
| Long-term portion | <u>\$ 33,464,658</u> | <u>\$ 34,316,227</u> |

Principal installments payable by CPA to the Bond Trustee through the life of the 1998 Senior Series A and the 2005 Senior Series A, Special Revenue Bonds, are due on March 15.

Principal and interest payments for subsequent years ending September 30, are as follows:

| <u>Year ending</u> <u>September 30,</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|--|----------------------|----------------------|----------------------|
| 2009 | \$ 895,000 | \$ 2,236,493 | \$ 3,131,493 |
| 2010 | 950,000 | 2,177,368 | 3,127,368 |
| 2011 | 1,015,000 | 2,114,393 | 3,129,393 |
| 2012 | 1,075,000 | 2,047,402 | 3,122,402 |
| 2013 | 1,145,000 | 1,976,233 | 3,121,233 |
| 2014 - 2018 | 6,895,000 | 8,646,110 | 15,541,110 |
| 2019 - 2023 | 9,355,000 | 6,057,699 | 15,412,699 |
| 2024 - 2028 | 12,670,000 | 2,547,050 | 15,217,050 |
| 2029 - 2031 | <u>1,500,000</u> | <u>126,499</u> | <u>1,626,499</u> |
| | <u>\$ 35,500,000</u> | <u>\$ 27,929,247</u> | <u>\$ 63,429,247</u> |

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(7) Revenue Bonds Payable, Continued

Seaport Division, Continued

Additionally, CPA has resolved to hold \$8,000,000 in the Seaport supplemental reserve fund. The supplemental reserve fund was established pursuant to the First Supplemental Indenture dated March 1, 2000 for the purpose of providing funding and maintenance for the 1998 Senior Series A Seaport Bonds. At September 30, 2008 and 2007, total deposits in the Seaport supplemental reserve fund amounted to \$8,038,346 and \$8,059,119, respectively.

Bond Redemption

In accordance with the Airport and Seaport Bond Indenture Agreements, Section 4.01, terms of redemption of the 1998 Senior Series A Bonds are as follows:

- a) Optional redemption - The 1998 Senior Bonds for the airport are subject to redemption prior to their respective stated maturities on or after March 15, 2013, at the option of CPA, from any source of available funds, as a whole on any date, or in part on any Interest Payment Date and by lot within a maturity, at the Redemption Prices (expressed as percentages of principal amount) set forth in the table below plus interest accrued thereon to the date fixed for redemption:

| <u>Redemption Dates</u> | <u>Redemption Prices</u> |
|---------------------------------------|--------------------------|
| March 15, 2013 through March 14, 2014 | 102% |
| March 15, 2014 through March 14, 2015 | 101% |
| March 15, 2015 and thereafter | 100% |

The option may only be exercised by depositing with the Trustee, prior to giving notice of such redemption in accordance with Section 4.03, moneys or Investment Securities sufficient in amount and maturing in a timely manner to provide for such redemption including moneys or Investment Securities sufficient to pay the premium upon such optional redemption if any. CPA shall notify the Trustee in writing at least 60 days prior to the date to be fixed for redemption of its intention to exercise its redemption option and specifying the amount and the maturities of the bonds to be redeemed and, if appropriate, the Mandatory Sinking Accounts Payments to which the bonds redeemed are to be allocated.

The 1998 Senior Bonds for the seaport are not subject to optional redemption prior to their stated maturity.

- b) Mandatory redemption - The 1998 Senior Bonds for the airport and seaport are subject to mandatory redemption, in part on the earliest Interest Payment Date for which notice can be given after completion of the Project or after three years from the date of issuance of the 1998 Senior Bonds, from moneys transferred from the 1998 Series A Account within the Construction Fund to the Optional Redemption Fund in accordance with Section 3.03, at a redemption price equal to 100% of the principal amount of such 1998 Senior Bonds to be redeemed plus accrued interest, if any, to the date fixed for redemption, without premium. On July 17, 2009, CPA received notice of redemption related to its 1998 Senior Series A Airport Bonds amounting to \$990,000 due September 15, 2009, payable from its Construction Fund account. Accordingly, it is included in the revenue bonds payable, current portion in the accompanying financial statements.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(7) Revenue Bonds Payable, Continued

Bond Redemption, Continued

- c) Insurance or condemnation award - At the option of CPA, prior to their stated maturity as a whole or in part by lot, the 1998 Senior Bonds for the airport and seaport are subject to redemption from the proceeds of any insurance or condemnation awards received by CPA due to a casualty loss or governmental taking of CPA's airport and seaport facilities, if such proceeds are not used to repair or replace such facilities under the circumstances and upon the conditions prescribed in Section 6.17 at the principal amount thereof and interest accrued thereon to the date fixed for redemption, without premium.
- d) Mandatory sinking account - The 1998 Senior Bonds for the airport and seaport are also subject to redemption prior to their stated maturity in part, by lot, from Mandatory Sinking Account Payments established for such maturity upon payment of the principal amount thereof and accrued interest thereon to the date fixed for redemption, without premium.

In accordance with the Second Supplemental Indenture of the Seaport Bond Indenture Agreement, Section 15.03, terms of redemption of the 2005 Senior Series A Bonds are as follows:

- a) Optional redemption - The 2005 Senior Series A Bonds maturing on or after March 15, 2016 are subject to redemption prior to their respective stated maturities, at the option of CPA, from lawfully available funds deposited in the Optional Redemption Fund, as a whole or in part on any date on or after March 15, 2015, at the following respective redemption prices (expressed as percentages of the principal amount of the 2005 Bonds to be redeemed) plus accrued interest thereon to the date fixed for redemption:

| <u>Redemption Dates</u> | <u>Redemption Prices</u> |
|---------------------------------------|--------------------------|
| March 15, 2015 through March 14, 2016 | 101.0% |
| March 15, 2016 through March 14, 2017 | 100.5% |
| March 15, 2017 and thereafter | 100.0% |

- b) Mandatory redemption - The 2005 Senior Series A Bonds are subject to mandatory redemption upon notice of completion of the 2005 Project (purchase, acquisition, construction/reconstruction, repair, renovation, improvement, certain capital improvements or expansion of CPA's seaports) or after three years from the date of issuance of the 2005 Senior Series A Bonds from moneys transferred from the Construction Fund to the Optional Redemption Fund in accordance with Section 3.03, at a redemption price equal to the principal amount thereof, without premium, together with accrued interest to the date fixed for redemption.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(7) Revenue Bonds Payable, Continued

Bond Redemption, Continued

- c) Insurance or condemnation award - At the option of CPA and prior to their stated maturity, the 2005 Senior Series A Bonds are subject to redemption from proceeds of any insurance or condemnation awards received by CPA due to a casualty loss or governmental taking of CPA's seaport facilities, if such proceeds are not used to repair or replace such facilities, under the circumstances and upon the conditions prescribed in Section 6.17 of the bond indenture, at a redemption price equal to the principal amount thereof, without premium, together with accrued interest to the date fixed for redemption.
- d) Mandatory sinking account - The 2005 Senior Series A Bonds maturing are also subject to redemption prior to their stated maturity in part, by lot, from Mandatory Sinking Account Payments established for such maturity d), at a redemption price equal to the principal amount thereof, without premium, together with accrued interest to the date fixed for redemption.

Pledge of Future Revenues

CPA has pledged future gross revenues to repay \$20,050,000 and \$33,775,000 in 1998 Senior Series A and \$7,225,000 of 2005 Senior Series A tax-exempt special revenue bonds. Proceeds from the bonds provided financing for capital assets. The bonds are payable from pledged gross revenues. The bonds are payable through fiscal years 2028, 2028 and 2031, respectively. The total principal and interest payable for the remainder of the life of these bonds is \$92,815,518 and 97,436,503 at September 30, 2008 and 2007, respectively. Pledged gross revenues received during the years ended September 30, 2008 and 2007 were \$13,799,457 and \$15,152,900, respectively. Debt service payments during the years ended September 30, 2008 and 2007 amounted to \$4,620,985 and \$4,480,128 representing 33% and 30%, respectively, of pledged gross revenues.

The bond indentures contain several restrictive covenants, including restrictions on the use of bond proceeds. Management of CPA is of the opinion that CPA was in compliance with all significant covenants as of September 30, 2008, except for the collection of gross revenues requirement related to the Airport and Seaport bond indentures. Section 6.11 of the Airport and Seaport Bond Indenture Agreements (Indenture) state that CPA shall impose, levy, enforce and collect such fees/dockage, entry and wharfage fees, tariffs, lease rentals, licensing fees and other fees and charges in aggregate amount with respect to each fiscal year to produce gross revenues to comply with subsections (A)(1), (A)(2), (A)(3) and (A)(4) of Section 6.11. CPA failed to comply with this requirement for the Airport Division and the Seaport Division for the years ended September 30, 2008 and 2007.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(7) Revenue Bonds Payable, Continued

Section 6.11(B) of the Indentures state that if the financial statements prepared pursuant to Section 6.06(B) of the Indentures reflect that at the end of a fiscal year, net revenues are less than the amount required by Section 6.11(A) for such fiscal year or if the revenues are less than the aggregate amount of all transfers required by Section 5.02(a) through (e) for such fiscal year, CPA shall not be in default under Section 7.01 if within sixty days after the date of such financial statements or the end of the fiscal year, CPA shall employ an independent consultant to make recommendations as to a revision of the rates, fees and charges or the methods of operation of the airports and seaports. If such recommendations fail to meet the requirements of Section 6.11(a), such deficiency will constitute an event of default under Section 7.01. CPA hired an independent consultant for the Airport and Seaport Divisions during the year ended September 30, 2008 to comply with Section 6.11(B) of the Indentures.

Changes in long-term liabilities for the years ended September 30, 2008 and 2007, are as follows:

| | Balance October 1, 2007 | <u>Additions</u> | <u>Reductions</u> | Balance September 30, 2008 | Due Within One Year |
|----------------------------------|-------------------------------|-------------------|-----------------------|----------------------------------|---------------------------|
| Bonds payable: | | | | | |
| Airport 1998 Senior Series A | \$ 17,230,000 | \$ - | \$ (420,000) | \$ 16,810,000 | \$ 1,435,000 |
| Seaport 1998 Senior Series A | 29,120,000 | - | (695,000) | 28,425,000 | 740,000 |
| Seaport 2005 Senior Series A | 7,225,000 | - | (150,000) | 7,075,000 | 155,000 |
| Note payable | 6,026,715 | - | (223,105) | 5,803,610 | - |
| Deferred amounts: | | | | | |
| Deferred costs of debt refunding | (1,069,062) | - | 38,652 | (1,030,410) | - |
| Discount on bonds | (114,711) | - | 4,779 | (109,932) | - |
| | 58,417,942 | - | (1,444,674) | 56,973,268 | 2,330,000 |
| Other: | | | | | |
| Compensated absences | 747,803 | 356,097 | (565,945) | 537,955 | 275,621 |
| Accrued interest | - | 304,994 | - | 304,994 | - |
| | <u>\$ 59,165,745</u> | <u>\$ 661,091</u> | <u>\$ (2,010,619)</u> | <u>\$ 57,816,217</u> | <u>\$ 2,605,621</u> |
| | Balance October 1, 2006 | <u>Additions</u> | <u>Reductions</u> | Balance September 30, 2007 | Due Within One Year |
| Bonds payable: | | | | | |
| Airport 1998 Senior Series A | \$ 17,625,000 | \$ - | \$ (395,000) | \$ 17,230,000 | \$ 420,000 |
| Seaport 1998 Senior Series A | 29,775,000 | - | (655,000) | 29,120,000 | 695,000 |
| Seaport 2005 Senior Series A | 7,225,000 | - | - | 7,225,000 | 150,000 |
| Note payable | 6,676,553 | - | (649,838) | 6,026,715 | 1,281,659 |
| Deferred amounts: | | | | | |
| Deferred costs of debt refunding | (1,105,940) | - | 36,878 | (1,069,062) | - |
| Discount on bonds | (119,490) | - | 4,779 | (114,711) | - |
| | 60,076,123 | - | (1,658,181) | 58,417,942 | 2,546,659 |
| Other: | | | | | |
| Compensated absences | 640,952 | 469,934 | (363,083) | 747,803 | 242,557 |
| | <u>\$ 60,717,075</u> | <u>\$ 469,934</u> | <u>\$ (2,021,264)</u> | <u>\$ 59,165,745</u> | <u>\$ 2,789,216</u> |

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(8) Note Payable to Related Party

CPA's note payable is as follows:

| | <u>2008</u> | <u>2007</u> |
|---|---------------------|---------------------|
| Promissory note due to the Commonwealth Development Authority (CDA) (a component unit of the CNMI), interest at 2.5% per annum, with maturity date of November 16, 2014. Principal and interest payments in the amount of \$204,113 are due quarterly. Beginning January 2008, principal and interest payments have been deferred for five and two years, respectively. | \$ 5,803,610 | \$ 6,026,715 |
| Less amounts due within one year | <u>-</u> | <u>1,281,659</u> |
| Long-term debt | <u>\$ 5,803,610</u> | <u>\$ 4,745,056</u> |

The CDA obligation is subordinate to CPA's obligation for the Seaport bonds.

Principal and interest payments for subsequent years ending September 30, are as follows:

| <u>Year ending September 30,</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|--------------------------------------|---------------------|-------------------|---------------------|
| 2009 | \$ - | \$ - | \$ - |
| 2010 | - | 619,575 | 619,575 |
| 2011 | - | 76,057 | 76,057 |
| 2012 | - | 57,373 | 57,373 |
| 2013 | 4,762,833 | 38,217 | 4,801,050 |
| 2014 - 2018 | <u>1,040,777</u> | <u>20,097</u> | <u>1,060,874</u> |
| | <u>\$ 5,803,610</u> | <u>\$ 811,319</u> | <u>\$ 6,614,929</u> |

(9) Risk Management

CPA is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. CPA has elected to purchase commercial insurance from independent third parties for the risks of losses at its airport facilities to which it is exposed. CPA has also elected to purchase partial commercial insurance from independent third parties for risk of losses at its seaport facilities to which it is exposed. Except as disclosed in note 13, settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

(10) Related Party Transactions

Total related party transactions for the years ended September 30, 2008 and 2007, and the related receivable and payable balances, are as follows:

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(10) Related Party Transactions, Continued

| | 2008 | | | |
|--|---|---------------------|---------------------|---------------------|
| | <u>Revenues and Capital Contributions</u> | <u>Expenses</u> | <u>Receivables</u> | <u>Payables</u> |
| Commonwealth Development Authority | \$ - | \$ 129,395 | \$ - | \$ - |
| Commonwealth Utilities Corporation | - | 881,460 | 4,515,491 | - |
| CNMI Government | 2,078,701 | 122,675 | - | 1,475,196 |
| Northern Mariana Islands Retirement Fund | - | 1,818,905 | - | 709,739 |
| | <u>\$ 2,078,701</u> | <u>\$ 2,952,435</u> | <u>\$ 4,515,491</u> | <u>\$ 2,184,935</u> |
| | 2007 | | | |
| | <u>Revenues and Capital Contributions</u> | <u>Expenses</u> | <u>Receivables</u> | <u>Payables</u> |
| Commonwealth Development Authority | \$ - | \$ 146,306 | \$ - | \$ - |
| Commonwealth Utilities Corporation | - | 597,068 | 4,700,947 | 39,265 |
| CNMI Government | 3,492,996 | 125,403 | - | 1,352,521 |
| Northern Mariana Islands Retirement Fund | - | 1,976,243 | - | 1,132,424 |
| Other | 9,754 | - | 53,181 | - |
| | <u>\$ 3,502,750</u> | <u>\$ 2,845,020</u> | <u>\$ 4,754,128</u> | <u>\$ 2,524,210</u> |

A note payable to CDA amounted to \$5,803,610 and \$6,026,715 at September 30, 2008 and 2007, respectively. Interest expense on this note for the years ended September 30, 2008 and 2007 amounted to \$129,395 and \$146,306, respectively.

CPA and the Commonwealth Utilities Corporation (CUC) have entered into Memorandums of Agreement (MOAs) specifying terms and conditions of the construction of a Sewerline Project. CPA, as signatory party to the project contract, paid for all payments of the project. CUC has agreed to reimburse CPA \$4,700,947 of project costs.

In accordance with the MOAs, CUC shall make installments payments over a term not to exceed five years, commencing on July 1, 2008, with interest at 6.25%. CPA has the right of offset/credit utility charges in lieu of payments. The offset/credit procedure shall terminate when CUC begins actual payments on the amount owed or total offset/credits equal the principal amount. At September 30, 2008 and 2007, the receivable from CUC amounted to \$4,515,491 and \$4,700,947, respectively.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(10) Related Party Transactions, Continued

On June 30, 2008, CPA and CUC entered into an amended and superceding MOA for the repayment of wharfage fees due to CPA amounting to \$3,385,131 with interest at 6.25%. In accordance with the MOA, CPA has the right to offset utility charges at the Port of Saipan and other ancillary accounts against the receivable from CUC beginning in July 1, 2008. Total utility charges offset during the year ended September 30, 2008 amounted to \$24,567. Due to the potential uncollectability of the remaining amount due, the remaining receivable has been fully allowed for.

The Seaport Division recorded accounts receivable amounting to \$53,181 at September 30, 2007 from a company in which a former Board member has an interest.

As of September 30, 2008 and 2007, CPA has liabilities of \$709,739 and \$1,132,424, respectively, to the Northern Mariana Islands Retirement Fund related to the increase in employer contribution rate from 24% to 36.77% inclusive of \$242,627 representing 25% penalty on the original outstanding balance.

In accordance with Public Law No. 14-74, the CNMI government contributed \$1,290,331 and \$707,503 during the years ended September 30, 2008 and 2007, respectively, towards CPA's airline incentive program. In addition, CPA recorded capital contributions of \$788,370 and \$2,785,493 from the CNMI government during the years ended September 30, 2008 and 2007, respectively. The amount due to the CNMI government relates to the 1% Public Auditor fee of \$1,475,196 and \$1,352,521 at September 30, 2008 and 2007, respectively.

(11) Commitment and Contingencies

Commitment

CPA's Airport Division leases rental car concession booths, office space, other ground space, and an electronic scanning device. The Seaport Division leases land and warehouse space. Lease terms range from one to fifteen years and in most instances contain provisions for percentage rent. Concession and lease income for the years ended September 30, 2008 and 2007, amounted to \$4,476,494 and \$4,213,807, respectively. Minimum future lease income is as follows:

| <u>Year ending September 30,</u> | <u>Minimum Lease Income Due</u> |
|--------------------------------------|-------------------------------------|
| 2009 | \$ 2,369,729 |
| 2010 | 1,992,501 |
| 2011 | 1,777,837 |
| 2012 | 1,698,928 |
| 2013 | 1,688,521 |
| 2014 - 2018 | 7,544,752 |
| 2019 - 2023 | 5,816,825 |
| 2024 - 2028 | 2,940,649 |
| 2029 - 2033 | 2,315,164 |
| 2034 - 2038 | 2,746,726 |
| 2039 - 2043 | 3,275,755 |
| 2044 - 2048 | <u>1,509,987</u> |
| | <u>\$ 35,677,374</u> |

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(11) Commitment and Contingencies, Continued

Contingencies

CPA incurred a combined loss before capital contributions and transfers from its two divisions of \$10,765,017 and \$9,632,812 during the years ended September 30, 2008 and 2007, respectively. Management's plans to increase revenues and/or decrease costs are as follows:

- a) Continue implementation of cost cutting measures.
- b) Explore non-aviation revenue generating options.
- c) Explore non-harbor revenue generating options.
- d) Implement recommendations from an independent consultant relating to rate structures at the Airport.

Management believes that these efforts will be successful in reducing future losses of CPA.

CPA participates in a number of federally assisted grant programs funded by the United States Government. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. Cumulative questioned costs of \$508,458 have been set forth in CPA's Single Audit Report for the year ended September 30, 2008. The ultimate disposition of these questioned costs can be determined only by final action of the respective grantor agencies. Therefore, no provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements. As of and for the year ended September 30, 2008, CPA recorded \$1,248,266, related to questioned costs for various Airport Improvement Program grants reported in CPA's audits of fiscal years 2005 through 2007 as an accrued expense liability and other expense as the management of CPA expects to pay the grantor agency for these questioned costs.

On May 19, 2005, CPA received a Unilateral Administrative Order (UAO) issued by the U.S. Environmental Protection Agency (EPA) concerning activities at the maintenance and waste burning facilities at the Saipan International Airport. For the years ended September 30, 2008 and 2007, CPA incurred cleanup expenditures related to the UAO totaling \$66,574 and \$166,236, respectively. The ultimate cost of the cleanup has not been determined; accordingly, no provision has been accrued at September 30, 2008 for additional costs that may be incurred.

(12) Major Customers

Aviation fees received by CPA are comprised of facility service charges and landing fees from air carriers providing scheduled flight service to CNMI airports, substantially all of which are located in the CNMI, Japan, United States, China and Korea. Seaport fees received by CPA are primarily comprised of wharfage fees on cargo from the CNMI, Japan, United States, the Philippines and other Asian countries. Lease revenue is derived primarily from Saipan International Airport's prime concessionaire who is located in the CNMI.

During the years ended September 30, 2008 and 2007, three customers accounted for 48% and 57% of the total operating revenues of the Airport Division, and one customer accounted for 17% and 18% of the total operating revenues of the Seaport Division during the years ended September 30, 2008 and 2007, respectively.

COMMONWEALTH PORTS AUTHORITY

Notes to Financial Statements
September 30, 2008 and 2007

(13) Typhoon Damages

During the year ended September 30, 2006, CPA received insurance proceeds relating to Typhoon Chaba damages. CPA recorded the proceeds as accrued expenses and expects to liquidate the accrual as typhoon repair costs are incurred. At September 30, 2008 and 2007, the remaining accrued expenses total \$1,720,478.

(14) Restatement

During the year ended September 30, 2008, management determined that operations receivable, net, passenger facility charge revenues and beginning net assets were misstated as of and for the year ended September 30, 2007 as follows:

| | <u>2007</u> <u>As Originally Stated</u> | <u>2007</u> <u>As Restated</u> |
|------------------------------------|--|-----------------------------------|
| Operations receivable, net | \$ 4,540,961 | \$ 4,944,500 |
| Passenger facility charge revenues | \$ 1,940,712 | \$ 1,925,589 |
| Net assets October 1, 2006 | \$ 131,817,464 | \$ 132,236,126 |

COMMONWEALTH PORTS AUTHORITY

Combining Schedule of Net Assets
September 30, 2008

| <u>ASSETS</u> | Airport Division | Seaport Division | Elimination | Total |
|---|-----------------------|----------------------|---------------------|-----------------------|
| Current assets: | | | | |
| Cash and cash equivalents | \$ 3,509,300 | \$ 401,639 | \$ - | \$ 3,910,939 |
| Receivables: | | | | |
| Grantor agencies | 1,441,123 | 81,278 | - | 1,522,401 |
| Operations, net | 3,318,898 | 411,677 | - | 3,730,575 |
| Related parties, net | 855,878 | - | - | 855,878 |
| Due from Seaport Division | 137,607 | - | (137,607) | - |
| Officers and employees | 57,898 | 3,029 | - | 60,927 |
| Prepaid expenses | 87,373 | - | - | 87,373 |
| Investments, restricted for construction and debt service purposes | <u>3,752,191</u> | <u>13,370,754</u> | <u>-</u> | <u>17,122,945</u> |
| Total current assets | <u>13,160,268</u> | <u>14,268,377</u> | <u>(137,607)</u> | <u>27,291,038</u> |
| Noncurrent assets: | | | | |
| Deferred bond issue costs | 521,631 | 939,666 | - | 1,461,297 |
| Receivable from related party, net | 3,659,613 | - | - | 3,659,613 |
| Capital assets, net | <u>140,016,580</u> | <u>50,730,905</u> | <u>-</u> | <u>190,747,485</u> |
| Total noncurrent assets | <u>144,197,824</u> | <u>51,670,571</u> | <u>-</u> | <u>195,868,395</u> |
| | <u>\$ 157,358,092</u> | <u>\$ 65,938,948</u> | <u>\$ (137,607)</u> | <u>\$ 223,159,433</u> |
| <u>LIABILITIES AND NET ASSETS</u> | | | | |
| Current liabilities: | | | | |
| Revenue bonds payable, current portion | \$ 1,435,000 | \$ 895,000 | \$ - | \$ 2,330,000 |
| Contractors payable | 3,211,212 | 338,461 | - | 3,549,673 |
| Trade and other payables | 269,551 | 9,106 | - | 278,657 |
| Due to related parties | 1,930,609 | 254,326 | - | 2,184,935 |
| Due to Airport Division | - | 137,607 | (137,607) | - |
| Accrued expenses | 1,474,012 | 1,799,668 | - | 3,273,680 |
| Deferred income | 5,625 | - | - | 5,625 |
| Compensated absences, current portion | <u>249,318</u> | <u>26,303</u> | <u>-</u> | <u>275,621</u> |
| Total current liabilities | 8,575,327 | 3,460,471 | (137,607) | 11,898,191 |
| Accrued interest payable | - | 304,994 | - | 304,994 |
| Compensated absences, net of current portion | 228,426 | 33,908 | - | 262,334 |
| Revenue bonds payable, net of current portion | 15,375,000 | 33,464,658 | - | 48,839,658 |
| Note payable to related party | <u>-</u> | <u>5,803,610</u> | <u>-</u> | <u>5,803,610</u> |
| Total liabilities | <u>24,178,753</u> | <u>43,067,641</u> | <u>(137,607)</u> | <u>67,108,787</u> |
| Net assets: | | | | |
| Invested in capital assets, net of related debt | 123,728,211 | 11,507,303 | - | 135,235,514 |
| Restricted | 3,752,191 | 13,370,754 | - | 17,122,945 |
| Unrestricted | <u>5,698,937</u> | <u>(2,006,750)</u> | <u>-</u> | <u>3,692,187</u> |
| Total net assets | <u>133,179,339</u> | <u>22,871,307</u> | <u>-</u> | <u>156,050,646</u> |
| | <u>\$ 157,358,092</u> | <u>\$ 65,938,948</u> | <u>\$ (137,607)</u> | <u>\$ 223,159,433</u> |

See Accompanying Independent Auditors' Report.

COMMONWEALTH PORTS AUTHORITY

Combining Schedule of Revenues, Expenses and Changes in Net Assets
Year Ended September 30, 2008

| | Airport Division | Seaport Division | Elimination | Total |
|--|-----------------------|----------------------|-------------|-----------------------|
| Operating revenues: | | | | |
| Concession and lease income | \$ 3,399,801 | \$ 1,076,693 | \$ - | \$ 4,476,494 |
| Aviation fees | 4,120,192 | - | - | 4,120,192 |
| Seaport fees | - | 3,532,991 | - | 3,532,991 |
| Other | 1,110,327 | 559,453 | - | 1,669,780 |
| | <u>8,630,320</u> | <u>5,169,137</u> | - | <u>13,799,457</u> |
| Less bad debt | (198,974) | (252,255) | - | (451,229) |
| Operating revenues, net | <u>8,431,346</u> | <u>4,916,882</u> | - | <u>13,348,228</u> |
| Operating expenses: | | | | |
| Depreciation and amortization | 7,271,917 | 2,418,305 | - | 9,690,222 |
| Salaries and wages | 4,207,888 | 774,360 | - | 4,982,248 |
| Employee benefits | 1,716,586 | 307,908 | - | 2,024,494 |
| Insurance | 713,683 | 1,088,827 | - | 1,802,510 |
| Utilities | 797,526 | 83,934 | - | 881,460 |
| Contractual services | 678,117 | 81,147 | - | 759,264 |
| Repairs and maintenance | 316,576 | 33,669 | - | 350,245 |
| Supplies | 220,807 | 24,093 | - | 244,900 |
| Professional fees | 173,611 | 52,046 | - | 225,657 |
| Travel | 95,562 | 23,565 | - | 119,127 |
| Training | 86,457 | - | - | 86,457 |
| Promotion and advertising | 33,948 | 1,624 | - | 35,572 |
| Other | 1,193,300 | 82,206 | - | 1,275,506 |
| Total operating expenses | <u>17,505,978</u> | <u>4,971,684</u> | - | <u>22,477,662</u> |
| Operating loss | <u>(9,074,632)</u> | <u>(54,802)</u> | - | <u>(9,129,434)</u> |
| Non-operating revenues (expenses): | | | | |
| Passenger facility charges | 2,160,681 | - | - | 2,160,681 |
| Interest income | 188,101 | 305,296 | - | 493,397 |
| Interest expense | (925,378) | (2,049,082) | - | (2,974,460) |
| Other expense | (1,248,266) | - | - | (1,248,266) |
| Amortization of bond issue costs | (24,459) | (42,476) | - | (66,935) |
| Total non-operating revenues (expenses), net | <u>150,679</u> | <u>(1,786,262)</u> | - | <u>(1,635,583)</u> |
| Loss before capital contributions | <u>(8,923,953)</u> | <u>(1,841,064)</u> | - | <u>(10,765,017)</u> |
| Capital contributions | <u>11,993,263</u> | <u>532,337</u> | - | <u>12,525,600</u> |
| Change in net assets | <u>3,069,310</u> | <u>(1,308,727)</u> | - | <u>1,760,583</u> |
| Net assets at beginning of year | <u>130,110,029</u> | <u>24,180,034</u> | - | <u>154,290,063</u> |
| Net assets at end of year | <u>\$ 133,179,339</u> | <u>\$ 22,871,307</u> | <u>\$ -</u> | <u>\$ 156,050,646</u> |

See Accompanying Independent Auditors' Report.

COMMONWEALTH PORTS AUTHORITY

Combining Schedule of Cash Flows
Year Ended September 30, 2008

| | Airport Division | Seaport Division | Elimination | Total |
|---|---------------------|---------------------|-------------|---------------------|
| Cash flows from operating activities: | | | | |
| Cash received from customers | \$ 10,007,570 | \$ 4,770,411 | \$ - | \$ 14,777,981 |
| Cash payments to suppliers for goods and services | (3,387,532) | (1,435,364) | - | (4,822,896) |
| Cash payments to employees for services | (6,102,925) | (1,113,665) | - | (7,216,590) |
| Net cash provided by operating activities | <u>517,113</u> | <u>2,221,382</u> | <u>-</u> | <u>2,738,495</u> |
| Cash flows from capital and related financing activities: | | | | |
| Acquisition of capital assets | (16,134,225) | (5,907,297) | - | (22,041,522) |
| Capital contributions received | 13,113,926 | 1,111,502 | - | 14,225,428 |
| Passenger facility charge receipts | 2,160,681 | - | - | 2,160,681 |
| Principal paid on revenue bond maturities | (420,000) | (845,000) | - | (1,265,000) |
| Payments on note payable to related party | - | (223,105) | - | (223,105) |
| Interest paid on revenue bonds and note payable to related party | (1,065,685) | (2,396,911) | - | (3,462,596) |
| Net cash used for capital and related financing activities | <u>(2,345,303)</u> | <u>(8,260,811)</u> | <u>-</u> | <u>(10,606,114)</u> |
| Cash flows from investing activities: | | | | |
| Net change in restricted investments | (581,008) | 2,187,618 | - | 1,606,610 |
| Interest income | 188,101 | 305,296 | - | 493,397 |
| Net cash (used for) provided by investing activities | <u>(392,907)</u> | <u>2,492,914</u> | <u>-</u> | <u>2,100,007</u> |
| Net change in cash and cash equivalents | (2,221,097) | (3,546,515) | - | (5,767,612) |
| Cash and cash equivalents at beginning of year | <u>5,730,397</u> | <u>3,948,154</u> | <u>-</u> | <u>9,678,551</u> |
| Cash and cash equivalents at end of year | <u>\$ 3,509,300</u> | <u>\$ 401,639</u> | <u>\$ -</u> | <u>\$ 3,910,939</u> |
| Reconciliation of operating loss to net cash provided by operating activities: | | | | |
| Operating loss | \$ (9,074,632) | \$ (54,802) | \$ - | \$ (9,129,434) |
| Adjustments to reconcile operating loss to net cash provided by operating activities: | | | | |
| Depreciation and amortization | 7,271,917 | 2,418,305 | - | 9,690,222 |
| Bad debts | 198,974 | 252,255 | - | 451,229 |
| (Increase) decrease in assets: | | | | |
| Receivables - operations | 1,214,603 | (451,907) | - | 762,696 |
| Due from Seaport Division | (16,949) | 16,949 | - | - |
| Receivables - officers and employees | (5,858) | - | - | (5,858) |
| Prepaid expenses | 9,496 | 500 | - | 9,996 |
| Receivables - related parties | 185,456 | 53,181 | - | 238,637 |
| Increase (decrease) in liabilities: | | | | |
| Accounts payable - trade and other | 56,346 | (2,389) | - | 53,957 |
| Accounts payable - related parties | (307,507) | (31,768) | - | (339,275) |
| Accrued expenses | 1,163,718 | 52,455 | - | 1,216,173 |
| Compensated absences | (178,451) | (31,397) | - | (209,848) |
| Net cash provided by operating activities | <u>\$ 517,113</u> | <u>\$ 2,221,382</u> | <u>\$ -</u> | <u>\$ 2,738,495</u> |

See Accompanying Independent Auditors' Report.

COMMONWEALTH PORTS AUTHORITY

INDEPENDENT AUDITORS' REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2008

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

Board of Directors
Commonwealth Ports Authority:

We have audited the financial statements of the Commonwealth Ports Authority (CPA) as of and for the year ended September 30, 2008, and have issued our report thereon dated March 3, 2010. We conducted our audit 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered CPA's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of CPA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of CPA's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency described in the accompanying Schedule of Findings and Questioned Costs (pages 8 through 22) as item 2008-1 to be a significant deficiency in internal control over financial reporting.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiency described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether CPA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Schedule of Findings and Questioned Costs as item 2008-2.

We noted certain matters that we reported to management of CPA in a separate letter dated March 3, 2010.

CPA's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit CPA's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management and the Board of Directors of CPA, others within the entity, federal awarding agencies, and the cognizant audit and other federal agencies and is not intended to be and should not be used by anyone other than these specified parties.

Deville & Touche LLC

March 3, 2010

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 AND ON
THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Board of Directors
Commonwealth Ports Authority:

Compliance

We have audited the compliance of the Commonwealth Ports Authority (CPA) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2008. CPA's major federal program is identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (pages 8 through 22). Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of CPA's management. Our responsibility is to express an opinion on CPA's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about CPA's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on CPA's compliance with those requirements.

As described in items 2008-3 through 2008-6 in the accompanying Schedule of Findings and Questioned Costs, CPA did not comply with requirements regarding allowable costs/cost principles, procurement and suspension and debarment, cash management and equipment and real property management, that are applicable to its CFDA # 20.106 Airport Improvement Program. Compliance with such requirements is necessary, in our opinion, for CPA to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, CPA complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended September 30, 2008.

Internal Control Over Compliance

The management of CPA is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered CPA's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of CPA's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in CPA's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies, one of which that we consider to be a material weakness.

A *control deficiency* in an entity internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 2008-3 through 2008-6 to be significant deficiencies.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs, we consider item 2008-4 to be a material weakness.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of CPA as of and for the year ended September 30, 2008, and have issued our report thereon dated March 3, 2010. Our audit was performed for the purpose of forming our opinion on CPA's basic financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards (page 6) is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

CPA's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit CPA's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management and the Board of Directors of CPA, others within the entity, federal awarding agencies and the cognizant audit and other federal agencies and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLC

March 3, 2010

COMMONWEALTH PORTS AUTHORITY

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2008

| Program Title | Federal CFDA Number/ Grantor I.D. No. | Expenditures FY08 |
|---|---|----------------------|
| <u>U.S. Department of Transportation</u> | | |
| <u>Airport Improvement Program</u> | 20.106 | |
| Direct Grants: | | |
| Saipan International Airport - Saipan Rehabilitation Phase I, II, III & IV | 3-69-0002-31/32/50/53 | \$ 2,352,115 |
| Saipan International Airport - Noise Mitigation Measures | 3-69-0002-37 | - |
| Saipan International Airport - Security Enhancement Phase I | 3-69-0002-38/41/52/55 | 441,468 |
| Saipan International Airport - Rehabilitate Apron Taxilane | 3-69-0002-43/56 | 1,326,663 |
| Saipan International Airport - Airport Runway Safety | 3-69-0002-45/49 | 375,161 |
| Saipan International Airport - Terminal Building Passenger Loading Bridge | 3-69-0002-48/55 | 1,046,386 |
| Saipan International Airport - ARFF Vehicle/Typhoon Repairs | 3-69-0002-51 | 258,382 |
| Saipan International Airport - ARFF Building Expansion | 3-69-0002-54 | 74,502 |
| Saipan International Airport - Emergency Generator/Procurement/Install | 3-69-0002-57 | 9,241 |
| Saipan International Airport - Rehabilitate Runway 7/25 Phase V | 3-69-0002-58 | 1,646 |
| Saipan International Airport - Master Plan Study (Pagan) | 3-69-0004-01 | 263,638 |
| Rota International Airport - Extended Runway | 3-69-0003-19/20 | 445,032 |
| Tinian International Airport - Strengthen Parallel Taxiway - Phase I | 3-69-0011-15/17/19/20 | 3,677,056 |
| Tinian International Airport - ARFF Building Relocation Phase I | 3-69-0011-18 | 195,775 |
| Tinian International Airport - Strengthen Taxiway Phase IV | 3-69-0011-21 | 1,278 |
| | | <u>10,468,343</u> |
| <u>U.S. Department of Homeland Security</u> | | |
| Passed through the Government of the CNMI: | | |
| Saipan International Airport - Disaster Grants - Public Assistance (Presidentially Declared Disasters) | 97.036 | 277,614 |
| Homeland Security Grant Program | 97.067 | 300,000 |
| National Explosives Detection Canine Team Program (NEDCTP) | 97.072 | 150,500 |
| | | <u>728,114</u> |
| <u>Transportation Security Administration</u> | | |
| Saipan International Airport - Reimbursement Agreement | DTSA20-03-P-01657 | 195,231 |
| <u>U.S. Department of the Interior</u> | | |
| OMIP CNMI-CPA-2007-1 Specialized Equipment/Training | 15.875 | 289,755 |
| OMIP CNMI-CPA-2006-4 2nd Year ARFF Training | 15.875 | 55,787 |
| | | <u>345,542</u> |
| | | <u>\$ 11,737,230</u> |
| Reconciliation: | | |
| Expenditures per Statement of Revenues, Expenses and Changes in Net Assets | | \$ 12,525,600 |
| Contributions from the CNMI government | | <u>(788,370)</u> |
| | | <u>\$ 11,737,230</u> |

See accompanying notes to the schedule of expenditures of federal awards.

COMMONWEALTH PORTS AUTHORITY

Notes to the Schedule of Expenditures of Federal Awards Year Ended September 30, 2008

(1) Scope of Audit

The Commonwealth Ports Authority (CPA) was established as a public corporation by the Commonwealth of the Northern Mariana Islands (CNMI) by Public Law 2-48, effective November 8, 1981. All significant operations of CPA are included in the scope of the OMB Circular A-133 audit (the "Single Audit"). The U.S. Department of the Interior's Office of the Inspector General has been designated as CPA's cognizant agency for the Single Audit.

All of the programs presented in the Schedule of Expenditures of Federal Awards are subject to the Single Audit. U.S. Federal Covenant funds received as a loan from the Commonwealth Development Authority (CDA) are also subject to the Single Audit.

(2) Summary of Significant Accounting Policies

a. Basis of Accounting

For purposes of this report, certain accounting procedures were followed which help illustrate the authorizations and expenditures of the individual programs. The Schedule of Expenditures of Federal Awards is prepared on the accrual basis of accounting. All authorizations represent the total allotments or grant awards received. All expenses and capital outlays are reported as expenditures.

Any federal funds expended in excess of federal funds received are recorded as a receivable from the grantor agency and any federal funds received in excess of federal funds expended are recorded as a payable to the grantor agency.

b. Indirect Cost Allocation

CPA does not receive any indirect cost allocation and no indirect costs were recorded against any federal program for fiscal year 2008. The Federal Aviation Administration programs do allow, upon grantor approval, certain administrative expenses to be charged against the grants.

c. Matching Requirements

In allocating project expenditures between the federal share and the local share, a percentage is used based upon local matching requirements, unless funds are specifically identified to a certain phase of the project.

(3) Loan Funds from the Commonwealth Development Authority (CDA)

CPA receives loan funds from CDA that are part of a revolving fund established by CDA under the "Agreement of the Special Representatives on Future United States Financial Assistance for the Northern Mariana Islands" into which repayments of principal and interest from revenue-producing projects funded under Section 702(c) of the Covenant shall be deposited. As of September 30, 2008, CPA's outstanding balance due to this revolving fund was \$5,803,610. No additional amounts were received during the year ended September 30, 2008.

(4) Prepayments

At September 30, 2008, the schedule of expenditures of federal awards includes prepayments of \$101,962.

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs
Year Ended September 30, 2008

A. SUMMARY OF AUDITORS' RESULTS

Financial Statements

- | | | |
|----|--|---------------|
| 1. | Type of auditors' report issued: | Unqualified |
| | Internal control over financial reporting: | |
| 2. | Material weakness(es) identified? | Yes |
| 3. | Significant deficiency(ies) identified that is not considered to be a material weakness? | None reported |
| 4. | Noncompliance material to the financial statements noted? | Yes |

Federal Awards

Internal control over major programs:

- | | | |
|-----|--|-----------|
| 5. | Material weakness(es) identified? | Yes |
| 6. | Significant deficiency(ies) identified that is not considered to be a material weakness? | Yes |
| 7. | Type of auditors' report issued on compliance for major programs: | Qualified |
| 8. | Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? | Yes |
| 9. | CPA's major program was as follows: | |
| | CFDA | |
| | <u>Number</u> <u>Federal Program</u> | |
| | 20.106 Airport Improvement Program | |
| 10. | Dollar threshold used to distinguish between Type A and Type B Programs, as those terms are defined in OMB Circular A-133: | \$352,117 |
| 11. | CPA qualified as a low-risk auditee, as that term is defined in OMB Circular A-133? | No |

B. FINDINGS RELATING TO THE FINANCIAL STATEMENTS, WHICH ARE REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

| <u>Reference Number</u> | <u>Findings</u> | <u>Refer Page #</u> |
|-------------------------|-----------------------|---------------------|
| 2008-1 | Internal Controls | 10 - 13 |
| 2008-2 | Revenue Bonds Payable | 14 |

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs
Year Ended September 30, 2008

**C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS
AUDIT**

| <u>Reference Number</u> | <u>Findings</u> | <u>Questioned Costs</u> | <u>Refer Page #</u> |
|-----------------------------|--|-----------------------------|-------------------------|
| 2008-3 | Allowable Costs/Cost Principles | \$ 15,874 | 15 - 16 |
| 2008-4 | Procurement and Suspension and Debarment | \$ 412,652 | 17 |
| 2008-5 | Cash Management | \$ - | 18 - 19 |
| 2008-6 | Equipment and Real Property Management | \$ - | 20 |

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

**B. FINDINGS RELATING TO THE FINANCIAL STATEMENTS, WHICH ARE
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS**

Internal Controls

Finding No. 2008-1

Criteria: Proper internal controls are established to mitigate risks associated with the processing and recording of information in the general ledger.

Condition: During the year ended September 30, 2008, the following were noted:

Cash

During the year ended September 30, 2008, the payroll checking accounts (1020-00 and 1040-00 for the Airport and Seaport, respectively) were not reconciled on a regular basis.

Receivables from Grantor Agencies

The Airport and Seaport Divisions recorded receivables from grantor agencies of \$1,441,123 and \$81,278, respectively, as of September 30, 2008. Our preliminary examination of the account balances noted that the accounts were not reconciled, monitored or maintained during the fiscal year. A reconciliation was subsequently provided.

Prepaid Expenses

At September 30, 2008, CPA recorded prepaid expenses (account #1210-100) of \$243,668 for items and/or services that had already been received or provided. The account was subsequently reconciled and a proposed audit adjustment decreased the account balance to \$75,723.

Capital Assets

During the year ended September 30, 2008, the fixed asset subledger was not properly maintained and reconciled to the general ledger. Numerous asset items were not recorded in the subledger but were recorded in the general ledger and vice versa. In addition, depreciation expense and related accumulated depreciation did not agree to the general ledger. Although the fixed asset subledger was subsequently updated and reconciled to the general ledger, the reconciliation resulted in a proposed audit adjustment.

Construction in Progress

Construction in progress accounts (CIP) for the Airport and Seaport divisions were not maintained and reconciled during the year. As a result, numerous audit adjustments were proposed to reconcile the subledger to the general ledger. The reconciled CIP schedules were subsequently provided.

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

Finding No. 2008-1, Continued

Condition, Continued:

Contracts Payable

The Airport and Seaport Divisions recorded contracts payable of \$3,211,212 and \$338,461, respectively, as of September 30, 2008. Our preliminary examination of the account balances noted that the accounts were not reconciled, monitored or maintained during the fiscal year. A reconciliation was subsequently provided.

Accrued Vacation

- During the year ended September 30, 2008, accrued vacation payable for both the Airport and Seaport Divisions was not adjusted or reconciled. Upon auditor request, the accounts were subsequently reconciled and adjustments were proposed to reflect actual balances at September 30, 2008. The accrued annual leave schedule is manually maintained and requires an update each payperiod.
- Of five items tested, the vacation earned for one employee was understated by 26.5 hours amounting to \$273.

Purchases/Disbursements

- Of twenty-eight non-payroll disbursements tested, we noted the following:
 1. Invoices and related supporting documents for three items (AP-000154 - invoice # 7786-7 for Dec 07 for \$7,659; MC-000211 - utilities for Dec 07 for \$18,075; JE-000261 - utilities for Aug 07 Acct 22524-3 S-Building EC for \$5,247) were not made available.
 2. A journal voucher for one item (JE-000279 for \$41,233) was not made available.
 3. The reconciliation between the manual check register and the general ledger for two items (MC-000165 for \$27,609 and MC-000293 for \$122,781) was not made available
 4. A reconciliation of a general ledger amount in relation to the travel advance reconciliation provided for one item (JE-000131 for \$3,607) was not made available.

Payroll

Of twenty-eight payroll items tested, eleven items had an un-reconciled variance between the payroll register and G/L account. Details are as follows:

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

Finding No. 2008-1, Continued

Condition, Continued:

Payroll, Continued

| PP # | PPE | Location | Department | Per G/L (Date Posted) | G/L Account No. | Per Register | Per G/L (Amount) | Variance |
|------|----------|----------|----------------|--------------------------|--------------------|-----------------|---------------------|------------|
| 11 | 02/16/08 | Saipan | Operations | 02/26/08 | 6151-100 | \$ 19,483 | \$ 21,099 | \$ (1,616) |
| 01 | 09/29/07 | Saipan | Operations | 10/09/07 | 6151-100 | \$ 15,446 | \$ 19,224 | (3,778) |
| 18 | 05/24/08 | Saipan | Custodial | 06/03/08 | 6451-100 | \$ 12,314 | \$ 10,635 | 1,679 |
| 24 | 08/16/08 | Saipan | Custodial | 08/26/08 | 6451-100 | \$ 10,232 | \$ 8,721 | 1,511 |
| 08 | 01/05/08 | Saipan | Custodial | 01/14/08 | 6451-100 | \$ 10,385 | \$ 11,477 | (1,092) |
| 17 | 05/10/08 | Saipan | ARFF | 05/20/08 | 6751-100 | \$ 38,298 | \$ 39,935 | (1,637) |
| 26 | 09/13/08 | Saipan | ARFF | 09/23/08 | 6751-100 | \$ 35,613 | \$ 37,250 | (1,637) |
| 26 | 09/13/08 | Saipan | ARFF | 09/23/08 | 6751-100 | \$ 35,613 | \$ 37,250 | (1,637) |
| 16 | 04/26/08 | Saipan | Administration | 05/05/08 | 6851-101 | \$ 7,547 | \$ 7,020 | 527 |
| 23 | 08/02/08 | Saipan | Personnel | 08/12/08 | 6851-107 | \$ 6,927 | \$ 2,398 | 4,529 |
| 26 | 09/13/08 | Tinian | Flight Service | 09/23/08 | 7151-300 | \$ 2,020 | \$ 2,661 | (641) |
| | | | | | | | | \$ (3,792) |

Subsequent Disbursement FY 2009

During our examination of subsequent disbursements, the related invoices for fifteen items were not available.

Journal Entries

During our examination of journal entries for the Airport and Seaport Divisions, we noted that there were a significant number of journal entries posted during the year, some of which relate to reclassifications and reversals of posting errors. Further, we noted that voided journal entries are not properly accounted for.

Grant Expenditures

- During our examination of projects, one progress billing related to the Tinian International Airport project funded by the CNMI government totaling \$104,780 of which \$73,653 was not recorded in the general ledger. In addition, the accounts receivable and payable for the related project were not reconciled with the CNMI government. An audit adjustment was proposed to record payments made by the CNMI government.
- Variances were noted between expenses reported on the preliminary schedule of expenditures of federal awards (SEFA) and supporting detailed schedules. The SEFA was subsequently updated to reflect actual expenditures and adjustments.
- During our examination of subsequent cash receipts from a grantor, we noted a request for reimbursement of expenditures, amounting to \$150,500, for which no receivable was recorded at September 30, 2008. The receivable and related expenditures were subsequently recorded in the general ledger through a proposed audit adjustment.
- Truck parts and tires totaling \$27,049 (PO # 08-15803) were purchased and received on September 18, 2008. The related expenditure and liability were not recorded in the general ledger at September 30, 2008. Management did not consider this amount material to the financial statements.

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2008

Finding No. 2008-1, Continued

Recommendation: We recommend the following:

- All general ledger accounts are reconciled, reviewed and monitored on a monthly basis.
- Supporting journal vouchers, disbursement vouchers, invoices, and reconciliations be properly maintained.
- Examination of current system capabilities to alleviate and/or minimize manual journal entries and the use of spreadsheets.
- Adequate review of journal entries be performed.
- Consider providing training to staff with respect to their duties.
- Management establishes communications with the CNMI Government to ensure all interagency transactions are recorded and accounted for.

Prior Year Status: The above condition related to cash and prepaid expenses was reported as a finding in our previous management letter for fiscal year 2007 and the above condition related to construction in progress was reported as a finding in our previous management letters for fiscal years 2005 through 2007.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Frances C. Mafnas, Comptroller

Corrective Action: CPA concurs with the findings. CPA, for the period of 2007 and 2008, functioned without a Comptroller. Further, for most of the fiscal year under audit, CPA had no functioning Board of Directors. Additionally, CPA suffered a near complete turnover in staff during the two-year period. This allowed for the deficiencies to develop. Further, the 2008 audit was also complicated by the fact that during the same year, CPA also closed out the 2006 and 2007 annual audits. However, subsequent to year end, CPA devoted additional assets to correct these known problems. This included subsequent reconciliations resulting in adjustments up to the end of your fieldwork.

Subsequent to year end, CPA hired a Comptroller, and filled six other accounting positions. The Comptroller issued a series of directives to strengthen internal controls particularly in the areas of journal entries, payroll and purchasing. An in-house training program has been developed, arrangements have been made for software training and an accounting manual has been prepared and distributed in draft form. CPA believes that with these changes and priorities, significant deficiencies in internal controls will be greatly reduced.

Proposed Completion Date: Ongoing

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

Revenue Bonds Payable

Finding No. 2008-2

Criteria: Section 6.11 of the Airport and Seaport Bond Indenture Agreements state that CPA shall impose, levy, enforce and collect such fees, tariffs, lease rentals, licensing fees and other fees and charges in aggregate amount with respect to each fiscal year to produce gross revenues to comply with subsections (A)(1), (A)(2), (A)(3) and (A)(4) of Section 6.11.

Condition: The required gross revenues for Airport and Seaport to be in compliance with Section 6.11 amount to \$12,287,723 and \$6,727,176, respectively. Actual gross revenues for the Airport amounted to \$9,264,470, resulting in a variance of \$3,023,253. Actual gross revenues for the Seaport amounted to \$5,474,433, resulting in a variance of \$1,252,743.

Cause: The cause of the above condition is insufficient revenues generated during the year.

Effect: The effect of the above condition is noncompliance with Section 6.11 of the Airport and Seaport Bond Indenture Agreements. The Indenture specifies requirements of CPA if this condition occurs. If after such requirements are met and required gross revenues continue to be insufficient, the deficiency shall constitute an event of default as specified in Section 7.01 of the Airport and Seaport Bond Indenture Agreements.

Recommendation: We recommend that CPA review all revenue generating sources to ensure amounts collected will be sufficient to meet requirements of Section 6.11.

Prior Year Status: Noncompliance with Section 6.11 of the Airport and Seaport Bond Indenture Agreements was reported as a finding in the Single Audits of CPA for fiscal years 2006 and 2007.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Frances C. Mafnas, Comptroller

Corrective Action: CPA concurs with this finding. As noted in the finding, CPA failed to meet the bond indenture revenue requirements for fiscal years 2006, 2007 and 2008. For this three-year period, CPA had a total of five Executive Directors. Further, for most of the fiscal year, CPA did not fill such important positions as Airport Manager or Comptroller. Due to this lack of consistent direction, no workable policies were developed or initiated to meet the required goals. Subsequent to year end, the Executive Director recommended to the Board of Directors and the Board passed two major recommendations as follows:

1. The airport incentive program was discontinued. This program, which offered a 100% rebate of landing fees, failed to attract any new airlines, while, in fact, one major airline discontinued service entirely. In the first nine months of the current fiscal year, CPA has seen an increase in Airport cash deposits of \$1.8 million due to the discontinuation of the airport incentive program and better collection efforts.
2. Port handling fees had not been increased in several years. Effective March 2009, a 90% increase in port fees was approved. For the months of April, May and June 2009, CPA has seen an average increase in cash deposits for the Seaport of nearly \$150,000 per month.

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

Finding No. 2008-2, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

CPA believes that with these two major policy changes along with better collection efforts and minimizing costs, the required ratios will be met. However, CPA will request a review of its efforts by a third party expert to provide an outside opinion as required by the bond indenture agreement.

Proposed Completion Date: Ongoing

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

**C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS
AUDIT**

Allowable Costs/Cost Principles

Finding No. 2008-3

| Program | Reason for Questioned Costs | Questioned Costs | | | | | | | | | | | | | | | | | | |
|---|---|-------------------------|---------------------|---------------------|---|-----------------|-----------|------------------------------------|--------------|--------------|-----------------------|--------------|--------|---|-----------------|--------------|--|--|------------------|-----------|
| U.S. Department of Transportation / Airport Improvement Program / CFDA # 20.106 / Federal Award #s AIP Nos. 3-69-0002-49, 3-69-0002-50, 3-69-0002-53, 3-69-0002-56, 3-69-0011-19 and 3-69-0011-20 / Federal Award Periods Ended 06/24/08, 06/24/08, 08/16/09, 08/20/10, 08/10/10 and 08/08/11 | <p><u>Criteria:</u> Administrative costs charged to projects and recorded in the general ledger should be properly supported.</p> <p><u>Condition:</u> CPA recorded administrative costs related to ongoing/completed projects amounting to \$263,091. Of \$201,111 tested, the following items were noted:</p> <ul style="list-style-type: none"> Justification for 25% of gross salaries claimed were not properly supported for the following: <table border="1" style="margin-left: 40px;"> <thead> <tr> <th style="text-align: center;">Project</th> <th style="text-align: center;">AIP No.</th> <th style="text-align: center;">Amount</th> </tr> </thead> <tbody> <tr> <td>Saipan Rehabilitation - Phase I, II, III & IV</td> <td style="text-align: center;">3-69-0002-50/53</td> <td style="text-align: right;">\$ 3,548</td> </tr> <tr> <td>Rehabilitate Runway Apron/Taxilane</td> <td style="text-align: center;">3-69-0002-56</td> <td style="text-align: right;">2,195</td> </tr> <tr> <td>Airport Runway Safety</td> <td style="text-align: center;">3-69-0002-49</td> <td style="text-align: right;">2,074</td> </tr> <tr> <td>Airport Parallel T'way Strengthening - Phase I and II</td> <td style="text-align: center;">3-69-0011-19/20</td> <td style="text-align: right;"><u>3,428</u></td> </tr> <tr> <td></td> <td></td> <td style="text-align: right;">\$ <u>11,245</u></td> </tr> </tbody> </table> | Project | AIP No. | Amount | Saipan Rehabilitation - Phase I, II, III & IV | 3-69-0002-50/53 | \$ 3,548 | Rehabilitate Runway Apron/Taxilane | 3-69-0002-56 | 2,195 | Airport Runway Safety | 3-69-0002-49 | 2,074 | Airport Parallel T'way Strengthening - Phase I and II | 3-69-0011-19/20 | <u>3,428</u> | | | \$ <u>11,245</u> | \$ 11,245 |
| | Project | AIP No. | Amount | | | | | | | | | | | | | | | | | |
| | Saipan Rehabilitation - Phase I, II, III & IV | 3-69-0002-50/53 | \$ 3,548 | | | | | | | | | | | | | | | | | |
| | Rehabilitate Runway Apron/Taxilane | 3-69-0002-56 | 2,195 | | | | | | | | | | | | | | | | | |
| | Airport Runway Safety | 3-69-0002-49 | 2,074 | | | | | | | | | | | | | | | | | |
| | Airport Parallel T'way Strengthening - Phase I and II | 3-69-0011-19/20 | <u>3,428</u> | | | | | | | | | | | | | | | | | |
| | | | \$ <u>11,245</u> | | | | | | | | | | | | | | | | | |
| | <ul style="list-style-type: none"> Recalculation of Airport Operation Area (AOA) payroll charges claimed resulted in the following variances: <table border="1" style="margin-left: 40px;"> <thead> <tr> <th style="text-align: center;">AIP No.</th> <th style="text-align: center;">Claimed</th> <th style="text-align: center;">Actual</th> <th style="text-align: center;">Variance</th> </tr> </thead> <tbody> <tr> <td style="text-align: center;">3-69-0002-49</td> <td style="text-align: right;">\$ 79,928</td> <td style="text-align: right;">\$ 76,938</td> <td style="text-align: right;">\$ 2,990</td> </tr> <tr> <td style="text-align: center;">3-69-0002-56</td> <td style="text-align: right;">\$ 22,991</td> <td style="text-align: right;">\$ 22,522</td> <td style="text-align: right;">\$ 469</td> </tr> </tbody> </table> | AIP No. | Claimed | Actual | Variance | 3-69-0002-49 | \$ 79,928 | \$ 76,938 | \$ 2,990 | 3-69-0002-56 | \$ 22,991 | \$ 22,522 | \$ 469 | 3,459 | | | | | | |
| | AIP No. | Claimed | Actual | Variance | | | | | | | | | | | | | | | | |
| | 3-69-0002-49 | \$ 79,928 | \$ 76,938 | \$ 2,990 | | | | | | | | | | | | | | | | |
| 3-69-0002-56 | \$ 22,991 | \$ 22,522 | \$ 469 | | | | | | | | | | | | | | | | | |
| <ul style="list-style-type: none"> Variances between the amount of hours claimed and the amount of hours certified were as follows: <table border="1" style="margin-left: 40px;"> <thead> <tr> <th style="text-align: center;">AIP No.</th> <th style="text-align: center;">Timesheet Certification</th> <th style="text-align: center;">Amount Claimed</th> <th style="text-align: center;">Variance (in hours)</th> <th style="text-align: center;">Variance (amount)</th> </tr> </thead> <tbody> <tr> <td style="text-align: center;">3-69-0002-49</td> <td style="text-align: center;">64</td> <td style="text-align: center;">66</td> <td style="text-align: center;">2</td> <td style="text-align: right;">\$ 43</td> </tr> <tr> <td style="text-align: center;">3-69-0011-19/20</td> <td style="text-align: center;">473</td> <td style="text-align: center;">517</td> <td style="text-align: center;">44</td> <td style="text-align: right;">\$ 1,127</td> </tr> </tbody> </table> | AIP No. | Timesheet Certification | Amount Claimed | Variance (in hours) | Variance (amount) | 3-69-0002-49 | 64 | 66 | 2 | \$ 43 | 3-69-0011-19/20 | 473 | 517 | 44 | \$ 1,127 | <u>1,170</u> | | | | |
| AIP No. | Timesheet Certification | Amount Claimed | Variance (in hours) | Variance (amount) | | | | | | | | | | | | | | | | |
| 3-69-0002-49 | 64 | 66 | 2 | \$ 43 | | | | | | | | | | | | | | | | |
| 3-69-0011-19/20 | 473 | 517 | 44 | \$ 1,127 | | | | | | | | | | | | | | | | |
| <p><u>Cause:</u> The cause of the above condition is estimates are being used to determine costs charged to federally funded projects and the lack of grantor approval of such estimates. In addition, timely reconciliation of the related accounts is not being performed.</p> <p><u>Effect:</u> The effect of the above condition is the possible misstatement of expenditures reported and claimed to the grantor and questioned costs of \$15,874.</p> | <u>15,874</u> | | | | | | | | | | | | | | | | | | | |
| <p><u>Recommendation:</u> We recommend that grantor approval be obtained for estimated percentages and hours utilized in CPA's administrative expense calculations. We also recommend reconciliation of accounts be performed in a timely manner.</p> <p><u>Prior Year Status:</u> The lack of grantor approval of cost estimates charged to projects and lack of timely reconciliation was reported as a finding in the Single Audits of CPA for fiscal years 2005 through 2007.</p> | | | | | | | | | | | | | | | | | | | | |

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

Finding No. 2008-3 Continued

| <u>Program</u> | <u>Reason for Questioned Costs</u> | <u>Questioned Costs</u> |
|----------------|---|-------------------------|
| | <p><u>Auditee Response and Corrective Action Plan:</u></p> <p>Name of Contact Person: Frances C. Mafnas, Comptroller</p> <p>Corrective Action: CPA concurs with this finding, but not its entire effect. Of the total questioned cost of \$15,874, the amount of \$11,245 related to an inability to locate the appropriate timesheets. CPA's Accounting Department, in the immediate year of the audit, moved its physical office two times. This has led to a great deal of misplaced paperwork. CPA believes that, if given enough time, appropriate documentation can be found. However, the need to complete the audit supersedes CPA's ability to locate the paperwork.</p> <p>CPA is in the process of filing with the Federal Aviation Administration (FAA) a federal overhead rate analysis. If accepted by the FAA, this will provide a clear, transparent and accountable methodology for administrative costs associated with federal grants.</p> <p>Proposed Completion Date: Ongoing</p> | |

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

Procurement and Suspension and Debarment

Finding No. 2008-4

| Program | Reason for Questioned Costs | Questioned Costs |
|---|---|-------------------|
| U.S. Department of Transportation / Airport Improvement Program / CFDA # 20.106 / Federal Award #s AIP Nos. 3-69-0002-51 and 3-69-0002-55 / Federal Award Periods Ended 08/15/08 and 08/20/10 | <p><u>Criteria:</u> CPA's Procurement Rules & Regulations state the following:</p> <ul style="list-style-type: none"> • Emergency Procurement: In accordance with Section 3.5 of CPA's Procurement Rules & Regulations, in case of any major public calamity, or whenever it is in the interest of aviation or shipping safety, or necessary to keep the ports operable by the Authority, the Board may determine that the public interest and necessity demand the immediate expenditure of funds to keep the ports facilities open to traffic or in a safe condition, and thereupon authorize the expenditure of such sums as may be needed without the observation of provision requiring contracts, bids or notices. • Sole Source Procurement: A contract may be awarded for supply, service or construction item without competition when the contracting officer determines in writing that there is only one source for the required supply, service or construction item. The written determination shall state the unique capabilities required and why they are required and the consideration given to alternative sources. | |
| | <p><u>Condition:</u> Of \$10,468,343 expenditures, \$10,327,645 were tested and the following items were noted:</p> | |
| | <ul style="list-style-type: none"> • Jetway repairs totaling \$122,781 were procured through emergency procurement. The justification for the emergency procurement relates to the deadline to draw down funds. | 122,781 |
| | <ul style="list-style-type: none"> • The justification for emergency procurement related to the purchase of surveillance cameras and security upgrade totaling \$578,950 was approved by the Acting Executive Director on August 1, 2007. The actual contract and notice to proceed was executed on March 14, 2008. Further, we did not note the approval of the emergency procurement justification from the Board of Directors. Of the total contract amount, \$265,003 was funded by AIP. | 265,003 |
| | <ul style="list-style-type: none"> • Sole source procurement was utilized to purchase proximity suits amounting to \$37,485. There was no indication that consideration was given to alternative sources. Further, we did not note the approval from the Board of Directors. Total funds drawn down and received amounted to \$24,868 on August 18, 2008. The invoice date of the items was November 14, 2008. Further, we noted that when the actual invoice was paid in fiscal year 2009, the entire amount was paid (check # 1770) from the FAA checking account (#1010-100). | <u>24,868</u> |
| | <p><u>Cause:</u> The cause of the above condition is noncompliance with CPA's procurement rules & regulations.</p> | |
| | <p><u>Effect:</u> The effect of the above condition is questioned cost of \$412,652.</p> | <u>412,652</u> |
| | <p><u>Recommendation:</u> All purchases should comply with CPA's procurement rules and regulations.</p> | |
| Total Questioned Costs | | \$ <u>428,526</u> |

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

Finding No. 2008-4, Continued

| Program | Reason for Questioned Costs | Questioned Costs |
|---------|---|------------------|
| | <p><u>Auditee Response and Corrective Action Plan:</u></p> <p>Name of Contact Person: Frances C. Mafnas, Comptroller</p> <p>Corrective Action: CPA contests a portion of this finding and the majority of its effect. CPA's subsequent review confirms that the procurement documentation was weak in its definition of both emergency and sole source procurement.</p> <p>In the first case (jetway repairs of \$122,781), CPA argues that the vendor photos of the damaged area were severe enough to warrant an emergency, but that was not clearly reflected in the emergency declaration. The fact that the declaration mentions a deadline to draw down the funds, the only source of possible funding for the emergency, should not be construed or misinterpreted that it was solely the deadline that motivated the repairs. Further, on May 12, 2008, the Governor declared a State of Emergency for CPA. This can be argued in support of the emergency procurement.</p> <p>In the second case (surveillance cameras of \$265,003), CPA agrees that the emergency procurement was improper, but it is quite possible that it could have been justifiable as a sole source contract. Regardless, it is unacceptable given the description and detail of the work performed, that the grantor suffered a 100% overcharge of their 50% contribution.</p> <p>In the third case (purchase of proximity suits of \$37,485), CPA agrees that the written documentation was inadequate. However, CPA also maintains that the vendor selected is the only vendor who carries the certified hazard suits. Additionally, the Board of Directors issue is moot, as the Board had been dissolved by the Governor in an emergency declaration. Again, the declared State of Emergency for CPA can be argued in support of the emergency procurement.</p> <p>Proposed Completion Date: Ongoing</p> | |

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

U.S. Department of Transportation

Cash Management - Airport Improvement Program

CFDA #20.106, Federal Award #s AIP Nos. 3-69-0002-48, 3-69-0002-49, 3-69-0002-50/53, 3-69-0002-51, 3-69-0002-54, 3-69-0002-55, 3-69-0002-56, 3-69-0004-01, 3-69-0011-17/19/20/21 and 3-69-0011-18

Federal Award Periods Ended 06/24/08, 06/24/08, 6/24/08, 08/16/09, 08/15/08, 08/16/09, 08/20/10, 08/20/10, 08/16/09, 08/22/08, 08/10/10, 08/08/11, 06/12/10 and 08/23/09

Finding No. 2008-5

Criteria: In accordance with 49 CFR, Section 18.21(b) and (c), methods and procedures for payment shall minimize the time elapsing between the transfer of funds and disbursement by the grantee or subgrantee, in accordance with Treasury regulations at 31 CFR part 205.

Condition: For forty-nine of one hundred one samples tested, disbursement checks cleared (subsequent to three business days) between one and twenty-eight days after cash receipt:

| <u>Amount</u> | <u>Check Number</u> | <u>Check Clearance Date</u> | <u>Cash Receipt Date</u> | <u>Days Elapsed After Cash Receipt</u> |
|---------------|---------------------|-----------------------------|--------------------------|--|
| \$ 865,355 | 1690 | 03/03/08 | 02/25/08 | 2 |
| \$ 6,434 | 1698 | 03/27/08 | 03/17/08 | 5 |
| \$ 3,923 | 1716 | 06/04/08 | 05/20/08 | 8 |
| \$ 4,707 | 1740 | 08/07/08 | 07/30/08 | 3 |
| \$ 7,114 | 1755 | 10/01/08 | 09/24/08 | 2 |
| \$ 11,104 | 1669 | 01/04/08 | 12/27/07 | 3 |
| \$ 14,468 | 1688 | 03/07/08 | 02/25/08 | 4 |
| \$ 63,944 | 1715 | 06/02/08 | 05/20/08 | 6 |
| \$ 24,178 | 1725 | 07/10/08 | 07/02/08 | 3 |
| \$ 16,831 | 1738 | 08/08/08 | 07/30/08 | 3 |
| \$ 87,068 | 1670 | 01/07/08 | 12/27/07 | 4 |
| \$ 214,167 | 1677 | 02/11/08 | 01/30/08 | 5 |
| \$ 136,251 | 1687 | 03/03/08 | 02/25/08 | 2 |
| \$ 261,561 | 1726 | 07/10/08 | 07/02/08 | 3 |
| \$ 30,938 | 1727 | 07/11/08 | 07/02/08 | 4 |
| \$ 6,499 | 1695 | 03/24/08 | 03/17/08 | 2 |
| \$ 386,636 | 1756 | 10/02/08 | 09/23/08 | 4 |
| \$ 11,068 | 1757 | 10/03/08 | 09/24/08 | 4 |
| \$ 87,635 | 1672 | 01/07/08 | 12/27/07 | 4 |
| \$ 37,698 | 1678 | 02/11/08 | 01/30/08 | 5 |
| \$ 271,067 | 1686 | 03/04/08 | 02/25/08 | 3 |
| \$ 13,619 | 1717 | 06/02/08 | 05/20/08 | 10 |
| \$ 251,036 | 1739 | 08/07/08 | 07/30/08 | 5 |
| \$ 23,836 | 1668 | 01/04/08 | 12/27/07 | 5 |
| \$ 58,247 | 1733 | 07/23/08 | 06/17/08 | 25 |
| \$ 12,213 | 1679 | 02/12/08 | 01/30/08 | 8 |
| \$ 3,053 | 1731 | 07/15/08 | 07/03/08 | 5 |
| \$ 28,615 | 1671 | 01/07/08 | 12/27/07 | 4 |
| \$ 40,089 | 1693 | 03/24/08 | 03/17/08 | 2 |
| \$ 32,293 | 1673 | 01/07/08 | 12/27/07 | 4 |
| \$ 43,800 | 1680 | 02/11/08 | 01/30/08 | 5 |
| \$ 119,432 | 1685 | 03/07/08 | 02/25/08 | 6 |
| \$ 19,564 | 1694 | 03/24/08 | 03/17/08 | 1 |
| \$ 11,096 | 1752 | 10/02/08 | 09/24/08 | 3 |
| \$ 55,178 | 1689 | 03/07/08 | 02/25/08 | 6 |
| \$ 49,059 | 1699 | 04/16/08 | 04/08/08 | 3 |
| \$ 134,753 | 1701 | 04/14/08 | 04/08/08 | 1 |
| \$ 59,431 | 1730 | 07/10/08 | 07/02/08 | 3 |

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

Finding No. 2008-5, Continued

Condition, Continued:

| <u>Amount</u> | <u>Check Number</u> | <u>Check Clearance Date</u> | <u>Cash Receipt Date</u> | <u>Days Elapsed After Cash Receipt</u> |
|---------------|---------------------|-----------------------------|--------------------------|--|
| \$ 36,163 | 1753 | 10/02/08 | 09/24/08 | 3 |
| \$ 141,314 | 1682 | 02/11/08 | 01/30/08 | 5 |
| \$ 115,279 | 1667 | 12/14/07 | 12/04/07 | 5 |
| \$ 59,819 | 1683 | 02/11/08 | 01/30/08 | 5 |
| \$ 4,655 | 1691 | 03/07/08 | 02/25/08 | 6 |
| \$ 95 | 1745 | 09/05/08 | 08/21/08 | 8 |
| \$ 45,447 | 1736 | 08/06/08 | 07/30/08 | 2 |
| \$ 45,447 | 1737 | 08/06/08 | 07/30/08 | 2 |
| \$ 122,781 | 1728 | 07/16/08 | 07/03/08 | 6 |
| \$ 24,868 | 1770 | 11/24/08 | 08/18/08 | 28 |
| \$ 20,736 | - | 09/30/08 | 08/18/08 | 28 |

The cash receipt of \$20,736 received from the grantor on August 18, 2008 has not been disbursed to the vendor, therefore, interest is calculated through September 30, 2008.

Cause: The cause of the above condition is the lack of procedures in place to ensure cash advanced from the grantor agency is disbursed within a timely manner.

Effect: The effect of the above condition is noncompliance with federal cash management requirements. An interest liability of \$868 exists. However, no questioned costs result from the condition as the projected interest liability is less than \$10,000.

Recommendation: We recommend that management ensure strict compliance with federal cash management requirements.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Frances C. Mafnas, Comptroller

Corrective Action: CPA concurs with the findings and the recommendations.

Proposed Completion Date: Ongoing

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2008

U.S. Department of Transportation
Equipment and Real Property Management - Airport Improvement Program
CFDA #20.106, Federal Award #s All AIP Grants
Federal Award Period Available Until Expended

Finding No. 2008-6

Criteria: In accordance with 49 CFR, Section 18.31(4)(d)(1)(2)(3)(4) Procedures for managing equipment (including replacement equipment), whether acquired in whole or in part with grant funds, until disposition takes place will, as a minimum, meet the following requirements:

- (1) Property records must be maintained that include a description of the property, a serial number or other identification number, the source of property, who holds title, the acquisition date, and cost of the property, percentage of Federal participation in the cost of the property, the location, use and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property.
- (2) A physical inventory of the property must be taken and the results reconciled with the property records at least once every two years.
- (3) A control system must be developed to ensure adequate safeguards to prevent loss, damage, or theft of the property. Any loss, damage, or theft shall be investigated.
- (4) Adequate maintenance procedures must be developed to keep the property in good condition.
- (5) If the grantee or subgrantee is authorized or required to sell the property, proper sales procedures must be established to ensure the highest possible return.

Condition: CPA has not conducted a physical inventory of its fixed assets in the last two years. In addition, a log indicating the location (Department) of equipment is not being maintained. Total fixed asset additions related to CPA's major program amounted to \$9,826,975, \$22,986,600 and \$12,786,137 during fiscal years 2008, 2007 and 2006, respectively. Of the total additions, \$9,778,502, \$22,022,560 and \$12,350,084 represent additions to construction in progress during the fiscal years ended September 30, 2008, 2007 and 2006, respectively.

Cause: The cause of the above condition is a lack of personnel.

Effect: The effect of the above condition is noncompliance with 49 CFR, Section 18.31(4)(d)(1)(2)(3)(4).

Recommendation: We recommend management ensure a physical inventory is conducted at least once every two years. We also recommend that documentation procedures be established to ensure recordkeeping of the assets are maintained.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Frances C. Mafnas, Comptroller

Corrective Action: CPA concurs with the findings and the recommendations.

Proposed Completion Date: Ongoing

COMMONWEALTH PORTS AUTHORITY

Unresolved Prior Year Comments
Year Ended September 30, 2008

Questioned Costs

The prior year Single Audit report on compliance with laws and regulations noted the following questioned costs and comments that were unresolved at September 30, 2008:

| | |
|---|-------------------|
| Questioned costs as previously reported | \$ 621,238 |
| Resolved with a grantor agency (Note 1) | (541,306) |
| Questioned costs of fiscal year 2008 Single Audit | <u>428,526</u> |
| Unresolved questioned costs at September 30, 2008 | \$ <u>508,458</u> |

Unresolved Findings

The status of unresolved prior year findings is discussed within the Schedule of Findings and Questioned Costs section of this report (pages 8 through 22).

Note1: Subsequent to year end, CPA paid \$541,306 to a grantor agency related to questioned costs reported in the audits of CPA for fiscal years 2005 through 2007.



COMMONWEALTH PORTS AUTHORITY

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SUMMARY OF SCHEDULE OF PRIOR AUDIT FINDINGS

Status of audit findings included in the schedule of findings and questioned costs for the year ended September 30, 2007:

FINDINGS RELATING TO THE FINANCIAL STATEMENTS, WHICH ARE REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

Finding No. 2007-1 - Not corrected. See corrective action plan to Finding No. 2008-2.

FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS AUDIT

Finding No. 2007-2 - Not corrected. See corrective action plan to Finding No. 2008-3.

Finding No. 2007-3 - Corrective action was taken.

Finding No. 2007-4 - Corrective action was taken.

Finding No. 2007-5 - Corrective action was taken.

Finding No. 2007-6 - Corrective action was taken.

Finding No. 2007-7 - Corrective action was taken.