

COMMONWEALTH DEVELOPMENT AUTHORITY

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

YEAR ENDED SEPTEMBER 30, 2006

COMMONWEALTH DEVELOPMENT AUTHORITY

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2006 AND 2005

INDEPENDENT AUDITORS' REPORT

Board of Directors
Commonwealth Development Authority:

We have audited the accompanying combined statements of net assets of the Commonwealth Development Authority (CDA), a component unit of the Commonwealth of the Northern Mariana Islands (CNMI), as of September 30, 2006 and 2005, and the related combined statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of CDA'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 respective 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 the CDA's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective 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 Development Authority as of September 30, 2006 and 2005, and their changes in net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3 through 12 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board (GASB). This supplementary information is the responsibility of the Commonwealth Development Authority's management. We did not audit and do not express an opinion on such information. However, we have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. As a result of these limited procedures, we believe that the Management's Discussion and Analysis is not in conformity with guidelines established by GASB because it refers to components of CDA and not the basic financial statements and there is insufficient analysis of the basic financial statements.

Our audits were conducted for the purpose of forming an opinion on the Commonwealth Development Authority's basic financial statements. The Combining Statement of Net Assets, the Combining Statement of Revenues, Expenses and Changes in Net Assets and the Combining Statement of Cash Flows as of and for the year ended September 30, 2006 (pages 41 through 43) 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 Development Authority's management. The Combining Statement of Net Assets, the Combining Statement of Revenues, Expenses and Changes in Net Assets and the Combining Statement of Cash Flows as of and for the year ended September 30, 2006 have been subjected to the auditing procedures applied by us in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 12, 2008, on our consideration of internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte & Touche LLC

December 12, 2008



COMMONWEALTH DEVELOPMENT AUTHORITY

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Management's Discussion and Analysis Year Ended September 30, 2006

The Management's Discussion and Analysis of the Commonwealth Development Authority's (CDA) financial performance provides an overview of CDA's financial activity for the fiscal year ended September 30, 2006.

CDA, formerly known as the Economic Development Loan Fund, was established as an autonomous public agency in 1985 through Public Law 4-49. Its overall purpose is to stimulate economic development in the Commonwealth of the Northern Mariana Islands (CNMI). Its mission statement is to provide appropriate financial and technical assistance to facilitate the start-up or expansion of private and public enterprises for their success, the benefit of the CNMI's economic welfare and the long-term sustainability of CDA. CDA's functions are carried out through the Development Banking Division (DBD) and the Development Corporation Division (DCD). Additionally, in 1994, the Northern Marianas Housing Corporation (NMHC) was consolidated into CDA. CDA, as the financing arm of the CNMI, successfully continues its role to stimulate the CNMI's economy by financing major capital improvements and investing in its people. CDA has a Board of Directors composed of seven individuals that are appointed staggered four-year terms by the Governor of the CNMI.

The Banking Division (DBD) generally engages in government and public sector activities while the Corporation Division (DCD) engages in private sector activities. Additionally, on December 1, 2000, CDA was given administrative authority for the Qualifying Certificate Program (QC). The QC is a tax incentive program to encourage new investment within the CNMI. The Housing Division (NMHC) provides low-cost housing and rentals and housing loans to qualifying residents of the CNMI. In addition, NMHC has many loan programs to all income level qualified applicants. CDA maintains three offices: its main office is in Saipan and branch offices are in Tinian and Rota.

DCD's mission is to initiate, stimulate and facilitate development of the economy of the CNMI for the economic and social advancement of the people of the CNMI by making loans, loan guarantees and providing financial, technical and advisory assistance in its discretion to the private sector in the CNMI.

DCD's primary activity relates to the servicing of its direct loan portfolio. As of year-end, CDA's loans receivable, net portfolio was \$11,226,108, a decrease of \$2,539,527 or 18% compared to the previous year. The cause of the decrease was due to the continuous effort of the Loan Department to provide loan servicing to all clients and to refer accounts that were 120 days in arrears to the legal counsel for litigation process. Auction processes were also in effect decreasing the loan delinquency. The vast majority of the outstanding balances relate to loans that were initiated during the late 1980's and the early 1990's.

Unfortunately, with the Asian economic crisis in the early 1990's, many of the projects financed by these loans greatly diminished in value both as commercial enterprises and in carrying assets that DCD placed on them. This was further exacerbated by the events of the 911, SARS, the war in Iraq and the increase in fuel prices and utility rates as well.

Additionally, the CNMI was swept by two major typhoons. Typhoon Tingting struck the CNMI on June 27, 2004 and about a month later, Typhoon Chaba devastated the CNMI again on August 21, 2004. With these two major typhoons, the clients in the Marine and Agriculture Divisions were greatly impacted in their operations and productivity resulting in nonrevenue generating activities. As a result, their financial obligation with CDA was a problem.

As stated earlier, the net value of the loans receivable portfolio, after provision for doubtful accounts was \$11,226,108. The total provision for doubtful accounts was \$4,746,223. This figure represents CDA's estimated potential of the loss of value of the loans and accrued interest for the current year. This was a drastic increase from prior year due to the 5% allowance on bad debts on current status accounts as approved by the Board of Directors in accordance with the FY2005 audit implementation. The ultimate collection of the earned interest and the principal value of loans is DCD's biggest financial concern. The inability of borrowers to repay their commitments has not allowed funds to be accumulated and re-loaned to new borrowers. CDA has recognized this concern and continued the moratorium up to June 1, 2005. CDA prompted to the lifting of the moratorium after a thorough analysis was made of its asset accounts and cash flow resulting in a positive financial re-lending position.

The Board of Directors continuously emphasize to management that the collection of delinquent loans is its top priority.

As its number one priority, CDA proceeded with numerous court judgments on seriously delinquent clients. CDA has foreclosed on several properties. Furthermore, CDA had properties on auction, which resulted in an increase in collection for the year.

Delinquency will continue to plague CDA's financial condition but if we work closely with our clients, we will decrease the delinquency ratio then monitor a consistent collection activity and structure to meet the clients' cash flow capability. But we must maintain constant communication with them.

Even if many of our clients continue to be seriously in arrears, we will continue with full force what we have been doing for the past years. The current assets for DCD for this fiscal year increased by \$484,951 or 10%. This is a strong indication that CDA is moving in a positive direction to decrease its loan delinquency and increase its assets.

Financial Highlights

- In spite of efforts by the Loan Department to increase collection and service our clients, DCD has net operating revenue of \$ (1,230,347) while DBD has \$351,666. This was caused by the adjustment on the NMHC loan of the due to/due from accounts. Fortunately, the interest earned on loans for DCD for the year slightly increased by \$227,766 or 8%. On the other hand, DBD had a slight decrease of \$23,230 or 11% compared to the previous year.
- Operating expenses for DCD, omitting the provision of doubtful accounts and foreclosed real estate, decreased by \$233,002 or 16%. This decrease was related primarily to the decrease in activities of the provision for foreclosed real estate.
- DCD's provision for doubtful accounts and foreclosed real estate increased dramatically by \$3,635,792 or 180%. The increase reflected the amount of the write-off of loans and the adjustment on the due to/due from on the NMHC loan. Additionally, the transfer of \$4,000,000 as per Public Law 15-1 for the Commonwealth Utilities Corporation Emergency Declaration attributed to the increase.

- The Combined Statement of Net Assets decreased by \$14,775,786 or 19% compared to last year. This was due to decreases on all categories except for noncurrent liabilities which increased by \$729,317 or 5%.
- On January 25, 2006, the CDA Board of Directors approved for recommendation Qualifying Certificate Resolution #2006-01 for Bridge Capital, LLC. The resolution was approved and signed by Governor Benigno Fitial on February 17, 2006.

Capital Assets and Debt Administration

Capital Assets

At September 30, 2006 and 2005, CDA had \$15,689,514 and \$17,696,691, respectively, invested in capital assets, net of depreciation where applicable. This represents a net decrease of \$2,007,177 or 11% during fiscal year 2006.

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Property and equipment, net	\$ 2,814,400	\$ 5,161,806	\$ 5,468,296
Asset held for sale	443,000	443,000	834,000
Land	10,409,682	10,409,682	10,409,682
Foreclosed real estate	<u>2,022,432</u>	<u>1,682,203</u>	<u>795,238</u>
	<u>\$ 15,689,514</u>	<u>\$ 17,696,691</u>	<u>\$ 17,507,216</u>

See notes 7, 8 and 9 to the financial statements for more detail information on CDA's capital assets and changes therein.

Long-Term Debt

At September 30, 2006 and 2005, CDA had \$10,709,566 and \$11,808,043, respectively, in long-term debt outstanding. See note 10 to the financial statements for more detail information on CDA's long-term debt and changes therein.



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Management's Discussion and Analysis Year Ended September 30, 2006

Division Analysis of the Northern Marianas Housing Corporation (NMHC)

NMHC is a multifaceted organization that offers direct housing loans, housing loan guarantees, rental properties, housing and community development and where necessary, infrastructure development.

NMHC has finalized the closing of Tottotville and 45 houses are all fully occupied and sold to respective homeowners. With closure of the Expansion Project, NMHC is in process of transferring infrastructure values to CUC and DPW. During FY 2005, homeowners have filed complaints with respect to the poor workmanship in the construction of their homes and NMHC is still attempting resolution with the homeowners. The designer/construction management and contractor for the subdivision have been contacted and all parties are addressing the areas of complaints. Mediation was also pursued; however, major issues being disputed are still unresolved by parties involved. Court hearings are ongoing with the latest held on Wednesday, March 7, 2007. Although NMHC has set aside a \$225,000 settlement with the homeowners, only nine (9) have accepted the offer. An additional \$1,200 is available for each of the 36 remaining homeowners.

Another major concern is the newly-enacted Public Law 15-48 (H.B. No. 15-197) which Governor Benigno R. Fitial signed into law on Tuesday, March 13, 2007. This law repealed in their entirety, 2 CMC §§ 4486 and 4498, and amended 2 CMC §4497 to eliminate the moratorium extended to NMHC on the loan made to NMHC by the Marianas Public Land Trust (MPLT). PL 15-48 has serious financial burdens as NMHC is forced to commence payment to MPLT.

The U.S. Department of Housing and Urban Development (HUD), through NMHC assisted the victims of Typhoon Pongsona with an award of 50 Housing Choice Vouchers for the Island of Rota, exclusively, and an annual budget of \$520,000. As of September 30, 2006, all 50 Vouchers have been utilized. The occupancy rate is at 100% with a turnover average of 4 tenant households per quarter. Housing assistance to prospective tenants on the waiting list is on a first-come first-served basis.

NMHC's revenues decreased 77% from prior year due to the provision for doubtful account allowance. Expenses increased by 3% due to an increase in housing assistance payments to landlords and additional drawdowns and disbursements of grants under the Community Development Block Grant (CDBG) and HOME Programs. In March 2004, 63 additional vouchers were awarded by HUD to assist families who were left homeless by Typhoon Tingting. All vouchers were utilized in Saipan at a 100% occupancy rate. Subsequently, HUD also awarded an additional 85 vouchers for families affected by Typhoon Chaba - 74 for Saipan and 11 for Tinian. All 85 are at a 100% occupancy rate.

Short-Term Goals: NMHC - 2006

The Mortgage and Credit Division continues to work diligently to sell the 2 remaining Sugar King II units and updated appraisal reports have been obtained. Interested parties have come forward to purchase the homes and final disposition of these units are anticipated within the next few months.

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"NMHC is an equal employment and fair housing public agency"

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NMHC has prepared a "standard" Loan Guaranty Agreement for use with participating lenders. NMHC did not renew the BankPacific Agreement as the requirements became too stringent. Bank of Hawaii has also changed their requirements and as such, loans that have already been done, cannot be transferred. The revolving effect will not avail NMHC with more funds for these programs. However, First Hawaiian Bank and the Bank of Saipan have formally submitted their interest to purchase NMHC's performing loans.

NMHC now services a total of 409 loans and has implemented the HOME New Construction Loan Program. Rehab projects are also continuing. NMHC has started update of applications, commitments and loan closing for the islands of Rota and Tinian. This engendered 30 new loans at approximately \$800,000 for new construction and rehab projects.

With \$250,000 set aside, the Board of Directors has implemented a pilot loan program to assist 6 very-low income families achieve homeownership.

The Partnership Program with Rural Development (RD) is underway and NMHC has received nine (9) loan commitments. This is a leveraging program between NMHC and RD so that more loans can be made with budgeted funds.

HUD's approval of additional vouchers under the Housing Choice Voucher Program has significantly increased the activities of the Program and Housing Division. Overall occupancy rate for the program is 95.7%. The additional vouchers for Typhoons Tingting and Chaba are 63 and 85 vouchers, respectively, bringing a grand total of 363 voucher units that NMHC now administers and monitors for compliance. At present, the occupancy rate is 99%. We submitted Typhoon Pongsona's request for reimbursement to FEMA which would entitle NMHC to 90% of the total reimbursement and it is anticipated anytime soon.

The New Construction, Project-Based Program, consisting of 132 housing units, has a 98% occupancy rate. As much as NMHC receives its revenues for its operations from the rental of housing units, repairs and maintenance of project-based units require the majority of the revenues collected. The housing units are nearly 20 years old and with each passing year, costs to maintain the units become greater. However, HUD's Housing Quality Standards (HQS) must continually be met. HUD's inspector has raised critical issues in the maintenance of the Section 8 units which are more than 15 years old, and thus, costs to bring up the units to standards will be greater and continue to escalate considering increased costs of materials purchased from vendors. Replacement of appliances and smoke alarms will be costly as well. Due to the continued preventive maintenance and repairs, the actual cost for FY 2006 totaled \$467,126 compared to prior year's expense.

NMHC works to account for the real estate properties which had been originally turned over to us from Marianas Public Lands. These assets have never been shown on our financial statements and should enhance NMHC's financial standing.

CDBG 5 Year Consolidated Plan

To improve the quality of life for all citizens of the Commonwealth of the Northern Mariana Islands (CNMI) through economic development and capital improvements such as public facilities (general); infrastructure upgrades; rehabilitation/revitalization and the removal of blight; public services and recreational opportunities in order to promote economic development throughout the CNMI. The CNMI intends to accomplish this over the next five years by meeting priority goals and objectives. During the course of the 2005-2009 Five Year Consolidated Plan (ConPlan), NMHC intends to utilize CDBG funding along with matching funds for larger yet fewer capital improvement projects, and would like to rotate the funding between islands each program year. However, this has never been achieved because of priorities of each island change based on needs. Public hearings are held on each island to solicit the input of the community as part of the ConPlan's Citizen Participation requirements.

NMHC would retain roughly 20% percent of the CDBG funding for smaller projects and activities for those islands not in the funding rotation. The HOME program is transitioning from funding rehabilitation into funding new construction. It is anticipated that forty-five new units will be completed over the next five years. The goal of Section 8 housing is to increase vouchers, concentrate on decreasing the waiting list, promoting self-sufficiency, promoting homeownership and maintain the existing units under management.

Commonwealth Development Authority
 Combined Statement of Net Assets
 As of September 30, 2006, 2005 and 2004

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Current assets	\$ 6,920,156	\$ 9,096,426	\$ 8,843,001
Other assets	19,584,021	23,305,984	21,081,500
Capital assets	15,689,514	17,696,691	17,507,216
Noncurrent assets	<u>21,144,397</u>	<u>28,014,773</u>	<u>30,374,556</u>
Total assets	<u>\$ 63,338,088</u>	<u>\$ 78,113,874</u>	<u>\$ 77,806,273</u>
Current liabilities	\$ 4,471,051	\$ 5,451,835	\$ 3,991,814
Noncurrent liabilities	<u>14,146,288</u>	<u>13,416,971</u>	<u>11,801,367</u>
Total liabilities	<u>18,617,339</u>	<u>18,868,806</u>	<u>15,793,181</u>
Invested in capital assets	15,689,514	17,696,691	17,507,216
Restricted	<u>29,031,235</u>	<u>41,548,377</u>	<u>44,505,876</u>
Total net assets	<u>44,720,749</u>	<u>59,245,068</u>	<u>62,013,092</u>
Total liabilities and net assets	<u>\$ 63,338,088</u>	<u>\$ 78,113,874</u>	<u>\$ 77,806,273</u>

Commonwealth Development Authority
Development Banking Division
Condensed Comparative Statement of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2006, 2005 and 2004

	2006	%	2005	%	Increase (Decrease) Between Years	%	2004
Operating revenues							
Interest on fees and loans	\$ 183,790	39%	\$ 207,020	60%	\$ (23,230)	-11%	\$ 220,598
Interest on investments	<u>287,193</u>	<u>61%</u>	<u>138,023</u>	<u>40%</u>	<u>149,170</u>	<u>108%</u>	<u>71,088</u>
	470,983	100%	345,043	100%	125,940	36%	291,686
Recoveries	<u>(119,317)</u>		<u>-</u>		<u>(119,317)</u>	<u>100%</u>	<u>-</u>
Net operating revenues	<u>351,666</u>		<u>345,043</u>		<u>6,623</u>	<u>2%</u>	<u>291,686</u>
Operating expenses							
Other	<u>153,261</u>	<u>100%</u>	<u>169,046</u>	<u>100%</u>	<u>(15,785)</u>	<u>-9%</u>	<u>180,331</u>
Total operating expenses	<u>153,261</u>	<u>100%</u>	<u>169,046</u>	<u>100%</u>	<u>(15,785)</u>	<u>-9%</u>	<u>180,331</u>
Operating income	<u>198,405</u>		<u>175,997</u>		<u>22,408</u>	<u>13%</u>	<u>111,355</u>
Nonoperating revenues (expenses)							
Other income	208,495		211,150		(2,655)	-1%	274,069
Write-off of due to/from other funds	6,695,556		-		6,695,556	100%	-
Interest expense	<u>(113,395)</u>		<u>(121,028)</u>		<u>7,633</u>	<u>-6%</u>	<u>(172,234)</u>
Total nonoperating revenues (expenses), net	<u>6,790,656</u>		<u>90,122</u>		<u>6,700,534</u>	<u>7435%</u>	<u>101,835</u>
Income before transfers	6,989,061		266,119		6,722,942	2526%	213,190
Transfers (out) in for capital development grants	<u>(2,608,963)</u>		<u>(1,359,489)</u>		<u>(1,249,474)</u>	<u>92%</u>	<u>75,406</u>
Change in net assets	<u>\$ 4,380,098</u>		<u>\$ (1,093,370)</u>		<u>\$ 5,473,468</u>	<u>-501%</u>	<u>\$ 288,596</u>

Commonwealth Development Authority
Development Corporation Division
Condensed Comparative Statement of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2006, 2005 and 2004

	2006	%	2005	%	Increase (Decrease) Between Years	%	2004
Operating revenues							
Interest and fees on loans	\$ 3,111,482	88%	\$ 2,883,716	88%	\$ 227,766	8%	\$ 3,643,461
Interest on investments	285,290	8%	140,038	4%	145,252	104%	88,192
Other	119,104	4%	256,053	8%	(136,949)	-53%	84,585
	<u>3,515,876</u>	100%	<u>3,279,807</u>	100%	<u>236,069</u>	7%	<u>3,816,238</u>
Bad debts	<u>(4,746,223)</u>		<u>(1,281,657)</u>		<u>(3,464,566)</u>	270%	<u>(5,168,121)</u>
Net operating revenues	<u>(1,230,347)</u>		<u>1,998,150</u>		<u>(3,228,497)</u>	-162%	<u>(1,351,883)</u>
Operating expenses							
Salaries and wages	453,327	22%	521,244	24%	(67,917)	-13%	534,830
Depreciation	65,984	3%	101,398	5%	(35,414)	-35%	100,298
Provision for foreclosed real estate	914,650	43%	743,424	34%	171,226	23%	-
Employee benefits	196,875	9%	201,865	9%	(4,990)	-2%	160,214
Professional fees	7,153	1%	117,790	5%	(110,637)	-94%	118,685
Office rent	122,733	6%	126,514	6%	(3,781)	-3%	128,762
Travel	48,061	2%	79,183	4%	(31,122)	-39%	93,431
Other	297,421	14%	276,562	13%	20,859	8%	248,397
Total operating expenses	<u>2,106,204</u>	100%	<u>2,167,980</u>	100%	<u>(61,776)</u>	-3%	<u>1,384,617</u>
Operating loss	<u>(3,336,551)</u>		<u>(169,830)</u>		<u>(3,166,721)</u>	1865%	<u>(2,736,500)</u>
Nonoperating revenues (expenses)							
Write-off of due to/from other funds	(6,695,556)		-		(6,695,556)	-100%	-
Interest expense	-		-		-	0%	(10,998)
Contributions to the CNMI	<u>(4,000,000)</u>		<u>-</u>		<u>(4,000,000)</u>	-100%	<u>-</u>
Total nonoperating revenues (expenses), net	<u>(10,695,556)</u>		<u>-</u>		<u>(10,695,556)</u>	-100%	<u>(10,998)</u>
Change in net assets	<u>\$ (14,032,107)</u>		<u>\$ (169,830)</u>		<u>\$ (13,862,277)</u>	8162%	<u>\$ (2,747,498)</u>

Commonwealth Development Authority
Northern Marianas Housing Corporation
Condensed Comparative Statement of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2006, 2005 and 2004

	2006	%	2005	%	Increase (Decrease) Between Years	%	2004
Operating revenues							
Interest and fees on loans	\$ 1,195,369	16%	\$ 1,279,806	17%	\$ (84,437)	-7%	\$ 1,314,345
Section 8 grant	4,055,736	54%	3,542,192	46%	513,544	14%	3,417,261
CDBG grant	765,393	10%	1,676,479	22%	(911,086)	-54%	757,557
Other grants	1,279,000	17%	869,126	11%	409,874	47%	218,226
Other	187,046	1%	289,054	5%	(102,008)	-35%	695,352
	<u>7,482,544</u>	100%	<u>7,656,657</u>	100%	<u>(174,113)</u>	-2%	<u>6,402,741</u>
Bad debts	<u>(6,892,390)</u>		<u>(228,025)</u>		<u>(6,664,365)</u>	2923%	<u>(169,999)</u>
Net operating revenues	<u>590,154</u>		<u>7,428,632</u>		<u>(6,838,478)</u>	-92%	<u>6,232,742</u>
Operating expenses							
Section 8 program	2,471,599	34%	2,075,088	29%	396,511	19%	1,816,204
CDBG grant projects	765,393	10%	1,676,479	24%	(911,086)	-54%	757,557
Repairs and maintenance	512,660	7%	474,148	7%	38,512	8%	701,982
Salaries and wages	560,341	8%	446,487	6%	113,854	25%	633,638
Depreciation	613,180	8%	596,073	8%	17,107	3%	592,217
Other grant programs	1,279,000	17%	869,126	12%	409,874	47%	218,226
Employee benefits	260,958	4%	251,089	4%	9,869	4%	194,238
Professional fees	194,106	3%	148,573	2%	45,533	31%	72,551
Travel	45,198	1%	48,000	1%	(2,802)	-6%	49,803
Office rent	5,273	0%	9,100	0%	(3,827)	-42%	9,307
Other	606,703	8%	508,697	7%	98,006	19%	441,886
Total operating expenses	<u>7,314,411</u>	100%	<u>7,102,860</u>	100%	<u>211,551</u>	3%	<u>5,487,609</u>
Operating (loss) income	<u>(6,724,257)</u>		<u>325,772</u>		<u>(7,050,029)</u>	-2164%	<u>745,133</u>
Nonoperating revenues (expenses)							
Write-off of note and interest payable to CNMI	4,174,042		-		4,174,042	100%	-
Other income	41,210		-		41,210	100%	-
Interest income	51,463		42,377		9,086	21%	44,212
Interest expense	(764,713)		(766,533)		1,820	0%	(768,628)
Infrastructure transferred out to related party	<u>(1,769,371)</u>		<u>-</u>		<u>(1,769,371)</u>	-100%	<u>-</u>
Total nonoperating revenues (expenses), net	<u>1,732,631</u>		<u>(724,156)</u>		<u>2,456,787</u>	-339%	<u>(724,416)</u>
Change in net assets	<u>\$ (4,991,626)</u>		<u>\$ (398,384)</u>		<u>\$ (4,593,242)</u>	1153%	<u>\$ 20,717</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Combined Statements of Net Assets
September 30, 2006 and 2005

<u>ASSETS</u>	2006	2005 (As Restated)
Current assets:		
Cash and cash equivalents	\$ 1,712,434	\$ 3,910,505
Time certificates of deposit	1,022,514	511,448
Receivables:		
Current portion of loan receivable, net	3,278,521	3,012,885
Current portion capital development loans from related parties, net	219,218	644,195
Rent, net	57,122	35,878
Accrued interest, net of allowance for doubtful accounts of \$16,499,317 and \$13,661,832 as of September 30, 2006 and 2005, respectively	480,277	903,726
Other	133,287	65,669
Prepaid expenses	16,783	12,120
Total current assets	<u>6,920,156</u>	<u>9,096,426</u>
Other assets:		
Cash and cash equivalents, restricted	7,559,694	5,633,461
Time certificates of deposit, restricted	12,024,327	17,672,523
Total other assets	<u>19,584,021</u>	<u>23,305,984</u>
Noncurrent assets:		
Loans receivable, net	19,066,784	25,724,770
Capital development loans receivable from related parties, net	2,077,613	2,290,003
Property and equipment, net	2,814,400	5,161,806
Asset held for sale	443,000	443,000
Land	10,409,682	10,409,682
Foreclosed real estate	2,022,432	1,682,203
Total noncurrent assets	<u>36,833,911</u>	<u>45,711,464</u>
	<u>\$ 63,338,088</u>	<u>\$ 78,113,874</u>
<u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Current installment of notes payable to related party	\$ 107,457	\$ 102,465
Accounts payable and accrued expenses	2,085,215	678,068
Interest payable	1,162,317	3,568,269
Due to grantor agency	852,677	938,111
Deferred revenues	263,385	164,922
Total current liabilities	4,471,051	5,451,835
Deferred revenues, net of current portion	3,544,179	1,711,393
Notes payable to related party, net of current installments	10,602,109	11,705,578
Total liabilities	<u>18,617,339</u>	<u>18,868,806</u>
Commitments and contingencies		
Net assets:		
Invested in capital assets	15,689,514	17,696,691
Restricted	29,031,235	41,548,377
Total net assets	<u>44,720,749</u>	<u>59,245,068</u>
	<u>\$ 63,338,088</u>	<u>\$ 78,113,874</u>

See accompanying notes to financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

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

	<u>2006</u>	<u>2005</u> <u>(As Restated)</u>
Operating revenues:		
Interest and fees on loans	\$ 4,490,641	\$ 4,370,542
Section 8 income:		
Federal housing assistance rentals	3,977,799	3,444,245
Tenant share	77,937	97,947
Interest on investments	572,483	278,061
HOME Investment Partnership Program grants	1,211,497	815,449
HOME Investment Partnership grants program income	119,276	-
CDBG Program Grant	765,393	1,676,479
ESG Program Grant	67,503	53,677
Housing rental	963	225
Other	91,714	544,882
	<u>11,375,206</u>	<u>11,281,507</u>
Bad debts	<u>(11,638,614)</u>	<u>(1,509,682)</u>
Net operating revenues	<u>(263,408)</u>	<u>9,771,825</u>
Operating expenses:		
Section 8 rental	2,471,599	2,075,088
HOME Investment Partnership Program grants	1,211,497	815,449
Salaries and wages	1,013,668	967,731
CDBG Program Grant	765,393	1,676,479
Depreciation	679,164	697,471
Provision for foreclosed real estate	914,650	743,424
Repairs and maintenance	512,660	474,148
Employee benefits	457,833	452,954
Professional fees	201,259	266,363
Office rent	128,006	135,614
Travel	93,259	127,183
ESG Program Grant	67,503	53,677
Other	963,188	954,305
Total operating expenses	<u>9,479,679</u>	<u>9,439,886</u>
Operating (loss) income	<u>(9,743,087)</u>	<u>331,939</u>
Nonoperating revenues (expenses):		
Write-off of note and interest payable to CNMI	4,174,042	-
Other income	249,705	211,150
Interest income	51,463	42,377
Interest expense	(878,108)	(887,561)
Infrastructure transferred out to related party	(1,769,371)	-
Contributions to the CNMI	(4,000,000)	-
Total nonoperating revenues (expenses), net	<u>(2,172,269)</u>	<u>(634,034)</u>
Loss before transfers	<u>(11,915,356)</u>	<u>(302,095)</u>
Transfers out for capital development grants	<u>(2,608,963)</u>	<u>(1,359,489)</u>
Change in net assets	<u>(14,524,319)</u>	<u>(1,661,584)</u>
Net assets - beginning	<u>59,245,068</u>	<u>60,906,652</u>
Net assets - ending	<u>\$ 44,720,749</u>	<u>\$ 59,245,068</u>

See accompanying notes to financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

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

	2006	2005 (As Restated)
Cash flows from operating activities:		
Cash received from interest and fees on loans receivable	\$ 1,861,644	\$ 2,012,464
Cash received from interest and fees on capital development loans	182,986	227,169
Interest and dividends on investments	536,840	273,515
Cash payments to suppliers for goods and services	(1,228,911)	(2,340,748)
Cash received from customers	105,686	368,848
Cash payments to employees for services	(1,013,668)	(967,731)
Cash received from federal grant awards	6,056,034	7,001,005
Cash payments from federal grant awards	<u>(5,094,152)</u>	<u>(5,094,841)</u>
Net cash provided by operating activities	<u>1,406,459</u>	<u>1,479,681</u>
Cash flows from capital and related financing activities:		
Acquisition of property and equipment	(101,129)	(202,011)
Proceeds from sale of property and equipment	-	431,630
Net (disbursements of) proceeds from loans receivable	(794,164)	1,514,628
Contributions to the CNMI	(4,000,000)	-
Payments received on capital development loans	637,366	798,698
Transfers for capital development grants	(2,608,963)	(1,359,489)
Interest paid on notes payable	<u>-</u>	<u>(1,820)</u>
Net cash (used for) provided by capital and related financing activities	<u>(6,866,890)</u>	<u>1,181,636</u>
Cash flows from investing activities:		
Net proceeds from (purchase of) restricted cash and cash equivalents	(1,926,233)	5,080,967
Net proceeds from (purchase of) time certificates of deposit	5,137,130	(7,316,899)
Interest income	<u>51,463</u>	<u>42,377</u>
Net cash provided by (used for) investing activities	<u>3,262,360</u>	<u>(2,193,555)</u>
Net (decrease) increase in cash and cash equivalents	(2,198,071)	467,762
Cash and cash equivalents at beginning of year	<u>3,910,505</u>	<u>3,442,743</u>
Cash and cash equivalents at end of year	<u>\$ 1,712,434</u>	<u>\$ 3,910,505</u>
Reconciliation of operating (loss) income to net cash provided by operating activities:		
Operating (loss) income	\$ (9,743,087)	\$ 331,939
Adjustments to reconcile operating (loss) income to net cash provided by operating activities:		
Provision for doubtful accounts	11,638,614	1,509,682
Provision for foreclosed real estate	914,650	743,424
Depreciation	679,164	697,471
Gain on sale of property and equipment	-	(229,600)
(Increase) decrease in assets:		
Receivables:		
Rent	(64,928)	(44,606)
Other	(67,618)	45,219
Accrued interest	(2,414,036)	(2,107,630)
Prepaid expenses	(4,663)	9,063
Increase (decrease) in liabilities:		
Accounts payable and accrued expenses	553,797	(413,392)
Due to grantor agency	<u>(85,434)</u>	<u>938,111</u>
Net cash provided by operating activities	<u>\$ 1,406,459</u>	<u>\$ 1,479,681</u>

See accompanying notes to financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

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

	<u>2006</u>	<u>2005</u> <u>(As Restated)</u>
Supplemental disclosure of noncash capital and related financing activities:		
Transfer of Koblerville Expansion Project:		
Noncash decrease in property and equipment	\$ 1,769,371	\$ -
Noncash increase in nonoperating expenses	<u>(1,769,371)</u>	<u>-</u>
	<u>\$ -</u>	<u>\$ -</u>
Recognition of liability arising from defaulted loans guaranteed:		
Noncash increase in other assets	\$ 853,350	\$ -
Noncash increase in accounts payable and accrued expenses	<u>(853,350)</u>	<u>-</u>
	<u>\$ -</u>	<u>\$ -</u>
Write-off of note and interest payable to CNMI:		
Noncash decrease in note payable	\$ (1,003,377)	\$ -
Noncash decrease in interest payable	<u>(3,170,665)</u>	<u>-</u>
Noncash increase in nonoperating revenues	<u>4,174,042</u>	<u>-</u>
	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(1) Reporting Entity

The Commonwealth Development Authority (CDA), a component unit of the Commonwealth of the Northern Mariana Islands (CNMI), was created as an autonomous public agency of the CNMI pursuant to Public Law 4-49 as amended by Public Laws 4-63 and 5-27. CDA is affiliated with all other component units of the CNMI Government. CDA's existence is to be perpetual and it shall have all the rights and privileges of a corporation. The purpose of CDA is to stimulate the economic development of the CNMI.

The functions of CDA are carried out through a Development Banking Division (DBD, government and public sector activities), a Development Corporation Division (DCD, private sector activities), and a discretely presented component unit, the Northern Marianas Housing Corporation (NMHC). NMHC, formerly the Mariana Islands Housing Authority (MIHA), was established under Public Law 5-37 to assist in the development and administration of low cost residential housing in the Northern Mariana Islands. In 1977, Public Law 5-37 was succeeded by Public Law 5-67, which empowered MIHA to provide low cost residential housing and employment through the construction, maintenance, and repair of such housing. On October 20, 1994, Executive Order 94-3 became effective which abolished MIHA and all of its functions, assets and liabilities were transferred to CDA. CDA established a subsidiary corporation (i.e., NMHC) to account for the operations, assets and liabilities of MIHA. NMHC is governed by a five member Board of Directors appointed by the Board of Directors of CDA. The purpose and functions of the two divisions and NMHC are as follows:

Development Banking Division:

- To receive and hold United States economic assistance for economic development loans provided under Section 702(c) of the Covenant to Establish a Commonwealth of the Northern Mariana Islands in Political Union with the United States of America (the Covenant);
- To aid in the financing of capital improvement projects and other projects undertaken by the CNMI and its autonomous public agencies;
- To achieve the greatest possible return, in terms of economic development, on the funds made available to the CNMI by the United States in accordance with the Covenant; and on such other funds as may be made available to CDA as capital contributions;
- To disseminate modern practices and techniques of financing, management and business administration in order to raise the levels of efficiency and productivity in all sectors; and
- To serve as the Northern Marianas development bank identified in Article IX, Section 6(c) of the Constitution.

As such, DBD considers all its net assets restricted for such purposes.

Development Corporation Division:

- To identify, formulate, initiate, stimulate and facilitate business and commercial enterprises, with special emphasis on agricultural and marine resources, manufacturing and processing activities, import substitution, export development and responsible use of indigenous raw materials;

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(1) Reporting Entity, Continued

Development Corporation Division, Continued:

- To identify, formulate, initiate, stimulate and facilitate business and commercial enterprises where a service necessary and vital to economic development is required, or where profit incentives are not sufficient to attract private sector investors; and
- To serve as the economic development loan fund agency for qualified private sector enterprises.

As such, DCD considers all its net assets, except net assets invested in capital assets, to be restricted for such purposes.

Northern Marianas Housing Corporation:

- To administer direct loans to qualified individuals for housing construction;
- To participate as guarantor or trustee in housing loan programs;
- To develop and construct rental housing;
- To construct and/or administer various other Federal and local residential and housing projects; and
- To participate in projects subsidized by the U.S. Department of Housing and Urban Development (HUD). Upon completion of the projects, the residential units are rented to qualifying families and individuals.

As such, NMHC considers all its net assets, except net assets invested in capital assets, to be restricted for such purposes.

(2) Summary of Significant Accounting Policies

The accounting policies of CDA 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. CDA has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(2) Summary of Significant Accounting Policies, Continued

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 on 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 by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Budgets

In accordance with Public Law 3-68, the Planning and Budgeting Act of 1983, CDA submits an annual budget to the CNMI Office of the Governor.

Cash and Cash Equivalents and Time Certificates of Deposit

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

For purposes of the statements of net assets and cash flows, cash and cash equivalents is defined as cash held in demand deposits, savings and unrestricted time certificates of deposit with a maturity date within three months of the date acquired. Deposits maintained in time certificates of deposit with original maturity dates greater than ninety days are separately classified. At September 30, 2006 and 2005, total unrestricted cash and cash equivalents were \$1,712,434 and \$3,910,505, respectively, and the corresponding bank balances were \$1,881,058 and \$4,524,439, respectively. Of the bank balance amounts, \$1,881,058 and \$4,524,439 are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance as of September 30, 2006 and 2005, respectively. Bank deposits in the amount of \$254,662 and \$335,978 were FDIC insured as of September 30, 2006 and 2005, respectively. CNMI law does not require component units to collateralize their bank accounts and thus CDA's deposits in excess of FDIC insurance are uncollateralized. Accordingly, the deposits are exposed to custodial credit risk.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(2) Summary of Significant Accounting Policies, Continued

Cash and Cash Equivalents and Time Certificates of Deposit, Continued

Time certificates of deposit (TCDs), with maturities of more than three months when purchased, had fair value approximating cost as of September 30, 2006 and 2005. At September 30, 2006 and 2005, approximately \$1,022,514 and \$511,448 respectively, of CDA's TCDs are with financial institutions subject to FDIC. As of September 30, 2006 and 2005, TCDs in the amount of \$100,000 were FDIC insured. CNMI law does not require component units to collateralize their bank accounts and thus CDA's deposits in excess of FDIC insurance are uncollateralized. Accordingly, the deposits are exposed to custodial credit risk.

Prepaid Expenses

Payments made to vendors for services that will benefit future periods are recorded as prepaid expenses.

Property and Equipment

Property and equipment are recorded at cost. Depreciation is provided by using the straight-line method over the estimated useful lives of the assets. Current policy is to capitalize items in excess of \$500.

Long-lived assets for which management has committed to a plan to dispose of the assets, whether by sale or abandonment, are reported at the lower of carrying amount or fair value less costs to sell.

Foreclosed Real Estate

Real estate properties acquired through, or in lieu of, loan foreclosure are to be sold and are initially recorded at fair value at the date of foreclosure less estimated selling costs establishing a new cost basis. Valuations are periodically performed by management and adjustments are made to reflect the real estate at the lower of the carrying amount or fair value less estimated costs to sell. Operating expenses or income, reductions in estimated values, and gains or losses on disposition of such properties are charged to current operations.

Land

Land is recorded at fair market value. Valuations are periodically performed by management and adjustments are made to reflect the land at the lower of the carrying amount or fair market value.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(2) Summary of Significant Accounting Policies, Continued

Loans Receivable, Interest Receivable and Allowance for Loan Losses

Loans and interest receivable are stated at the amount of unpaid principal and interest, reduced by an allowance for loan losses. Interest on loans is calculated by using the simple interest method on daily balances of the principal amount outstanding. The allowance for loan losses is established through a provision for doubtful accounts charged to expense. Loans are charged against the allowance for loan losses when management believes that the collection of the principal is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing loans that may be uncollectible, based on evaluations of the collectability of loans and prior loan loss experience. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans and current economic conditions that may affect the borrowers' ability to pay.

Restricted Cash and Cash Equivalents and Time Certificates of Deposit

As described in note 1, DBD receives and holds United States economic assistance for economic development loans provided under Section 702(c) of the Covenant. The *Agreement of the Special Representatives on Future United States Financial Assistance for the Northern Mariana Islands* requires that a revolving fund be established into which repayments of principal and interest from revenue-producing projects shall be deposited for financing of additional revenue-producing capital development projects. From its inception on October 1, 1985, DBD has exclusively accounted for Covenant 702(c) funding and thus represents the required revolving fund.

As described in note 1, DCD serves as the economic development loan fund agency for qualified private sector enterprises. DCD accounts for all funds received by the former Northern Mariana Islands Economic Development Loan Fund pursuant to Article VII, Section 702(c) of the Covenant from February 15, 1975 through September 30, 1985. In addition to the aforementioned financial resources, DCD has been designated as the administrative agency for economic development loans transferred from the Trust Territory of the Pacific Islands government to the CNMI. DCD represents a revolving fund to account for economic development loans to qualified private sector enterprises.

As described in note 1, NMHC administers various Federal and local residential and housing projects. In administering these programs, NMHC is required to maintain certain funds as collateral or in accounts which are restricted for specific purposes.

Revenue Recognition

Operating revenues include all direct revenues such as interest and fees on loans, federal grants and interest on investments.

Interest on loans is calculated by using the simple interest method on daily balances of the principal amount outstanding. Interest on loans is accrued and credited to income based on the principal amount outstanding for both performing and nonperforming loans. Due to current confines of CDA and NMHC's systems, interest on nonperforming loans remains to be accrued and credited to income. However, a bad debt expense is recognized for the amount of interest deemed uncollectible. CDA and NMHC are currently working to be able to prospectively cease recognition of interest income on nonperforming loans.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(2) Summary of Significant Accounting Policies, Continued

Revenue Recognition, Continued

Federal grant revenues are recognized when allowable expenses are incurred.

Non-operating revenues result from capital and financing activities.

Retirement Plan

CDA 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 CDA is required to contribute at an actuarially determined rate. The current rate is 26.4% of annual covered payroll. The contribution requirements of plan members and CDA are established and may be amended by the Fund's Board of Trustees. CDA's contributions to the Fund for the years ended September 30, 2006, 2005 and 2004 were \$326,053, \$331,105 and \$273,169, respectively, which were equal to the required contributions for each year.

Net Assets

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

- Invested in capital assets; capital assets, net of accumulated depreciation.
- Restricted:

Nonexpendable - Net assets subject to externally imposed stipulations that CDA maintain them permanently. At September 30, 2006 and 2005, CDA does not have nonexpendable net assets.

Expendable - Net assets whose use by CDA is subject to externally imposed stipulations that can be fulfilled by actions of CDA pursuant to those stipulations or that expire by the passage of time. As described in note 1, CDA considers all assets, except investments in capital assets, to be restricted for economic development.

- Unrestricted; net assets that are not subject to externally imposed stipulations. As CDA considers all assets, except investments in capital assets, to be restricted for economic development, CDA does not have unrestricted net assets of September 30, 2006 and 2005.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During fiscal year 2006, CDA implemented the following pronouncements:

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

The implementation of these pronouncements did not have a material impact on the accompanying 2006 financial statements.

In April 2004, GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. GASB Statement No. 43 establishes uniform financial reporting for other postemployment benefit plans by state and local governments. The provisions of this Statement are effective for periods beginning after December 15, 2005. Management does not believe that the implementation of this statement will have a material effect on the financial statements of CDA.

In May 2004, GASB issued Statement No. 44, *Economic Condition Reporting: The Statistical Section, an amendment to NCGA Statement 1*. GASB Statement No. 44 improves the understandability and usefulness of statistical section information and adds information from the new financial reporting model for state and local governments required by GASB Statement No. 34. The provisions of this Statement are effective for periods beginning after June 15, 2005. Management does not believe that the implementation of this statement will have a material effect on the financial statements of CDA.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Post employment Benefits Other Than Pensions*. 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. 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 CDA.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

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

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 CDA.

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

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 CDA.

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 CDA.

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 CDA.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(2) Summary of Significant Accounting Policies, Continued

Off-Balance Sheet Financial Instruments

In the ordinary course of business, CDA has entered into off-balance sheet financial instruments consisting of commitments to extend credit and loan guarantees. Such financial instruments are recorded in the financial statements when they become payable.

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.

Reclassification

Certain 2005 balances in the accompanying financial statements have been reclassified to conform to the 2006 presentation.

(3) Restricted Cash and Cash Equivalents and Time Certificates of Deposit

Development Banking Division

Restricted cash and cash equivalents and time certificates of deposit represent the proceeds of Covenant funding and liquidated revenue bonds derived from pledged Covenant funding, and are restricted for capital development purposes. Proceeds are deposited with commercial lending institutions and the securities are held in the name of CDA.

At September 30, 2006 and 2005, restricted cash and cash equivalents and time certificates of deposit consist of time certificates of deposit with maturity periods ranging from eight to sixteen months and amounts held in demand deposit accounts. These investments are presented at fair value in the accompanying financial statements, in accordance with GASB Statement No. 31. At September 30, 2006 and 2005, total restricted cash and cash equivalents and time certificates of deposit were \$8,568,102 and \$10,176,252, respectively, with \$8,568,102 and \$10,176,252, respectively, maintained in financial institutions subject to FDIC insurance. Restricted cash and cash equivalents and investments in the amount of \$100,000 were FDIC insured as of September 30, 2006 and 2005. CNMI law does not require component units to collateralize their bank accounts and thus CDA's restricted cash and cash equivalents and investments in excess of FDIC insurance are uncollateralized. Accordingly, the deposits are exposed to custodial credit risk.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(3) Restricted Cash and Cash Equivalents and Time Certificates of Deposit, Continued

Development Corporation Division

At September 30, 2006 and 2005, restricted cash and cash equivalents and time certificates of deposit consist of time certificates of deposit with maturity periods ranging from six to nine months and amounts held in demand deposit accounts. Restricted cash and cash equivalents and time certificates of deposit amounted to \$5,804,402 and \$10,137,476 at September 30, 2006 and 2005, respectively, and comprise amounts maintained as a guarantee against loans issued by the bank. Of the bank balance amounts, \$4,842,412 and \$8,893,913 is maintained in financial institutions subject to FDIC insurance as of September 30, 2006 and 2005, respectively, and \$961,990 and \$1,242,503 are maintained at a non-FDIC insured bank as of September 30, 2006 and 2005, respectively. Restricted cash and cash equivalents and investments in the amount of \$100,000 were FDIC insured as of September 30, 2006 and 2005. Accordingly, the deposits are exposed to custodial credit risk.

Northern Marianas Housing Corporation

NMHC maintains depository accounts with financial institutions in the CNMI which are restricted for various purposes, as detailed below. At September 30, 2006 and 2005, restricted cash and cash equivalents consist of amounts held in demand deposit accounts and time certificates of deposit with sixty days maturity. Of the amounts detailed below, \$145,338 and \$100,000 at September 30, 2006 and 2005, respectively, were FDIC insured. Accordingly, the deposits are exposed to custodial credit risk.

	<u>2006</u>	<u>2005</u>
<u>Restricted cash and cash equivalents:</u>		
Escrow account maintained as a guarantee for any deficiency in foreclosure proceeds related to U.S. Farmers Home Administration loans	\$ 255,588	\$ 254,313
Savings account restricted for Koblerville Section 8 project repairs and maintenance expenses, per contract with the U.S. Department of Housing and Urban Development	196,033	195,191
Savings account maintained as a guarantee of housing loans made by a savings and loan in the CNMI	93,172	120,611
MPLT collateral account	2,001,112	1,237,072
Time certificates of deposit for MPLT loan program	1,070,234	1,033,120
Collateral account designated as sinking fund for U.S. Farmers Home Administration defaulted loans	907,649	-
Other depository accounts reserved for various purposes	<u>687,729</u>	<u>151,949</u>
	<u>\$ 5,211,517</u>	<u>\$ 2,992,256</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(3) Restricted Cash and Cash Equivalents and Time Certificates of Deposit, Continued

CDA's investments in time certificates of deposit had the following maturities at September 30, 2006:

	<u>Fair Value</u>	<u>Investment Maturities (In Years)</u>			
		<u>Less Than 1</u>	<u>1 - 5</u>	<u>6 - 10</u>	<u>More Than 10</u>
DBD	\$ 7,181,915	\$ 2,902,307	\$ 4,279,608	\$ -	\$ -
DCD	<u>4,842,412</u>	<u>567,414</u>	<u>4,274,998</u>	<u>-</u>	<u>-</u>
	<u>\$ 12,024,327</u>	<u>\$ 3,469,721</u>	<u>\$ 8,554,606</u>	<u>\$ -</u>	<u>\$ -</u>

(4) Loans Receivable

Development Corporation Division

As described in note 1, DCD was established to serve as the economic development loan fund agency for qualified private sector enterprises pursuant to Public Law 4-49. In this capacity all functions, powers, duties, funds, contracts, obligations and liabilities managed and administered by the Northern Marianas Islands Economic Development Loan Fund (EDLF) were transferred to DCD. EDLF was established pursuant to Article VII, Section 702(c) of the Covenant, dated February 15, 1975, to administer financial resources received under the Covenant which were specifically set aside for a loan program to assist the general economic development of the Northern Marianas Islands. Additionally, the Trust Territory of the Pacific Islands Government contributed to the economic development loan portfolio.

Outstanding loans are due within various periods not to exceed twenty (20) years. The interest rates charged are based on the economic purpose of the loan. Production development loans bear interest at 9%, marine and agriculture loans bear interest at 5%, commercial development loans bear interest at 9%, and microloans bear interest at 9% to 12%.

Northern Marianas Housing Corporation

NMHC makes loans for the specific purpose of providing residents of the Northern Mariana Islands with approved low-cost housing. The loans have terms from ten to thirty-three years in duration at interest rates of 4.5% to 12%. Loans are restricted to ninety percent (90%) of the appraised value of the property or the purchase price, whichever is lower. For construction loans, the purchase price of the property is defined as the value of the land plus the estimated cost of construction.

Major classifications of economic development loans as of September 30, 2006 and 2005 (with combining information as of September 30, 2006), are as follows:

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Notes to Financial Statements
September 30, 2006 and 2005

(4) Loans Receivable, Continued

	<u>Development Corporation Division</u>	<u>Northern Marianas Housing Corporation</u>	<u>2006</u>	<u>2005</u>
General	\$ 24,718,737	\$ 1,905,415	\$ 26,624,152	\$ 25,896,386
Direct family home loans	-	12,024,566	12,024,566	11,904,207
Marine	5,566,464	-	5,566,464	5,565,371
Agriculture	2,638,013	-	2,638,013	2,672,969
HOME Investment Partnerships Act grant	-	2,294,299	2,294,299	1,584,463
Housing construction	-	598,220	598,220	604,057
Tinian turnkey	-	505,645	505,645	511,737
Home revenue bond	-	84,658	84,658	85,956
Section 8	-	164,793	164,793	160,294
Housing preservation grant	-	49,713	49,713	53,339
Trust Territory Guaranteed	<u>8,887</u>	<u>-</u>	<u>8,887</u>	<u>8,887</u>
Loan principal receivable	32,932,101	17,627,309	50,559,410	49,047,666
Less allowance for loan losses	<u>(21,705,993)</u>	<u>(6,508,112)</u>	<u>(28,214,105)</u>	<u>(20,310,011)</u>
Net loans receivable	<u>\$ 11,226,108</u>	<u>\$ 11,119,197</u>	<u>\$ 22,345,305</u>	<u>\$ 28,737,655</u>

Maturities of the above principal balances subsequent to September 30, 2006, will be as follows:

	<u>Development Corporation Division</u>	<u>Northern Marianas Housing Corporation</u>	<u>Total</u>
Fully matured and others	\$ 18,611,086	\$ 849,741	\$ 19,460,827
1 - 6 months	2,006,115	780,670	2,786,785
7 - 18 months	2,812,344	968,777	3,781,121
19 months - 3 years	3,191,556	1,328,107	4,519,663
After 3 years	<u>6,311,000</u>	<u>13,700,014</u>	<u>20,011,014</u>
	<u>\$ 32,932,101</u>	<u>\$ 17,627,309</u>	<u>\$ 50,559,410</u>

Allowance for Loan Losses

An analysis of the change in the allowance for loan losses is as follows:

	<u>Development Corporation Division</u>	<u>Northern Marianas Housing Corporation</u>	<u>2006</u>	<u>2005</u>
Balance - beginning of year	\$ 19,217,038	\$ 1,092,973	\$ 20,310,011	\$ 20,874,907
Recoveries of loan previously charged-off	-	-	-	(753,489)
Provision for loan losses	<u>2,488,955</u>	<u>5,415,139</u>	<u>7,904,094</u>	<u>188,593</u>
Balance - end of year	<u>\$ 21,705,993</u>	<u>\$ 6,508,112</u>	<u>\$ 28,214,105</u>	<u>\$ 20,310,011</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(5) Due from/to Other Funds

Due from/to balances between NMHC and DBD result from loans made by CDA to the former Marianas Islands Housing Authority (MIHA) prior to that entity being established as a subsidiary corporation of CDA. The year end balances are summarized as follows:

	<u>2006</u>	<u>2005</u>
Housing construction loan. On February 3, 1999, CNMI Public Law 11-57 authorized CDA to write off the portion of this loan not considered recoverable through sale of housing construction units. Interest has therefore been suspended pending sales of the units.	\$ 1,027,211	\$ 1,257,410
Operating expenses	<u>54,045</u>	<u>54,046</u>
	<u>\$ 1,081,256</u>	<u>\$ 1,311,456</u>

DBD provided an allowance of \$119,316 to the outstanding balance of the due from NMHC at September 30, 2006.

Due from/to balances between DBD and DCD result from the use of restricted funding between the two divisions. The year end balances are summarized as follows:

	<u>2006</u>	<u>2005</u>
Principal and interest payments made by DCD on a note payable to Bank of America-Asia Limited.	\$ 13,747,096	\$ 13,747,096
Principal and interest payments made by NMHC on the note payable to DBD.	(7,372,201)	(7,142,001)
Amount written-off	(6,695,556)	-
Operating expenses	<u>280,267</u>	<u>278,883</u>
	<u>\$ (40,394)</u>	<u>\$ 6,883,978</u>

NMHC is obligated to repay CDA for the construction cost of housing units at Sugar King II.

All due from/to balances of CDA are eliminated in the basic financial statements.

(6) Capital Development Loans Receivable From Related Parties

As described in note 2, DBD is required to establish a revolving fund into which repayments of principal and interest from revenue-producing projects shall be deposited. The revolving fund consists of the following notes receivable as of September 30, 2006 and 2005:

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Notes to Financial Statements
September 30, 2006 and 2005

(6) Capital Development Loans Receivable From Related Parties, Continued

	<u>2006</u>	<u>2005</u>
Note receivable from the Commonwealth Utilities Corporation (CUC), bearing interest at 7% per annum, with quarterly principal and interest payments due February 17, 1992 in the amount of \$658,469, with a maturity date of February 17, 2013. Proceeds are to be used for certain power generation and distribution projects within the CNMI.	\$ 30,000,000	\$ 30,000,000
Note receivable from CUC, bearing interest at 5% per annum, with quarterly principal and interest payments due January 12, 1994 in the amount of \$359,514, with a maturity date of January 12, 2014. Proceeds are to be used for certain water projects within the CNMI.	16,068,750	16,068,750
Due from CUC, bearing interest at 7% per annum, with monthly principal and interest payments of \$58,509. No promissory agreement related to this note has been signed.	10,000,000	10,000,000
Note receivable from CUC, bearing interest at 7% per annum, with quarterly principal and interest payments due two years after January 30, 1990 in the amount of \$276,471, with a maturity date of January 30, 2000. Proceeds are to be used for Saipan Power Plant expansion.	5,500,000	5,500,000
Note receivable from the Commonwealth Ports Authority (CPA), bearing interest at 2.5% per annum, with quarterly principal and interest payments in the amount of \$204,113, with maturity date of November 16, 2014. Proceeds are to be used for the Saipan Harbor Project.	<u>6,887,181</u>	<u>7,524,548</u>
Total capital development loans receivable	68,455,931	69,093,298
Less allowance for loan losses	<u>(66,159,100)</u>	<u>(66,159,100)</u>
Net capital development loans receivable	\$ <u>2,296,831</u>	\$ <u>2,934,198</u>

Allowance for Loan Losses

At September 30, 2006, estimated proceeds from principal and interest repayments of loans receivable (excluding all CUC loans) for the following years ending September 30, are as follows:

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(6) Capital Development Loans Receivable From Related Parties, Continued

Allowance for Loan Losses, Continued

<u>Year ending September 30,</u>	<u>Principal Amount</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 657,339	\$ 165,942	\$ 823,281
2008	666,927	149,526	816,453
2009	683,757	132,696	816,453
2010	701,012	115,441	816,453
2011	718,702	97,751	816,453
2012 - 2015	<u>3,459,444</u>	<u>190,044</u>	<u>3,649,488</u>
	<u>\$ 6,887,181</u>	<u>\$ 851,400</u>	<u>\$ 7,738,581</u>

On February 4, 2003, CDA authorized the deferral of 50% of CPA's current outstanding loan payment amounts, the reduction of quarterly loan payments for one year ended September 30, 2004, and extension of terms of the loan to accommodate the deferral. An amendment to the loan agreement has not been signed by both CPA and CDA. Management provided an allowance of \$4,590,350 representing 67% and 61% of the outstanding principal balance at September 30, 2006 and 2005, respectively.

The most recent audited financial statements of CUC are as of September 30, 2005, and reflect a net deficiency of \$52,781,063 and a working capital deficiency of \$156,315,715. Management of CDA has determined that collection of the principal of the above described loans to CUC is unlikely and has included 100% of the loan balances in its allowance for loan losses. CDA has also suspended accrual of interest income on the loans from CUC since collection of the principal has become doubtful. Unrecorded accrued interest receivable amounted to \$105,094,248 and \$95,026,401 at September 30, 2006 and 2005, respectively.

On November 21, 2002, a Memorandum of Agreement (MOA) was established between CDA and CUC to waive a portion of the capital development loans receivable and the conversion into equity ownership of the balance. Public Law 13-35 effectuated terms of the MOA requiring CDA to waive \$16,068,750 and waive certain specified interest payments and for other purposes. Public Law 13-36 effectuated terms of the MOA by authorizing CUC to issue shares to CDA of cumulative nonconvertible non-transferable preferred stock valued at \$45,500,000.

On June 6, 2006, the Governor of the CNMI approved Public Law (P.L.) No. 15-12 which authorized CDA to waive the sum of \$45,500,000 of the principal amount owed by CUC, such amount being the aggregate sum of all outstanding sewer and water project loans given to CUC and referenced in an amended MOA executed in January 2004. Pursuant to the amended MOA, CDA is authorized to waive any and all accrued interest owed by CUC on all outstanding loans. Section 2 of P.L. 15-12 provides that in the event the power generation system for the CNMI is privatized and controlled by an independent power producer, fifty percent of the principal amount of \$45,500,000 shall be paid by the independent power producer to CDA. As of September 30, 2006 and 2005, no adjustments have been made to the accompanying financial statements as CUC and CDA have yet to finalize an agreement on the execution of the provisions of P.L. 15-12.

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Notes to Financial Statements
September 30, 2006 and 2005

(7) Property and Equipment

Property and equipment consist of the following at September 30, 2006 and 2005:

Development Corporation Division

	Estimated Useful Lives	Balance at October 1, 2005	Additions	Deletions	Balance at September 30, 2006
Structure and improvements	7 years	\$ 468,456	\$ 669	\$ -	\$ 469,125
Vehicles/office equipment	3 - 5 years	133,094	500	(29,300)	104,294
Computer equipment	3 - 5 years	128,265	1,330	-	129,595
Furniture and fixtures	7 years	<u>125,619</u>	<u>-</u>	<u>-</u>	<u>125,619</u>
		855,434	2,499	(29,300)	828,633
Less accumulated depreciation		<u>(758,519)</u>	<u>(65,984)</u>	<u>29,300</u>	<u>(795,203)</u>
		\$ <u>96,915</u>	\$ <u>(63,485)</u>	\$ <u>-</u>	\$ <u>33,430</u>
	Estimated Useful Lives	Balance at October 1, 2004	Additions	Deletions	Balance at September 30, 2005
Structure and improvements	7 years	\$ 468,456	\$ -	\$ -	\$ 468,456
Vehicles/office equipment	3 - 5 years	136,954	26,115	(29,975)	133,094
Computer equipment	3 - 5 years	128,265	-	-	128,265
Furniture and fixtures	7 years	<u>125,619</u>	<u>-</u>	<u>-</u>	<u>125,619</u>
		859,294	26,115	(29,975)	855,434
Less accumulated depreciation		<u>(687,091)</u>	<u>(101,398)</u>	<u>29,970</u>	<u>(758,519)</u>
		\$ <u>172,203</u>	\$ <u>(75,283)</u>	\$ <u>(5)</u>	\$ <u>96,915</u>

Northern Marianas Housing Corporation

	Estimated Useful Lives	Balance at October 1, 2005	Additions	Deletions	Balance at September 30, 2006
Residential Housing Development Projects:					
Section 8 Mihaville Housing	30 years	\$ 2,442,014	\$ 18,670	\$ -	\$ 2,460,684
Section 8 Koblerville Housing	30 years	1,921,397	5,251	-	1,926,648
Section 8 Rota Housing	30 years	1,170,178	6,044	-	1,176,222
Section 8 Tinian Housing	30 years	1,063,057	2,097	-	1,065,154
Section 8 Housing Phase II	30 years	635,229	-	-	635,229
Section 8 Housing Phase I	30 years	<u>600,515</u>	<u>-</u>	<u>-</u>	<u>600,515</u>
		7,832,390	32,062	-	7,864,452
Other:					
Koblerville infrastructure	30 years	2,214,991	-	-	2,214,991
Tinian infrastructure	30 years	608,500	-	-	608,500
Building and improvements	20 years	424,586	-	-	424,586
Equipment and computers	3 - 8 years	409,743	66,568	-	476,311
Vehicles	3 years	<u>144,196</u>	<u>-</u>	<u>(4,999)</u>	<u>139,197</u>
		3,802,016	66,568	(4,999)	3,863,585
		11,634,406	98,630	(4,999)	11,728,037
Less accumulated depreciation		<u>(8,857,501)</u>	<u>(613,180)</u>	<u>523,614</u>	<u>(8,947,067)</u>
		2,776,905	(514,550)	518,615	2,780,970
Koblerville Expansion Project Infrastructure to be transferred out to related party		<u>2,287,986</u>	<u>-</u>	<u>(2,287,986)</u>	<u>-</u>
		\$ <u>5,064,891</u>	\$ <u>(514,550)</u>	\$ <u>(1,769,371)</u>	\$ <u>2,780,970</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(7) Property and Equipment, Continued

Northern Marianas Housing Corporation, Continued

	Estimated Useful Lives	Balance at October 1, 2004	Additions	Deletions	Balance at September 30, 2005
Residential Housing Development Projects:					
Section 8 Mihaville Housing	30 years	\$ 2,435,785	\$ 6,229	\$ -	\$ 2,442,014
Section 8 Koblerville Housing	30 years	1,918,058	3,339	-	1,921,397
Section 8 Rota Housing	30 years	1,170,178	-	-	1,170,178
Section 8 Tinian Housing	30 years	1,060,845	2,212	-	1,063,057
Section 8 Housing Phase II	30 years	635,229	-	-	635,229
Section 8 Housing Phase I	30 years	600,515	-	-	600,515
		<u>7,820,610</u>	<u>11,780</u>	<u>-</u>	<u>7,832,390</u>
Other:					
Koblerville infrastructure	30 years	2,214,991	-	-	2,214,991
Tinian infrastructure	30 years	608,500	-	-	608,500
Building and improvements	20 years	424,586	-	-	424,586
Equipment and computers	3 - 8 years	340,334	69,409	-	409,743
Vehicles	3 years	77,394	80,977	(14,175)	144,196
		<u>3,665,805</u>	<u>150,386</u>	<u>(14,175)</u>	<u>3,802,016</u>
		11,486,415	162,166	(14,175)	11,634,406
Less accumulated depreciation		<u>(8,478,308)</u>	<u>(596,073)</u>	<u>216,880</u>	<u>(8,857,501)</u>
		3,008,107	(433,907)	202,705	2,776,905
Koblerville Expansion Project Infrastructure to be transferred out to related party		<u>2,287,986</u>	<u>-</u>	<u>-</u>	<u>2,287,986</u>
		<u>\$ 5,296,093</u>	<u>\$ (433,907)</u>	<u>\$ 202,705</u>	<u>\$ 5,064,891</u>

NMHC also holds title to approximately 339,000 square meters of land acquired at no cost which was originally held for development of low income rental housing or resale to low income families for construction of housing. The land is recorded on NMHC's financial statements at estimated fair value of \$10,409,682 at September 30, 2006 and 2005. Public Law 6-34 provides NMHC, subject to certain terms and conditions, the authority to lease for commercial development certain land situated in the North Garapan Subdivision Annex No. 2. NMHC is currently in the process of promoting the development of the abovementioned land to allow NMHC to meet its future commitments.

On February 12, 1999, a Memorandum of Agreement (MOA) was executed between NMHC and CUC whereby CUC agreed to reimburse NMHC for the costs associated with power, water and sewer facilities within the Koblerville Expansion Project (KEP) and NMHC to transfer the KEP infrastructure to CUC. On April 19, 2001, the MOA was amended whereby CUC will instead reimburse the CNMI Government for the related power, water and sewer costs. In January 2002, the project was completed. The infrastructure was transferred to CUC during the fiscal year ended September 30, 2006. The infrastructure had a carrying value of \$1,769,371 at the date of transfer.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(8) Asset Held for Sale

Pursuant to Public Law 11-57, NMHC shall have the duty to pay CDA approximately \$3,364,412 for the cost of constructing fifty-two housing units located at the Sugar King II. Repayment of the loan shall come from the sale of the fifty-two units at Sugar King Part II. As of September 30, 2006 and 2005, NMHC has sold forty-six units amounting to \$2,932,000. The remaining value of the units to be disposed is \$443,000 as of September 30, 2006 and 2005. As of September 30, 2006 and 2005, NMHC has remitted \$2,264,600 to CDA.

(9) Foreclosed Real Estate

A summary of the changes in foreclosed real estate and the related valuation allowance as of September 30, 2006 and 2005 is as follows:

	<u>Development Corporation Division</u>	<u>Northern Marianas Housing Corporation</u>	<u>2006</u>	<u>2005</u>
Foreclosed Real Estate				
Balance at beginning of year	\$ 2,056,300	\$ 654,053	\$ 2,710,353	\$ 795,238
Additions	1,426,500	379	1,426,879	2,087,115
Decline in market value	<u>(746,800)</u>	<u>-</u>	<u>(746,800)</u>	<u>(172,000)</u>
	2,736,000	654,432	3,390,432	2,710,353
Valuation allowance	<u>(1,368,000)</u>	<u>-</u>	<u>(1,368,000)</u>	<u>(1,028,150)</u>
Balance at end of year	\$ <u>1,368,000</u>	\$ <u>654,432</u>	\$ <u>2,022,432</u>	\$ <u>1,682,203</u>
Valuation Allowance				
Balance at beginning of year	\$ 1,028,150	\$ -	\$ 1,028,150	\$ 284,726
Recoveries	(574,800)	-	(574,800)	-
Provision	<u>914,650</u>	<u>-</u>	<u>914,650</u>	<u>743,424</u>
Balance at end of year	\$ <u>1,368,000</u>	\$ <u>-</u>	\$ <u>1,368,000</u>	\$ <u>1,028,150</u>

(10) Notes Payable to Related Party

Development Banking Division

Note payable at September 30, 2006 and 2005, is as follows:

	<u>2006</u>	<u>2005</u>
Note payable to Marianas Public Land Trust (MPLT), bearing interest at 6.5% per annum, due over a fifteen-year term, beginning June, 2003. The note is collateralized by the full faith and credit of the CNMI Government held in trust by MPLT, for the purpose of development and maintenance of the American Memorial Park, and is being repaid from earnings of the investments pursuant to CNMI Public Law 11-72.	\$ <u>1,712,943</u>	\$ <u>1,808,043</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(10) Notes Payable to Related Party, Continued

Development Banking Division, Continued

Principal maturities for subsequent fiscal years are as follows (estimated as repayments depend on earnings on the investments):

<u>Year ending September 30,</u>	<u>Principal Balance</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 107,457	\$ 107,952	\$ 215,409
2008	107,886	101,180	209,066
2009	115,111	93,955	209,066
2010	122,820	86,246	209,066
2011	131,046	78,020	209,066
2012 - 2016	799,236	246,093	1,045,329
2017 - 2018	<u>329,387</u>	<u>19,054</u>	<u>348,441</u>
	<u>\$ 1,712,943</u>	<u>\$ 732,500</u>	<u>\$ 2,445,443</u>

Northern Marianas Housing Corporation

Notes payable at September 30, 2006 and 2005, are as follows:

	<u>2006</u>	<u>2005</u>
Note payable to MPLT, bearing interest at 8.5% per annum, due on March 1, 2016, collateralized by the full faith and credit of the CNMI Government. CNMI Public Law 12-27 approved the repayment of the loan through legislative appropriation of operating transfers to the general fund of the CNMI Government from investment income of MPLT. Operating transfers to the general fund reduce NMHC's liability to MPLT. Repayment of the loan principal is deferred for a period of ten years.	\$ 8,996,623	\$ 8,996,623
Note payable to the CNMI Government for amounts paid to MPLT through operating transfers to the general fund of the CNMI Government from investment income of MPLT pursuant to the approved repayment of the MPLT loan through legislative appropriation as provided for in Public Law 12-27. Operating transfers in the general fund reduces NMHC's payable to MPLT but recognizes a payable to the CNMI Government, which loan principal is deferred for ten years.	-	<u>1,003,377</u>
	<u>\$ 8,996,623</u>	<u>\$ 10,000,000</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(10) Notes Payable to Related Party, Continued

Northern Marianas Housing Corporation, Continued

Principal maturities for subsequent fiscal years are as follows:

<u>Year ending September 30,</u>	<u>Principal Balance</u>	<u>Interest</u>	<u>Total</u>
2007	\$ -	\$ 764,713	\$ 764,713
2008	-	764,713	764,713
2009	-	764,713	764,713
2010	-	764,713	764,713
2011	-	764,713	764,713
2012 - 2016	<u>8,996,623</u>	<u>3,137,033</u>	<u>12,133,656</u>
	<u>\$ 8,996,623</u>	<u>\$ 6,960,598</u>	<u>\$ 15,957,221</u>

Changes in loans payable for the years ended September 30, 2006 and 2005, are as follows:

	<u>Balance October 1, 2005</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2006</u>	<u>Due Within One Year</u>
DBD	\$ 1,808,043	\$ -	\$ (95,100)	\$ 1,712,943	\$ 107,457
NMHC (MPLT)	8,996,623	-	-	8,996,623	-
NMHC (CNMI)	<u>1,003,377</u>	<u>-</u>	<u>(1,003,377)</u>	<u>-</u>	<u>-</u>
	<u>\$ 11,808,043</u>	<u>\$ -</u>	<u>\$ (1,098,477)</u>	<u>\$ 10,709,566</u>	<u>\$ 107,457</u>
	<u>Balance October 1, 2004</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2005</u>	<u>Due Within One Year</u>
DBD	\$ 1,898,165	\$ -	\$ (90,122)	\$ 1,808,043	\$ 102,465
NMHC (MPLT)	8,996,623	-	-	8,996,623	-
NMHC (CNMI)	<u>1,003,377</u>	<u>-</u>	<u>-</u>	<u>1,003,377</u>	<u>-</u>
	<u>\$ 11,898,165</u>	<u>\$ -</u>	<u>\$ (90,122)</u>	<u>\$ 11,808,043</u>	<u>\$ 102,465</u>

(11) Contributions to the CNMI

On July 26, 2006, CDA contributed \$4,000,000 to the CNMI Government pursuant to P.L. 15-1. P.L. 15-1 authorized the Governor reprogramming authority prior to the enactment of a comprehensive appropriations act for fiscal year 2006 and for other purposes. Further, P.L. 15-1 was enacted in order to avoid a fiscal crisis and deficit spending of the CNMI Government and to assist the CNMI administration in prioritizing needs until a comprehensive budget for fiscal year 2006 was enacted.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(12) Transfers for Capital Development Grants

As described in note 2, DBD receives and holds U.S. economic assistance provided in the Covenant. Terms and conditions of this assistance are contained in the *Agreement of the Special Representatives on Future United States Financial Assistance for the Northern Mariana Islands* (the Agreement). In accordance with the Agreement, DBD uses the proceeds, and accumulated earnings, by issuing either grants or loans to subrecipients, and acts in a pass through capacity. Revenues and expenditures related to grant agreements are recognized by the subrecipient with DBD recording expense under the caption "transfer out for capital development grants".

Transfers for capital development grants consist of transfers to the CNMI Office of the Governor for matching funds for grants from the U.S. Department of the Interior amounted to \$2,608,963 and \$1,359,489 for the years ended September 30, 2006 and 2005, respectively.

(13) Related Party Transactions

CDA maintains depository accounts in FDIC insured financial institutions. One of the Board members of CDA is currently the President Regional Manager of one of these financial institutions. CDA's deposits in this financial institution amounted to \$15,121,542 and \$23,963,885 as of September 30, 2006 and 2005, respectively. Management is of the opinion that transactions with this financial institution are of similar terms and conditions as with unrelated parties.

(14) Commitment and Contingencies

Commitment

Under a lease agreement beginning April 30, 2003 and expiring September 30, 2020, CDA leases office space in Saipan. The lease agreement provides for an annual rental of \$96,000 during the term of the lease. Also, CDA leases its office space in Tinian for an annual rental of \$8,400. The related lease agreement expires on May 31, 2007. Rental expense for these leases for each of the years ended September 30, 2006 and 2005 is \$104,400 and \$106,000, respectively.

Total minimum future rentals under these operating leases as of September 30, 2006 are as follows:

<u>Year ending</u> <u>September 30,</u>	
2007	\$ 101,600
2008	96,000
2009	96,000
2010	96,000
2011	96,000
2012 - 2016	480,000
2016 - 2020	<u>480,000</u>
	<u>\$ 1,445,600</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(14) Commitment and Contingencies, Continued

Contingencies

CDA is authorized to guarantee up to 90% of the principal of loans and lines of credit made by financial institutions to qualified borrowers, in addition to approving direct loans. The amounts for which CDA was contingently liable under this arrangement at September 30, 2006 and 2005, was \$7,478,517 and \$7,610,832, respectively.

NMHC has entered into an agreement with the U.S. Farmers Home Administration (FmHA) whereby NMHC assists borrowers in obtaining FmHA financing for housing construction. The agreement requires NMHC to guarantee any deficiency in foreclosure proceeds should borrowers default on the FmHA loans. As security under the agreement, NMHC is required to maintain an escrow account of \$286,436. Beginning September 30, 1993, the amount in the escrow account will be reduced each year by the product of \$1,500 multiplied by the number of loans paid in full for that particular year, or 4% of the total outstanding balance, whichever is less. As of September 30, 2006 and 2005, NMHC has guaranteed outstanding loans of approximately \$8,800,000 and \$9,400,000, respectively. As of September 30, 2006 and 2005, the balance in the escrow account was \$255,588 and \$254,313, respectively. These amounts are included in "restricted cash and cash equivalents" in the accompanying financial statements. As of September 30, 2006, the amount of defaulted loans related to the agreement was \$3,541,503. Of the total defaulted loans, the amount with demand notices from FmHA was \$616,127, for which NMHC recorded a liability included in "accounts payable and accrued expenses" in the accompanying financial statements. NMHC management cannot presently determine any additional liability on the remaining defaulted loans of \$2,925,376 and, accordingly, no provision for any liability or potential loss that may result from this matter has been recorded in the accompanying financial statements.

NMHC entered into a loan agreement and related loan purchase agreement with a savings and loan in the CNMI whereby the savings and loan will make available up to \$6,000,000 for housing loans. Under the agreements, NMHC is responsible for administering the loan purchase program and the savings and loan agrees to purchase qualified loans from NMHC. NMHC guarantees the first 25% of the principal balance plus interest on each loan sold to the savings and loan. As of September 30, 2006 and 2005, NMHC was contingently liable for \$1,664,779 and \$1,767,408, respectively, of the balance of loans purchased by the savings and loan. In addition, NMHC is required to maintain an account at the savings and loan equal to the lesser of 5% of all loans sold to the savings and loan or \$100,000. The balance in the account at September 30, 2006 and 2005 was \$93,172 and \$120,611, respectively, which is included in "restricted cash and cash equivalents" in the accompanying financial statements.

NMHC also has similar arrangements with other financial institutions whereby NMHC guarantees a varying percentage of loans issued by the banks for housing construction. At September 30, 2006 and 2005, NMHC was contingently liable to these institutions for \$3,064,200 and \$5,338,479, respectively. As of September 30, 2006, the total amount of defaulted loans with demand notices related to these arrangements was \$237,223. As of September 30, 2006, the amount was recorded by NMHC as a liability and was included in "accounts payable and accrued expenses" in the accompanying financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2006 and 2005

(15) Risk Management

CDA 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. CDA has elected to purchase commercial insurance from independent third parties for the risks of loss to which it is exposed. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

(16) Subsequent Events

On March 13, 2007, the Governor of the CNMI approved P.L. 15-48 to repeal and amend the restrictions and obligations imposed by Public Laws 10-29 and 12-27. Public Law 15-48 repeals the appropriation of MPLT's annual interest distribution to the CNMI against NMHC's loans with MPLT. In addition, Public Law 15-48 lifts the ten-year repayment moratorium on NMHC and requires NMHC to begin making loan payments to MPLT.

On December 31, 2007, NMHC and MPLT entered into a Settlement Agreement to compromise and settle all disputed issues and claims relating to the \$10 million note payable. Under the Agreement, NMHC agreed to assign to MPLT certain loans and mortgages in the NMHC owned loan portfolio. The total amount of the loan portfolio to be transferred is \$10,621,895 representing the portfolio balance at December 31, 2007 which is the effective date of the assignment. Under the Agreement, NMHC will pay MPLT the sum of \$2,025,000 upon execution of the Agreement. Further, NMHC will retain an amount of \$1,500,000 as additional consideration for its obligations under the Agreement. Additionally, there are several loans which NMHC issued with funds from MPLT and subsequently sold or transferred to certain CNMI banking institutions. Under the Agreement, MPLT will assume liability for repayment of these loans in an amount not to exceed \$1,672,102 in contingent liabilities for and on behalf of NMHC in the form of guarantees to certain financial institutions. As of September 30, 2006, the related notes payable to MPLT is classified as noncurrent in the accompanying financial statements.

On December 14, 2007, CDA entered into a sublease agreement for a portion of its office space in Saipan. The sublease is for a period of two years commencing from December 1, 2007 for an annual rental of \$24,000.

On January 25, 2008, CDA entered into a ground lease and option to purchase agreement for a foreclosed real estate property. The lease is for a period of twenty-five years for a total rental of \$569,000, which will be paid by lessee in monthly installments based on a payment schedule specified in the agreement. At any time during the twenty-five year term of the lease, upon and subject to payment by lessee of the full \$569,000 rental, the lessee is given the option to purchase the property at \$100.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements September 30, 2006 and 2005

(16) Subsequent Events, Continued

In June 2008, NMHC entered into an agreement with the USDA Rural Development (formerly the U.S. Farmers Home Administration or FmHA) to resolve defaulted USDA Rural Development loans. The agreement has been established to outline the steps and mutually agreed-upon terms in liquidating defaulted USDA Rural Development loans which NMHC agreed to act as Trustee, in accordance with D.L. 5-42 (the Act) on Deeds of Trust securing Rural Development housing loans in the CNMI. The agreement encompasses forty-eight seriously delinquent loans totaling \$3,126,371. This number may decline if any accounts cure before the auction dates. On June 5, 2008, NMHC's Board of Directors approved a Board resolution authorizing the expenditure of \$1,521,923 from NMHC's funds for the purpose of paying any amount due and payable to USDA Rural Development from NMHC pursuant to the terms and conditions of the agreement.

On October 15, 2008, in light of P.L. 15-48 and the settlement agreement entered into between NMHC and MPLT on December 31, 2007, the CNMI Government agreed that NMHC does not have a liability to the CNMI for NMHC loan payments withheld by MPLT from interest due to the CNMI. As of September 30, 2006, the related note and interest payable to CNMI is written-off in the accompanying financial statements.

(17) Restatement

During the year ended September 30, 2006, NMHC determined that it had incorrectly recorded HOME Investment Partnership Program loan disbursements as revenues. HOME grants disbursed as loans should have been recorded as deferred revenues and HOME program income should be recorded for repayments of principal and interest on loans made with HOME funds.

The accompanying 2005 basic financial statements have been restated to correct this error. The effect on the 2005 financial statements is as follows:

	2005 As Previously <u>Presented</u>	2005 <u>As Restated</u>
Deferred revenues	\$ -	\$ 1,876,315
Net assets - beginning	\$ 62,013,092	\$ 60,906,652
HOME Investment Partnership grants program income	\$ 753,414	\$ -
Interest and fees on loans	\$ 4,387,003	\$ 4,370,542

COMMONWEALTH DEVELOPMENT AUTHORITY

Combining Statement of Net Assets
September 30, 2006

ASSETS	Development Banking Division	Development Corporation Division	Component Unit	Elimination Entries	Total
			Northern Marianas Housing Corporation		
Current assets:					
Cash and cash equivalents	\$ -	\$ 1,223,952	\$ 488,482	\$ -	\$ 1,712,434
Time certificates of deposit	-	1,022,514	-	-	1,022,514
Receivables:					
Loans, net	-	2,798,260	480,261	-	3,278,521
Capital development loans from related parties, net	219,218	-	-	-	219,218
Rent, net	-	-	57,122	-	57,122
Accrued interest, net	105,451	18,629	356,197	-	480,277
Other	-	133,287	-	-	133,287
Prepaid expenses	-	16,783	-	-	16,783
Total current assets	324,669	5,213,425	1,382,062	-	6,920,156
Other assets:					
Cash and cash equivalents, restricted	1,386,187	961,990	5,211,517	-	7,559,694
Time certificates of deposit, restricted	7,181,915	4,842,412	-	-	12,024,327
Total other assets	8,568,102	5,804,402	5,211,517	-	19,584,021
Noncurrent assets:					
Loans receivable, net	-	8,427,848	10,638,936	-	19,066,784
Capital development loans receivable from related parties, net	2,077,613	-	-	-	2,077,613
Due from other funds	961,940	40,394	-	(1,002,334)	-
Property and equipment, net	-	33,430	2,780,970	-	2,814,400
Asset held for sale	-	-	443,000	-	443,000
Land	-	-	10,409,682	-	10,409,682
Foreclosed real estate	-	1,368,000	654,432	-	2,022,432
Total noncurrent assets	3,039,553	9,869,672	24,927,020	(1,002,334)	36,833,911
	\$ 11,932,324	\$ 20,887,499	\$ 31,520,599	\$ (1,002,334)	\$ 63,338,088
LIABILITIES AND NET ASSETS					
Current liabilities:					
Current installment of notes payable to related party	\$ 107,457	\$ -	\$ -	\$ -	\$ 107,457
Accounts payable and accrued expenses	-	301,424	1,783,791	-	2,085,215
Interest payable	-	-	1,162,317	-	1,162,317
Due to grantor agency	-	-	852,677	-	852,677
Deferred revenues	-	13,529	249,856	-	263,385
Total current liabilities	107,457	314,953	4,048,641	-	4,471,051
Deferred revenues, net of current portion	-	730,571	2,813,608	-	3,544,179
Notes payable to related party, net of current installments	1,605,486	-	8,996,623	-	10,602,109
Due to other funds	40,394	-	1,081,256	(1,121,650)	-
Total liabilities	1,753,337	1,045,524	16,940,128	(1,121,650)	18,617,339
Net assets:					
Invested in capital assets	-	1,401,430	14,288,084	-	15,689,514
Restricted	10,178,987	18,440,545	292,387	119,316	29,031,235
Total net assets	10,178,987	19,841,975	14,580,471	119,316	44,720,749
	\$ 11,932,324	\$ 20,887,499	\$ 31,520,599	\$ (1,002,334)	\$ 63,338,088

See Accompanying Independent Auditors' Report.

COMMONWEALTH DEVELOPMENT AUTHORITY

Combining Statement of Revenues, Expenses and Changes in Net Assets
Year Ended September 30, 2006

	Development Banking Division	Development Corporation Division	Component Unit Northern Marianas Housing Corporation	Elimination Entries	Total
Operating revenues:					
Interest and fees on loans	\$ 183,790	\$ 3,111,482	\$ 1,195,369	\$ -	\$ 4,490,641
Section 8 income:					
Federal housing assistance rentals	-	-	3,977,799	-	3,977,799
Tenant share	-	-	77,937	-	77,937
Interest on investments	287,193	285,290	-	-	572,483
HOME Investment Partnership					
Program grants	-	-	1,211,497	-	1,211,497
HOME Investment Partnership grants					
program income	-	-	119,276	-	119,276
CDBG Program Grant	-	-	765,393	-	765,393
ESG Program Grant	-	-	67,503	-	67,503
Housing rental	-	-	963	-	963
Other	-	119,104	66,807	(94,197)	91,714
	470,983	3,515,876	7,482,544	(94,197)	11,375,206
Recoveries (bad debts)	(119,317)	(4,746,223)	(6,892,390)	119,316	(11,638,614)
Net operating revenues	351,666	(1,230,347)	590,154	25,119	(263,408)
Operating expenses:					
Section 8 rental	-	-	2,471,599	-	2,471,599
HOME Investment Partnership					
Program grants	-	-	1,211,497	-	1,211,497
Salaries and wages	-	453,327	560,341	-	1,013,668
CDBG Program Grant	-	-	765,393	-	765,393
Depreciation	-	65,984	613,180	-	679,164
Provision for foreclosed real estate	-	914,650	-	-	914,650
Repairs and maintenance	-	-	512,660	-	512,660
Employee benefits	-	196,875	260,958	-	457,833
Professional fees	-	7,153	194,106	-	201,259
Office rent	-	122,733	5,273	-	128,006
Travel	-	48,061	45,198	-	93,259
ESG Program Grant	-	-	67,503	-	67,503
Other	153,261	297,421	606,703	(94,197)	963,188
Total operating expenses	153,261	2,106,204	7,314,411	(94,197)	9,479,679
Operating income (loss)	198,405	(3,336,551)	(6,724,257)	119,316	(9,743,087)
Nonoperating revenues (expenses):					
Write-off of note and interest payable to CNMI	-	-	4,174,042	-	4,174,042
Other income	208,495	-	41,210	-	249,705
Interest income	-	-	51,463	-	51,463
Write-off of due to/from other funds	6,695,556	(6,695,556)	-	-	-
Interest expense	(113,395)	-	(764,713)	-	(878,108)
Infrastructure transferred out to related party	-	-	(1,769,371)	-	(1,769,371)
Contributions to the CNMI	-	(4,000,000)	-	-	(4,000,000)
Total nonoperating revenues (expenses), net	6,790,656	(10,695,556)	1,732,631	-	(2,172,269)
Income (loss) before transfers	6,989,061	(14,032,107)	(4,991,626)	119,316	(11,915,356)
Transfers out for capital development grants	(2,608,963)	-	-	-	(2,608,963)
Change in net assets	4,380,098	(14,032,107)	(4,991,626)	119,316	(14,524,319)
Net assets - beginning, as restated	5,798,889	33,874,082	19,572,097	-	59,245,068
Net assets - ending	\$ 10,178,987	\$ 19,841,975	\$ 14,580,471	\$ 119,316	\$ 44,720,749

See Accompanying Independent Auditors' Report.

COMMONWEALTH DEVELOPMENT AUTHORITY

Combining Statement of Cash Flows
Year Ended September 30, 2006

	Development Banking Division	Development Corporation Division	Component Unit Northern Marianas Housing Corporation	Elimination Entries	Total
Cash flows from operating activities:					
Cash received from interest and fees on loans receivable	\$ -	\$ 992,657	\$ 868,987	\$ -	\$ 1,861,644
Cash received from interest and fees on capital development loans	182,986	-	-	-	182,986
Interest and dividends on investments	251,550	285,290	-	-	536,840
Cash payments to suppliers for goods and services	(153,261)	(684,163)	(485,684)	94,197	(1,228,911)
Cash received from customers	-	119,104	80,779	(94,197)	105,686
Cash payments to employees for services	-	(453,327)	(560,341)	-	(1,013,668)
Cash received from federal grant awards	-	-	6,056,034	-	6,056,034
Cash payments from federal grant awards	-	-	(5,094,152)	-	(5,094,152)
Net cash provided by operating activities	281,275	259,561	865,623	-	1,406,459
Cash flows from capital and related financing activities:					
Net interdivisional transactions	82,172	148,028	(230,200)	-	-
Acquisition of property and equipment	-	(2,499)	(98,630)	-	(101,129)
Contributions to the CNMI	-	(4,000,000)	-	-	(4,000,000)
Net disbursements of loans receivable	-	(459,828)	(334,336)	-	(794,164)
Payments received on capital development loans	637,366	-	-	-	637,366
Capital development grants	(2,608,963)	-	-	-	(2,608,963)
Net cash used for capital and related financing activities	(1,889,425)	(4,314,299)	(663,166)	-	(6,866,890)
Cash flows from investing activities:					
Net proceeds from (purchase of) restricted cash and cash equivalents	11,455	281,573	(2,219,261)	-	(1,926,233)
Net proceeds from time certificates of deposit	1,596,695	3,540,435	-	-	5,137,130
Interest income	-	-	51,463	-	51,463
Net cash provided by (used for) investing activities	1,608,150	3,822,008	(2,167,798)	-	3,262,360
Net decrease in cash and cash equivalents	-	(232,730)	(1,965,341)	-	(2,198,071)
Cash and cash equivalents at beginning of year	-	1,456,682	2,453,823	-	3,910,505
Cash and cash equivalents at end of year	\$ -	\$ 1,223,952	\$ 488,482	\$ -	\$ 1,712,434
Reconciliation of operating income (loss) to net cash provided by operating activities:					
Operating income (loss)	\$ 198,405	\$ (3,336,551)	\$ (6,724,257)	\$ 119,316	\$ (9,743,087)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:					
(Recoveries) bad debts	119,317	4,746,223	6,892,390	(119,316)	11,638,614
Provision for foreclosed real estate	-	914,650	-	-	914,650
Depreciation	-	65,984	613,180	-	679,164
(Increase) decrease in assets:					
Receivables:					
Rent	-	-	(64,928)	-	(64,928)
Other	-	(67,618)	-	-	(67,618)
Accrued interest	(36,447)	(2,051,207)	(326,382)	-	(2,414,036)
Prepaid expenses	-	(4,663)	-	-	(4,663)
Increase (decrease) in liabilities:					
Accounts payable and accrued expenses	-	(7,257)	561,054	-	553,797
Due to grantor agency	-	-	(85,434)	-	(85,434)
Net cash provided by operating activities	\$ 281,275	\$ 259,561	\$ 865,623	\$ -	\$ 1,406,459
Supplemental disclosure of noncash capital and related financing activities:					
Transfer of Koblerville Expansion Project:					
Noncash decrease in property and equipment	\$ -	\$ -	\$ 1,769,371	\$ -	\$ 1,769,371
Noncash increase in nonoperating expenses	-	-	(1,769,371)	-	(1,769,371)
	\$ -	\$ -	\$ -	\$ -	\$ -
Recognition of liability arising from defaulted loans guaranteed:					
Noncash increase in other assets	\$ -	\$ -	\$ 853,350	\$ -	\$ 853,350
Noncash increase in accounts payable and accrued expenses	-	-	(853,350)	-	(853,350)
	\$ -	\$ -	\$ -	\$ -	\$ -
Write-off of note and interest payable to CNMI:					
Noncash decrease in note payable	\$ -	\$ -	\$ (1,003,377)	\$ -	\$ (1,003,377)
Noncash decrease in interest payable	-	-	(3,170,665)	-	(3,170,665)
Noncash increase in operating revenues	-	-	4,174,042	-	4,174,042
	\$ -	\$ -	\$ -	\$ -	\$ -

See Accompanying Independent Auditors' Report.

COMMONWEALTH DEVELOPMENT AUTHORITY

Combined Schedule of Revenues, Expenses and Changes in Net Assets
- Budget and Actual
Year Ended September 30, 2006

	Budget	Actual	Variance
Operating revenues:			
Interest and fees on loans	\$ 4,189,822	\$ 4,490,641	\$ 300,819
Section 8 income:			
Federal housing assistance rentals	4,719,302	3,977,799	(741,503)
Tenant share	-	77,937	77,937
Interest on investments	572,483	572,483	-
HOME Investment Partnership Program grants	1,194,554	1,211,497	16,943
HOME Investment Partnership grants program income	119,276	119,276	-
CDBG Program Grant	810,970	765,393	(45,577)
ESG Program Grant	-	67,503	67,503
Housing rental	-	963	963
Other	119,104	185,911	66,807
Total operating revenues	<u>11,725,511</u>	<u>11,469,403</u>	<u>(256,108)</u>
Recoveries (bad debts)	-	(11,638,614)	(11,757,930)
Net operating revenues	<u>11,725,511</u>	<u>(169,211)</u>	<u>(12,014,038)</u>
Operating expenses:			
Section 8 rental	3,171,560	2,471,599	699,961
Salaries and wages	1,212,564	1,235,786	(23,222)
HOME Investment Partnership Program grants	1,104,568	1,104,568	-
Provision for foreclosed real estate	-	914,650	(914,650)
Depreciation	440,000	679,164	(239,164)
CDBG Program Grant	564,924	642,198	(77,274)
Repairs and maintenance	371,555	512,660	(141,105)
Employee benefits	589,503	457,833	131,670
Professional fees	250,650	201,259	49,391
Office rent	133,580	128,006	5,574
Travel	147,439	101,265	46,174
Capital outlay	72,210	101,129	(28,919)
ESG Program Grant	-	67,503	(67,503)
Contingent expenses	387,518	-	387,518
Other	962,112	1,057,385	(95,273)
Total operating expenses	<u>9,408,183</u>	<u>9,675,005</u>	<u>(266,822)</u>
Operating (loss) income	<u>2,317,328</u>	<u>(9,844,216)</u>	<u>(12,280,860)</u>
Nonoperating revenues (expenses):			
Write-off of note and interest payable to CNMI	-	4,174,042	4,174,042
Other income	-	249,705	249,705
Interest income	38,426	51,463	13,037
Interest expense	-	(878,108)	(878,108)
Infrastructure transferred out to related party	-	(1,769,371)	(1,769,371)
Contributions to the CNMI	-	(4,000,000)	(4,000,000)
Total nonoperating revenues (expenses), net	<u>38,426</u>	<u>(2,172,269)</u>	<u>(2,210,695)</u>
(Loss) income before contributions and transfers	<u>2,355,754</u>	<u>(12,016,485)</u>	<u>(14,491,555)</u>
Transfers out for capital development grants	-	(2,608,963)	(2,608,963)
Change in net assets	<u>2,355,754</u>	<u>(14,625,448)</u>	<u>(17,100,518)</u>
Net assets - beginning, as restated	-	59,245,068	59,245,068
Net assets - ending	<u>\$ 2,355,754</u>	<u>\$ 44,619,620</u>	<u>\$ 42,144,550</u>
The following reconciles budget to GAAP differences:			
Net assets at end of year, budgetary basis		\$ 44,619,620	
Capital outlay reported as expense for budget purposes		101,129	
Net assets at end of year, GAAP basis		<u>\$ 44,720,749</u>	

See Accompanying Independent Auditors' Report.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Revenues, Expenses and Changes in Net Assets - Budget and Actual
Year Ended September 30, 2006

	Development Banking Division			Development Corporation Division			Northern Marianas Housing Corporation		
	Budget	Actual	Variance	Budget	Actual	Variance	Budget	Actual	Variance
Operating revenues:									
Interest and fees on loans	\$ 183,790	\$ 183,790	\$ -	\$ 3,111,482	\$ 3,111,482	\$ -	\$ 894,550	\$ 1,195,369	\$ 300,819
Section 3 income:									
Federal housing assistance rentals	-	-	-	-	-	-	4,719,302	3,977,799	(741,503)
Tenant share	-	-	-	-	-	-	-	77,937	77,937
Interest on investments	287,193	287,193	-	285,290	285,290	-	-	-	-
HOME Investment Partnership Program grants	-	-	-	-	-	-	1,194,554	1,211,497	16,943
HOME Investment Partnership grants program income	-	-	-	-	-	-	119,276	119,276	-
CDBG Program Grant	-	-	-	-	-	-	810,970	765,393	(45,577)
ESG Program Grant	-	-	-	-	-	-	-	67,503	67,503
Housing rental	-	-	-	-	-	-	-	963	963
Other	-	-	-	119,104	119,104	-	-	66,807	66,807
Total operating revenues	470,983	470,983	-	3,515,876	3,515,876	-	7,738,652	7,482,544	(256,108)
Recoveries (bad debts)	-	(119,317)	(119,317)	-	(4,746,223)	(4,746,223)	-	(6,892,390)	(6,892,390)
Net operating revenues	470,983	351,666	(119,317)	3,515,876	(1,230,347)	(4,746,223)	7,738,652	590,154	(7,148,498)
Operating expenses:									
Section 3 rental	-	-	-	-	-	-	3,171,560	2,471,599	699,961
HOME Investment Partnership Program grants	-	-	-	-	-	-	1,104,568	1,104,568	-
Salaries and wages	-	-	-	430,436	453,327	(22,891)	782,128	782,459	(331)
CDBG Program Grant	-	-	-	-	-	-	564,924	642,198	(77,274)
Depreciation	-	-	-	-	65,984	(65,984)	440,000	613,180	(173,180)
Provision for foreclosed real estate	-	-	-	-	914,650	(914,650)	-	-	-
Repairs and maintenance	-	-	-	-	-	-	371,555	512,660	(141,105)
Employee benefits	-	-	-	239,344	196,875	42,469	350,159	260,958	89,201
Professional fees	-	-	-	87,500	7,153	80,347	163,150	194,106	(30,956)
Office rent	-	-	-	122,360	122,733	(373)	11,220	5,273	5,947
Travel	-	-	-	54,671	48,061	6,610	92,768	53,204	39,564
ESG Program Grant	-	-	-	-	-	-	-	67,503	(67,503)
Capital outlay	-	-	-	3,730	2,499	1,231	68,480	98,630	(30,150)
Contingent expenses	-	-	-	-	-	-	387,518	-	387,518
Other	58,572	153,261	(94,689)	194,492	297,421	(102,929)	709,048	606,703	102,345
Total operating expenses	58,572	153,261	(94,689)	1,132,533	2,108,703	(976,170)	8,217,078	7,413,041	804,037
Operating (loss) income	412,411	198,405	(214,006)	2,383,343	(3,339,050)	(5,722,393)	(478,426)	(6,822,887)	(6,344,461)
Nonoperating revenues (expenses):									
Write-off of note and interest payable to CNMI	-	-	-	-	-	-	-	4,174,042	4,174,042
Other income	-	208,495	208,495	-	-	-	-	41,210	41,210
Interest income	-	-	-	-	-	-	38,426	51,463	13,037
Write-off of due to/from other funds	-	6,695,556	6,695,556	-	(6,695,556)	(6,695,556)	-	-	-
Interest expense	-	(113,395)	(113,395)	-	-	-	-	(764,713)	(764,713)
Infrastructure transferred out to related party	-	-	-	-	-	-	-	(1,769,371)	(1,769,371)
Contributions to the CNMI	-	-	-	-	(4,000,000)	(4,000,000)	-	-	-
Total nonoperating revenues (expenses), net	-	6,790,656	6,790,656	-	(10,695,556)	(10,695,556)	38,426	1,732,631	1,694,205
(Loss) income before contributions and transfers	412,411	6,989,061	6,576,650	2,383,343	(14,034,606)	(16,417,949)	(440,000)	(5,090,256)	(4,650,256)
Transfers out for capital development grants	-	(2,608,963)	(2,608,963)	-	-	-	-	-	-
Change in net assets	412,411	4,380,098	3,967,687	2,383,343	(14,034,606)	(16,417,949)	(440,000)	(5,090,256)	(4,650,256)
Net assets - beginning, as restated	-	5,798,889	5,798,889	-	33,874,082	33,874,082	-	19,572,097	19,572,097
Net assets - ending	\$ 412,411	\$ 10,178,987	\$ 9,766,576	\$ 2,383,343	\$ 19,839,476	\$ 17,456,133	\$ (440,000)	\$ 14,481,841	\$ 14,921,841

See Accompanying Independent Auditors' Report.

COMMONWEALTH DEVELOPMENT AUTHORITY

INDEPENDENT AUDITORS' REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2006

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND COMPLIANCE AND OTHER MATTERS
BASED UPON THE AUDIT PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS

Board of Directors
Commonwealth Development Authority:

We have audited the financial statements of the Commonwealth Development Authority (CDA), as of and for the year ended September 30, 2006, and have issued our report thereon dated December 12, 2008. 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 CDA's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect CDA's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs (pages 8 through 23) as items 2006-1 through 2006-4.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable conditions described above to be material weaknesses. We also noted other matters involving the internal control over financial reporting that we have reported to management in a separate letter dated December 12, 2008.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether CDA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Questioned Costs as items 2006-5 and 2006-6.

This report is intended solely for the information and use of management, the Board of Directors, federal awarding agencies, pass-through entities, 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

December 12, 2008

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND
INTERNAL CONTROL OVER COMPLIANCE APPLICABLE
TO EACH MAJOR FEDERAL AWARD PROGRAM AND ON
THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Board of Directors
Commonwealth Development Authority:

Compliance

We have audited the compliance of the Commonwealth Development Authority (CDA) 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, 2006. CDA's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs (pages 8 through 23). Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of CDA's management. Our responsibility is to express an opinion on CDA'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 CDA'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 CDA's compliance with those requirements.

As described in items 2006-7 through 2006-10 in the accompanying Schedule of Findings and Questioned Costs, CDA did not comply with requirements regarding cash management, program income and special test and provisions related to U.S. Department of Housing and Urban Development programs that are applicable to its major programs. Compliance with such requirements is necessary, in our opinion, for CDA to comply with the requirements applicable to those programs.

In our opinion, except for the noncompliance described in the preceding paragraph, CDA complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2006.

Internal Control Over Compliance

The management of CDA 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 CDA's internal control over compliance with 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 and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect CDA's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grants. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 2006-7 through 2006-10.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 2006-8 and 2006-9 to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the basic financial statements of CDA as of and for the year ended September 30, 2006, and have issued our report thereon dated December 12, 2008. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards (page 5) 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. This schedule is the responsibility of the management of CDA. 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.

This report is intended for the information of the management, the Board of Directors, federal awarding agencies, pass-through entities, 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

December 12, 2008

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2006

Federal Grantor/ Program Title	Federal CFDA Number	Federal Cumulative Amount of Grant Award	Receivable (Deferred Revenue) from Grantor at October 1, 2005	Federal Funds Received in Fiscal Year 2006	Federal Funds Expended in Fiscal Year 2006	Receivable (Deferred Revenue) from Grantor at September 30, 2006
Direct Programs:						
U.S. Department of Housing and Urban Development /Section 8 Housing Choice Vouchers	14.871	\$ 6,644,871	\$ (952,909)	\$ 2,551,233	\$ 2,739,851	\$ (764,291)
U.S. Department of Housing and Urban Development /Lower Income Housing Assistance Program_Section 8 Moderate Rehabilitation	14.856	464,544	-	464,544	464,544	-
		262,558	-	262,558	262,558	-
		234,112	-	234,112	234,112	-
		182,843	-	182,843	182,843	-
Subtotal CFDA #14.856		1,144,057	-	1,144,057	1,144,057	-
U.S. Department of Housing and Urban Development/Community Development Block Grants/Special Purpose Grants/Insular Areas						
Garapan Water Quality Restoration	14.225	1,000,000	-	34,673	34,673	-
Koblerville Sports Complex	14.225	200,000	-	25,495	25,495	-
Rota Pathway	14.225	350,000	-	166,244	166,244	-
Susupe Track and Field	14.225	250,000	-	9,905	9,905	-
Susupe Baseball Park Bleachers	14.225	165,000	-	157,442	157,442	-
Tinian Shelter	14.225	300,000	-	135,220	135,220	-
Living Transitional Model Homes	14.225	1,235,000	-	35,945	35,945	-
Administrative Fee	14.225	976,436	-	200,469	200,469	-
Subtotal CFDA #14.225		4,476,436	-	765,393	765,393	-
U.S. Department of Housing and Urban Development /Emergency Shelter Grants Program	14.231	285,785	14,798	74,062	67,503	8,239
U.S. Department of Housing and Urban Development /HOME Investment Partnerships Program	14.239	479,038	-	106,929	106,929	-
	14.239	164,922	-	164,922	119,276	(45,646)
	14.239	2,714,552	-	1,104,568	1,104,568	-
Subtotal CFDA #14.239		3,358,512	-	1,376,419	1,330,773	(45,646)
		\$ 15,909,661	\$ (938,111)	\$ 5,911,164	\$ 6,047,577	\$ (801,698)
Reconciliation of expenditures to Statement of Revenues, Expenses and Changes in Net Assets:						
Federal award expenditures per above:						
U.S. Department of Housing and Urban Development /Section 8 Housing Choice Vouchers					\$ 2,739,851	
U.S. Department of Housing and Urban Development /Lower Income Housing Assistance Program_Section 8 Moderate Rehabilitation					1,144,057	
					\$ 3,883,908	
Federal award expenditures per Statement of Revenues, Expenses and Changes in Net Assets:						
U.S. Department of Housing and Urban Development /Section 8 Housing Choice Vouchers:						
Section 8 rental					\$ 2,471,599	
Salaries and wages					114,425	
Other					153,827	
					2,739,851	
U.S. Department of Housing and Urban Development /Lower Income Housing Assistance Program_Section 8 Moderate Rehabilitation:						
Salaries and wages					217,095	
Employee benefits					101,292	
Professional fees					98,187	
Repairs and maintenance					512,660	
Office rent					5,273	
Other					209,550	
					1,144,057	
					\$ 3,883,908	

See accompanying notes to schedule of expenditures of federal awards.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Schedule of Expenditures of Federal Awards Year Ended September 30, 2006

(1) Scope of Review

The Commonwealth Development Authority (CDA) was created as an autonomous public agency of the Commonwealth of the Northern Mariana Islands (CNMI) pursuant to Public Law 4-49 as amended by Public Law 4-63 and 5-27. CDA's existence is to be perpetual and it shall have all the rights and privileges of a corporation. The purpose of CDA is to stimulate the economic development of the CNMI. The Northern Marianas Housing Corporation (NMHC), a component unit and subsidiary corporation of CDA, was established under Public Law 5-37 as amended by Public Law 5-67. The purpose of NMHC is to develop and administer low cost residential housing in the CNMI. All significant operations of CDA and NMHC are included in the scope of the OMB Circular A-133 audit (the "Single Audit"). The U.S. Department of the Interior has been designated as CDA's cognizant agency for 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 allotment or grant award received. Disbursements made to subrecipients related to grant agreements are reported as expenditures. Disbursements made to subrecipients related to loan agreements are reported within applicable loan portfolios, and are subject to the Single Audit.

b. Subgrantees

Certain program funds are passed through CDA to subgrantee organizations. The Schedule of Expenditures of Federal Awards does not contain separate schedules disclosing how the subgrantees outside of CDA's control utilized the funds.

c. Funds Received

U.S. Department of HUD - Community Development Block Grants/Special Purpose Grants/Insular Areas/HOME Investment Partnerships Program/Emergency Shelter Grants Program - NMHC received these funds in a direct capacity in fiscal year 2006 and administers the funds and is responsible for ensuring compliance with laws and regulations.

U.S. Department of HUD - Lower Income Housing Assistance Program Section 8 Moderate Rehabilitation/Section 8 Housing Choice Vouchers - NMHC records federal rental assistance as Section 8 income. Program requirements do not entail the reporting of expenditures except for project No. TQ10-0016-004, Koblerville.

d. Indirect Cost Allocation

CDA does not receive an indirect cost allocation.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Schedule of Expenditures of Federal Awards, Continued Year Ended September 30, 2006

(3) Loan Funds

a. Development Banking Division

The Development Banking Division of CDA represents the revolving fund required 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. These funds will be used for financing additional revenue-producing capital development projects. During the year ended September 30, 2006, such funds amounting to \$2,608,963 were transferred out as capital development grants to CNMI Office of the Governor for matching funds for grants from the U.S. Department of the Interior. As of September 30, 2006, \$6,542,421 (net of the allowance for doubtful accounts of \$61,913,510) of loans made out of this revolving fund were outstanding.

b. Development Corporation Division

The Development Corporation Division (DCD) of CDA represents the revolving fund established to account for funds received by the former Northern Mariana Islands Economic Development Loan Fund pursuant to Section 702(c) of the Covenant from February 15, 1975 through September 30, 1985. In addition to the aforementioned financial resources, DCD has been designated as the administrative agency for economic development loans transferred from the Trust Territory of the Pacific Islands government to the CNMI. DCD also served as an intermediary lender for part of the year, for the SBA Microloan Program and obtained loans from SBA and used the loan funds to issue short-term microloans to qualified newly established and growing small business concerns in the CNMI. As of September 30, 2006, \$11,226,108 (net of the allowance for doubtful accounts of \$21,705,993) of loans made out of this revolving fund were outstanding.

c. Northern Marianas Housing Corporation

The Northern Marianas Housing Corporation (formerly the Mariana Islands Housing Authority (MIHA)) received economic development loan funds from the former Northern Mariana Islands Economic Development Loan Fund pursuant to a Memorandum of Understanding transferring funds received under Section 702(c) of the Covenant to MIHA. These funds are used for a revolving fund for a special program of low interest housing loans for low-income families. As of September 30, 2006, \$2,708,844 (net of the related allowance for doubtful accounts of \$1,585,497 and out of total NMHC net loans receivable of \$11,119,197) of loans made out of this revolving fund were outstanding.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs
Year Ended September 30, 2006

Section I - Summary of Auditor's Results

1. The Independent Auditors' Report on the financial statements expressed an unqualified opinion.
2. Reportable conditions in internal control over financial reporting were identified, which are considered to be material weaknesses.
3. Instances of noncompliance considered material to the financial statements were disclosed by the audit.
4. Reportable conditions in internal control over compliance with requirements applicable to major federal awards programs were identified, two of which are considered to be material weaknesses.
5. The Independent Auditors' Report on compliance with requirements applicable to major federal award programs expressed a qualified opinion.
6. The audit disclosed findings required to be reported by OMB Circular A-133.
7. CDA's major programs were as follows:

<u>Name of Federal Program or Cluster</u>	<u>CFDA Number</u>
U.S. Department of Housing and Urban Development:	
Community Development Block Grants/Special Purpose Grants/Insular Areas	14.225
HOME Investment Partnerships Program	14.239
Lower Income Housing Assistance Program_Section 8Moderate Rehabilitation	14.856

8. A threshold of \$300,000 was used to distinguish between Type A and Type B programs as those terms are defined in OMB Circular A-133.
9. CDA did not qualify as a low-risk audit as that term is defined in OMB Circular A-133.

Section II - Financial Statement Findings

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>	<u>Refer Page #</u>
2006-1	DCD Loans Receivable	\$ -	9 - 13
2006-2	NMHC Loans Receivable	\$ -	14
2006-3	NMHC Land	\$ -	15
2006-4	NMHC Loan Guarantee Agreements	\$ -	16
2006-5	Local Noncompliance	\$ -	17
2006-6	Local Noncompliance	\$ -	18

Section III - Federal Award Findings and Questioned Costs

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>	<u>Refer Page #</u>
2006-7	Cash Management	\$ -	19 - 20
2006-8	Program Income	\$ -	21
2006-9 - 10	Special Tests and Provisions	\$ -	22 - 23

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Section II - Financial Statement Findings

DCD Loans Receivable

Finding No. 2006-1

Criteria: An effective system of internal control includes procedures to ensure that loan payments are received on a timely basis. Further, all receivables should be assessed and monitored for collectability. Balances deemed not collectible should be adequately allowed for. Additionally, calculation of allowance for loan losses and other related receivables should be regularly reviewed for accuracy, completeness and reasonableness. Further, for restructured loans, the allowance should be determined in the same manner as prior to the restructuring until a sufficient time has passed that the borrower can meet the revised debt service requirements.

Condition: Our tests of DCD's loans receivable noted the following:

- An analysis of DCD's past due loans was performed to determine the propriety of the allowance for doubtful loans as of September 30, 2006. This analysis revealed that as of September 30, 2006, one hundred fifty-three loans (75% of the two hundred five total loans outstanding) were six months or more in arrears. At September 30, 2005, one hundred seventy-two loans (85% of the two hundred three total loans outstanding) were six months or more in arrears. Accrued interest on loans has increased from \$13,140,752 at September 30, 2005 to \$15,191,959 as of September 30, 2006. As such, the collateral for these loans is decreasing as a percentage of the total loan and interest portfolio.
- We were not provided the revised agreement for one loan (# CD 70248), the authorization that payments are to be applied to principal first instead of interest for one loan (# AD 20791), the current year correspondence or legal action taken for six delinquent loans (#s AD 20283, CD 31222, CD 33194, RE 70158, RE 70151 and CD 32892), a copy of Civil Action 05-0562D to determine the status of three loans (#s AD 70026, AD 70027 and CD 70029) and loan files for two loans (#s RE 70166 and RE 40294). Further, we noted that approximately \$45,500 in interest income recognized for one loan (# AD 20283) relates to prior years.
- For restructured loans, CDA's loan system will age outstanding balances based on revised due dates. Further, we noted seven loans, which are matured, or twelve months in arrears but were classified as less than six months in arrears as they were restructured and the due dates were revised. As a result, the calculation of the related allowance was based on incorrect rates.

Cause: The cause of the above condition is the increase in past due loans.

Effect: The effect of the above condition is an increased possibility of loan losses due to non-payment by borrowers.

Recommendation: We recommend that follow-up procedures on past due loans be adhered to. We recommend that evaluations be performed on these loans and a corrective plan be developed and documented. Future results may be compared against this plan and actions taken by management as deemed necessary. Legal action should be considered for those loans, which are considered unlikely to be serviceable by the borrower. In addition, we recommend that all loan files, related memos and correspondences be maintained and interest income be recognized in the proper period. We further recommend CDA review the aging of restructured loans.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Finding No. 2006-1, Continued

Prior Year Status: Past due loans was reported as a finding in the Single Audits of CDA for fiscal years 1994 through 2005.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Oscar C. Camacho, CDA Acting Chief Executive Officer

Corrective Action: This response is a departure from previous cut and paste repeatedly general responses on the findings on the loans receivables. In past responses, there was the understanding that the loan department was to embark on certain actions addressing the findings which included aggressive loan collections, loan workout arrangements, revisions and amendments to the rules and regulations to allow for certain strategies to address delinquencies. As of October 2006, CDA had adopted a Strategic Mission Plan which became the working document on which to address the identified deficiencies. The Board had adopted a debt relief program and of which only recently has passed legal muster, thus allowing for a realistic approach on working with clients. The program has the following features: interest rates are to be reduced to as low as two percent (2%); terms are to be extended out to an additional thirty (30) years for purposes of amortization only with mandated three (3) years callable (balloon payment) provisions where warranted and justified; and the accrued interests will be deferred and set aside and will not be capitalized. The current principal balance will remain as is where the two percent (2%) will be applied.

The following responses are directed to correct or address the individual and specific account audit findings:

- Loan # CD 70248: The most recent revision was done on September 29, 2006.
- Loan # AD 20791: The Acting Executive Director instructed the Financial Administrator of the Accounting Department to allocate the rental payments received to the principal first instead of interest. The rationale behind this determination stems from the "stipulation Re: Settlement Between CDA and DLNR/Order" dated August 15, 1997. The stipulation acknowledges the assignment to CDA of the property Management Agreement between the Saipan Farmers Market (SFM) and the Department of Lands and Natural Resources (DLNR). The stipulation allows CDA to lease the building out to enable SFM to retire its debt as quickly as possible and until such time that the debt is fully paid. Once paid, the property reverts back to DLNR. Furthermore, the Board of Directors of CDA in its meeting on August 7, 2005, sanctioned DCD's recommendations on the application of proceeds on the sale of assets as noted which in essence is very similar to the SFM condition. Given the conditions of this loan and the circumstances surrounding its resolution, the Acting Executive Director determined that such application is in the best interest of CDA since SFM is no longer in existence and cannot service the loan and as such, there could not be a loan to a none entity. CDA manages the property via a rental arrangement with Car Quest and thus, has determined that the principal portion of the loan should be sought out first.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Finding No. 2006-1, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

- Loan # 20283: A Supreme Court judgment order was obtained on January 24, 2003. Legal Counsel is sorting out via the court order the lot delineation. A 2,000 square meter lot has been identified. A copy of the court order was provided. In regards to the interest income of \$45,500 recognized, which relates to prior years, the best response we can provide is that this loan was accruing a five percent (5%) interest rate prior to it being reclassified as a judgment loan and was adjusted to the required court ordered nine percent (9%) interest rate.
- Loan # 31222: A Deed in Lieu of Foreclosure (DILOF) Agreement was entered into on December 14, 2006. Along with the DILOF agreement, CDA wrote-off all other outstanding balances. A total of \$522,000 constituted "valid and sufficient consideration for the conveyance of the mortgaged property to CDA". With this agreement, CDA became the owner of approximately over 9,000 square meters of improved real estate in the Chalan Kiya area. The property has recently been rented out on a monthly arrangement on a 15-year lease.
- Loan # 33194: There has not been any formal response from the client to our communication as to CDA's offer for a loan workout arrangement via the debt relief program.
- Loan # 70158: An oral request to consolidate the loans has been communicated to the Loan Manager. This matter has been brought up to the Board and instruction was to obtain a written and formal request from the borrower. To date there has not been any submission from the borrower.
- Loan # 70151: There have been ongoing discussions with the client to avail of the debt relief program.

No legal actions have commenced on any of the last three loans above albeit are warranted. All borrowers are given monthly statements of their respective loan accounts along with monthly payment coupons showing arrearages and what amounts are needed to bring the loans current. Follow-ups are scheduled to move forward with the objectives of the debt relief program.

- Loan #s 70026, 70027 and 70029: A copy of the CDA/DCD Legal Counsel Reports on Calvo's Development, Inc. is enclosed. The filed complaint is available. To satisfy the auditor's concern, this page of the litigation report should suffice to disclose the status of the litigation.
- The files for loan #s 70166 and 40294 are and were available. I apologize that I was not made aware that files were not provided to the auditors. On loan # 70166, the debt relief program is being worked on. With loan # 40294, the loan has been reduced to judgment; however, the client has appealed to the Supreme Court.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Finding No. 2006-1, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

The auditor's analysis on the number of DCD past due loans shows an improvement over previous years. At September 30, 2006, 75% of total outstanding loans were six months or more in arrears while the previous year's rate was at 85%. However, between 2004 and 2005, the rate was at 61%. The change in accrued interest increases between the years 2006, 2005 and 2004 showed relatively the same rate at 16%. The objective of the debt relief program is to arrest this increase to an acceptable rate of 5 to 7% while aggressively collecting on the delinquent accounts. However, our primary objective is to reduce the delinquency thru this debt relief program while protecting CDA's interests in the collaterals posted to secure these accounts. CDA recognizes that the collateral values relative to the size of the loan accounts have been diminished or reduced due to mounting accrued interests and will not improve if objectives mentioned above are not met.

The concern on recently restructured loans versus related allowances incorrectly allocated, the debt relief program anticipates the following plan:

- A new bank or classification will be created and dedicated only to accounts under the debt relief program. Under this bank, the arrested accrued interests will be identified and will be presented to the Board to be written-off. A Rights to Possession Agreement as prelude to either a DILOF or actual judicial foreclosure proceeding will be a requisite to this debt relief. This agreement entitles CDA to take possession and control of the RE collaterals and business operations while foreclosure proceedings or a DILOF are pursued.
- Should borrowers adhere to the program, then there will be no need to foreclose and the loan will continue to be serviced until conditions improve. At such time that principal portions are substantially reduced and the loan becomes manageable and serviceable at higher interest rates, then CDA may negotiate to increase interest rates come the third year when the loan is due in its entirety in the form of a balloon payment. Should conditions remain, the same terms may be extended for another three years with the same amortization schedules.
- All CDA borrowers, except those reduced to judgment orders, are given this opportunity but not all will qualify since individual conditions and requirements are different. The goal of this plan is to increase cash collections by enticing delinquent borrowers to realize that there is still hope in escaping foreclosures and losing their prized collaterals.

Item # 2 Allowance For Loan Losses (DBD Receivable From NMHC)

Communication from the Financial Administrator is enclosed requesting for guidance as to language of Public Law (PL) 11-57 with respect to the accrual of interests on the remaining balance after the authorized and agreed write-off. Assessment as to the question at hand has to consider the Mariana Islands Authority - Commonwealth Development Authority Agreement and the PL 11-57 together to be able to respond appropriately. A review of the Agreement and the language of PL 11-57 reveal that interest of 1% above the Bank of America Reference Rate as announced publicly from time to time shall be interest rate assessed on the outstanding loan amount.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Finding No. 2006-1, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

Item # 2 Allowance For Loan Losses (DBD Receivable From NMHC), Continued

According to records, the reference rate has never been adjusted to reflect any changes as called forth in the agreement and as such, the interest rate has remained at the 7.5% since 1989. Because we cannot tell whether there was any action to maintain the rate at 7.5% and since there is no record of any objection, this response to the auditor shall be the controlling determination until such time that the matter is addressed appropriately. Interest shall continue to accrue at the 7.5% rate on the outstanding balance of \$3,364,412 and of which has been reduced to \$1,027,211. The treatment on interest allowance is to be reversed as stated in the Financial Administrator's Memorandum to the Acting CEO.

Proposed Completion Date: Fiscal year 2007

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

NMHC Loans Receivable

Finding No. 2006-2

Criteria: An effective system of internal control includes procedures to ensure that loan payments are received on a timely basis. Further, all receivables should be assessed and monitored for collectability. Balances deemed not collectible should be adequately allowed for. Additionally, calculation of allowance for loan losses and other related receivables should be regularly reviewed for accuracy, completeness and reasonableness.

Condition: Our tests of NMHC's loans receivable noted the following:

- An analysis of allowance for delinquent loans noted a significant increase of delinquent loans over ninety days. The delinquency report as of September 30, 2006 includes at least eighty-one borrowers who are seriously in default for more than two years (more than seven hundred thirty days). NMHC's position is that the loans are collateralized by real properties, which they can resell in the event of foreclosure. However, considering current economic conditions, NMHC should consider whether the fair market values of these properties are sufficient to cover the outstanding loan balances.
- NMHC has existing loan agreements and related loan purchase agreements with certain financial institutions. As of September 30, 2006, loan guarantees relating to these agreements amounted to approximately \$17,600,000 of which approximately \$1,300,000 is more than one hundred twenty days overdue. Further, \$853,350 of defaulted loans guaranteed was demanded from NMHC at September 30, 2006. An audit adjustment was proposed to record a reserve of \$853,350.

Cause: The cause of the above condition is the increase in past due loans.

Effect: The effect of the above condition is an increased possibility of loan losses due to non-payment by borrowers.

Recommendation: We recommend NMHC continue performing a detailed review of the adequacy of its reserve for seriously defaulted loans. We further recommend NMHC review guaranteed loans with these financial institutions and assess the need to provide additional reserve for defaulted loans.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Joshua T. Sasamoto, NMHC Corporate Director

Corrective Action: NMHC will perform a detailed review of the adequacy of its reserve for seriously defaulted loans and guaranteed loans with these financial institutions and assess the need to provide additional reserves for defaulted loans which is based on the appraisal value of the property.

Proposed Completion Date: Fiscal year 2007

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

NMHC Land

Finding No. 2006-3

Criteria: Long-lived assets should be reported at the lower of carrying amount or fair value. A review of the valuations of real properties should be periodically performed by management and adjustments should be made to reflect real estate at the lower of the carrying amount or fair market value.

Condition: As of September 30, 2006, NMHC has recorded land consisting of several lots with recorded values of \$10,409,602. These properties were appraised during fiscal year 2003. There were no appraisals obtained since then except for two lots with recorded values of \$256,000 as of September 30, 2006. Based on an independent appraisal obtained in November 2007 for the two lots, the appraised values amounted to \$172,000 which is an \$84,000 decline in the recorded value. A review of the valuation of the remaining lots amounting to \$10,153,682 was not performed by management.

Cause: The cause of the above condition is the lack of established policies and procedures of periodic review of recorded values of real properties and the high cost of obtaining appraisal services.

Effect: The effect of the above condition is the potential misstatement of the land account.

Recommendation: We recommend NMHC ensure that long-lived assets are reported at the lower of carrying amount or fair value. Additionally, we recommend NMHC establish policies and procedures to periodically evaluate recorded and fair value of long-lived assets.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Jesse S. Palacios, NMHC Manager, Mortgage Credit Division

Corrective Action: NMHC will take corrective measures to ensure that long-lived assets are reported at the lower of carrying amount or fair values. To determine the fair market value of these assets, NMHC will publish an RFP for the performance of an appraisal of each individual long-lived asset. The entities submitting the proposals must be licensed by the CNMI Board of Professional Licensing. The winning entity will then be contracted to perform the appraisals to determine each asset's fair market value. This process will be repeated every other year so that the most current fair market value is readily available.

Proposed Completion Date: From RFP announcement in the newspapers to selection of winning entity to the completion of appraisal reports, NMHC proposes a completion date of February 27, 2009.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

NMHC Loan Guarantee Agreements

Finding No. 2006-4

Criteria: An effective system of internal control includes procedures to ensure that contingent liabilities are assessed and reviewed for probable losses.

Condition: NMHC has existing loan guarantee agreements and related loan purchase agreements with certain financial institutions. As of September 30, 2006, NMHC's loan guarantees relating to these agreements amounted to \$13,528,979. Of the total guaranteed amount, NMHC has received demand notices to pay for past due loans amounting to \$853,350. NMHC has recorded a reserve for loan guaranty for the \$853,350. However, NMHC has not performed an analysis of whether an additional reserve should be established for remaining defaulted loans of \$2,925,376.

Cause: The cause of the above condition is the lack of established policies and procedures in assessing and reviewing the adequacy of the reserve for guaranteed loans and the lack of relevant and sufficient information from financial institutions to estimate probable losses.

Effect: The effect of the above condition is the possible misstatement of the reserve for loan guaranty and related accounts.

Recommendation: We recommend NMHC ensure that the reserve for guaranteed loans is assessed and reviewed for adequacy. Further, we recommend NMHC establish policies and procedures in assessing the adequacy of the reserve for guaranteed loans, both past due and current. Additionally, we recommend NMHC continue to obtain sufficient information from those financial institutions about the status of defaulted loans and determine which of the defaulted loans will likely result in being paid or settled by NMHC.

Auditee Response and Corrective Action Plan:

Name of Contact Persons: Roger A. Dris, NMHC Chief Accountant and Jesse S. Palacios, NMHC Manager, Mortgage Credit Division

Corrective Action: NMHC will ensure that reserve for guaranteed loans is assessed and reviewed for adequacy. NMHC will establish policies and procedures to obtain an appraisal once every two years. The Accounting and Loan Divisions of NMHC will coordinate to obtain an appraisal once every two years.

NMHC will review the existing agreements with banking institutions to determine if the reserve requirements are adequate. In addition, the MCD and FD will work closely to assess and review potential loan losses by taking into account changes in local economic and business conditions as well as future developments. MCD will also continue to monitor the delinquency reports provided by the banks so that we can contact those borrowers who are on the list, especially, those who are on the 60-day and above delinquency categories in order to prevent banks from debiting our guarantee accounts or to discourage the banks from calling on the loans.

Proposed Completion Date: Beginning of FY 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Local Noncompliance

Finding No. 2006-5

Criteria: Grants and contributions provided to grantees should be properly monitored to ensure funds are used in accordance with established agreements and for authorized purposes.

Condition: On July 26, 2006, CDA contributed \$4,000,000 from DCD's local funds to the CNMI Government pursuant to Public Law (P.L.) 15-1. P.L. 15-1 authorized the Governor reprogramming authority prior to the enactment of a comprehensive appropriations act for fiscal year 2006 and for other purposes. The letter that accompanied the transmittal of funds indicated that the \$4,000,000 could not be used for operating purposes. We were unable to determine whether CDA was monitoring the use of these funds.

Cause: The cause of the above condition is the fiscal crisis and deficit spending of the CNMI Government.

Effect: The effect of the above condition is that the CNMI Government is potentially using the funds for unauthorized purposes.

Recommendation: We recommend CDA determine whether the funds have been used for authorized purposes.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Oscar C. Camacho, CDA Acting Chief Executive Officer

Corrective Action: CDA will review the use of the local funds disbursed.

Proposed Completion Date: Fiscal year 2008

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Local Noncompliance

Finding No. 2006-6

Criteria: Public Law (P.L.) 12-27 and the loan agreement with the Marianas Public Land Trust (MPLT) specifically restrict the use of the \$10,000,000 loan and any interest earned for future housing loans.

Condition: Interest earned from housing loans funded by the \$10,000,000 loan from MPLT was included in NMHC's operations budget and expended for operations.

Cause: The cause of the above condition is the lack of control to ensure interest earned from housing loans funded by the \$10,000,000 loan from MPLT are strictly used for future housing loans.

Effect: The effect of the above condition is noncompliance with P.L. 12-27 and the loan agreement with MPLT.

Recommendation: We recommend NMHC ensure strict compliance with Public Law 12-27 and the loan agreement with MPLT.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Joshua T. Sasamoto, NMHC Corporate Director

Corrective Action: NMHC will ensure strict compliance with Public Law 12-27 and the loan agreement with MPLT. NMHC and its legal counsel are in the process of resolving the issues with MPLT's legal counsel.

Proposed Completion Date: Fiscal year 2007

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Section III - Federal Award Findings and Questioned Costs

U.S. Department of Housing and Urban Development
Cash Management - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M (01 to 05)-ST-69-0001
Federal Award Period October 1, 2001 - 2005 to September 30, 2006 - 2010

Finding No. 2006-7

Criteria: The terms stipulated in the Cash Management Improvement Act Agreement (CMIAA) between the CNMI and the U.S. Department of the Treasury should be followed by the CNMI and its component units. Additionally, the CMIAA states that the grantee shall be liable for interest on federal funds from the date federal funds are credited to the grantee's account until those funds are paid out for program purposes. Further, CFR Title 24 Part 92.502 (C) (2) states that HOME funds drawn from the United States Treasury account must be expended for eligible costs within fifteen (15) days. Any interest earned within the 15 day period may be retained by the participating jurisdiction as HOME funds. Any funds that are drawn down and not expended for eligible costs within 15 days of the disbursement must be returned to HUD for deposit in the participating jurisdiction's United States Treasury account of the HOME Investment Trust Fund. Interest earned after 15 days belongs to the United States and must be remitted promptly, but at least quarterly, to HUD, except that a local participating jurisdiction may retain interest amounts up to \$100 per year for administrative expenses.

Condition: For seventeen of one hundred nine disbursements tested, NMHC made payments from fifteen to fifty-four days after they received the drawdown reimbursement as follows:

<u>Check #</u>	<u>Amount</u>	<u>Clearing Date</u>	<u>Receipt Date</u>	<u>Days Elapsed</u>
19685	\$ 6,016	11/30/05	11/10/05	20
19686	\$ 3,008	11/30/05	11/10/05	20
19687	\$ 4,775	01/03/06	11/10/08	54
20002	\$ 4,725	01/11/06	12/13/05	29
20003	\$ 3,150	01/11/06	12/13/05	29
20027	\$ 3,500	01/11/06	12/20/05	22
20042	\$ 6,750	01/17/06	12/22/05	26
20498	\$ 2,420	03/03/06	02/16/06	15
20514	\$ 3,371	03/27/06	02/21/06	34
20519	\$ 13,689	03/27/06	02/21/06	34
20521	\$ 7,738	03/27/06	02/21/06	34
20637	\$ 15,340	04/06/06	03/07/06	30
20952	\$ 2,500	04/24/06	04/07/06	17
21540	\$ 2,427	07/10/06	06/19/06	21
22005	\$ 9,566	09/06/06	08/18/06	19
22006	\$ 7,634	09/06/06	08/18/06	19
22007	\$ 4,666	09/06/06	08/18/06	19

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

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

Finding No. 2006-7, Continued

Effect: The effect of the above condition is noncompliance with applicable cash management requirements. However, no questioned costs resulted from the condition, as the estimated interest liability to the U.S. Department of Housing and Urban Development is less than \$10,000.

Recommendation: We recommend NMHC establish procedures to ensure that cash advances are disbursed within a timely manner.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Joshua T. Sasamoto, NMHC Corporate Director

Corrective Action: We recommend that Deloitte & Touche calculate the beginning date based on the pick-up date by the vendor to clearing date to satisfy the fifteen-day clearing time. NMHC will consider the fifteen-day clearing when the vendors receive their checks and deposit them to their accounts. NMHC gives the checks to the vendors timely, but has no control over when they deposit the checks.

Proposed Completion Date: Fiscal year 2007

Auditor Response:

NMHC shall be liable for interest on federal funds from the date the federal funds are credited to NMHC's bank account until those funds are paid out and are deducted from that bank account for program purposes. The interest from the time elapsed between the date the funds are received in the bank account and the date those funds are removed from the bank account, after considering the clearance pattern of fifteen days, represents the basis for calculating the interest liability due to the grantor agency.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

U.S. Department of Housing and Urban Development
Program Income - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M (01 to 05)-ST-69-0001
Federal Award Period October 1, 2001 - 2005 to September 30, 2006 - 2010

Finding No. 2006-8

Criteria: Revenues should be recognized in the period earned. Unearned revenues should be deferred and presented as deferred revenues in the financial statements. Further, HOME program income should be recognized in the general ledger for repayments of principal and interest on loans made with HOME funds.

Condition: NMHC records HOME loan disbursements as contributed capital which NMHC presents as revenues in its financial statements. Further, repayments of principal and interest on loans made using HOME funds are not recorded as program income in the general ledger. This condition was corrected through a proposed audit adjustment.

Cause: The cause of the above condition is management's oversight of the proper accounting of HOME loan disbursements and program income generated from HOME funds.

Effect: The effect of the above condition is the misstatement of revenues and related liabilities.

Recommendation: We recommend that NMHC ensure that HOME loan disbursements and repayments from participants are properly recorded in the general ledger. Further, NMHC should ensure that program income is recognized in the general ledger for repayments of principal and interest on loans made using HOME funds.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Roger A. Dris, NMHC Chief Accountant

Corrective Action: NMHC will ensure that HOME loan disbursements and repayments from participants are properly recorded in the general ledger. NMHC will ensure that program income is recognized in the general ledger for repayment of principal and interest on loans made using HOME funds. NMHC agreed with the grantor agency in recording program income by drawing down first the program income before entitlement funds.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

U.S. Department of Housing and Urban Development
Special Tests and Provisions - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M (01 to 05)-ST-69-0001
Federal Award Period October 1, 2001 - 2005 to September 30, 2006 - 2010

Finding No. 2006-9

Criteria: HOME loans extended to eligible participants should be properly monitored and accounted for.

Condition: Beginning in fiscal year 2006, NMHC has recorded, in its general ledger, loans receivable for HOME loans under a deferment agreement. Prior to fiscal year 2006, NMHC had not recorded loans receivables in its general ledger for loans extended to borrowers under a deferment agreement. At September 30, 2006, NMHC is in the process of determining the cumulative amount of loans under deferment agreement prior to fiscal year 2006.

Cause: The cause of the above condition is NMHC's understanding that loans under deferment agreements should not be recorded in the general ledger since repayments from these deferred loans are not expected.

Effect: The effect of the above condition is the possibility that loans under deferment agreements are not properly accounted for and presented in the financial reports.

Recommendation: We recommend NMHC determine with the grantor agency whether NMHC should be recording deferred HOME loan receivable and monitoring HOME loans under a deferment agreement.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Roger A. Dris, NMHC Chief Accountant

Correction Action: NMHC has confirmed with the grantor agency that all deferred loans should be recorded. NMHC is working with the NMHC legal counsel on revising HOME loans under a deferment agreement. NMHC is implementing and recording deferred HOME loan receivable.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2006

U.S. Department of Housing and Urban Development
Special Tests and Provisions - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M (01 to 05)-ST-69-0001
Federal Award Period October 1, 2001 - 2005 to September 30, 2006 - 2010

Finding No. 2006-10

Criteria: Under NMHC's policies and procedures for Homeowner Rehabilitation, HOME loan applicants that have been determined eligible for financial assistance and have proven lack of financial resources for repayment of their direct loan may have their monthly loan payments deferred for a payment of up to fifteen years. Further, borrowers with a deferment agreement shall be required to be annually re-certified as eligible to continue receiving a deferment during any potential deferment period.

Condition: NMHC did not perform the required annual re-certification for borrowers with deferment agreements.

Cause: The cause of the above condition is oversight by NMHC management in ensuring compliance with established policies and procedures for Homeowner Rehabilitation.

Effect: The effect of the above condition is noncompliance with established policies and procedures on Homeowner Rehabilitation.

Recommendation: We recommend NMHC management ensure that the annual recertifications of borrowers with deferment agreements be strictly adhered to.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Roger A. Dris, NMHC Chief Accountant

Correction Action: NMHC has confirmed with the grantor agency that all deferred loans should be recorded. NMHC is working with the NMHC legal counsel on revising HOME loans under a deferment agreement. NMHC is implementing and recording deferred HOME loan receivable.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Unresolved Prior Year Comments
Year Ended September 30, 2006

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, 2006:

Questioned costs as previously reported	\$ 13,406
Questioned costs of fiscal year 2006 Single Audit	<u> -</u>
Unresolved questioned costs at September 30, 2006	\$ <u>13,406</u>

Unresolved Findings

The status of unresolved findings is discussed in the Schedule of Findings and Questioned Costs section of this report (pages 8 through 23).



COMMONWEALTH DEVELOPMENT 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, 2005:

Financial Statement Findings

Finding No. 2005-1 - Not corrected. See corrective action plan to Finding No. 2006-1.

Federal Award Findings and Questioned Costs

Finding No. 2005-2 - Corrective action was taken.