



COMMONWEALTH DEVELOPMENT AUTHORITY

INDEPENDENT AUDITORS' REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2007

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

Board of Directors
Commonwealth Development Authority:

We have audited the financial statements of the Commonwealth Development Authority (CDA), as of and for the year ended September 30, 2007, and have issued our report thereon dated December 29, 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 as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of CDA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of CDA's internal control over financial reporting.

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects CDA's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of CDA's financial statements that is more than inconsequential will not be prevented or detected by CDA's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs (pages 9 through 47) to be significant deficiencies in internal control over financial reporting as items 2007-1 through 2007-7.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items 2007-1, 2007-3, 2007-4 and 2007-7 to be material weaknesses.

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 grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Schedule of Findings and Questioned Costs as item 2007-8.

We noted certain matters that we reported to management of CDA in a separate letter dated December 29, 2008.

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

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 29, 2008

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

Board of Directors
Commonwealth 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, 2007. 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 9 through 47). 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 2007-9 through 2007-28 in the accompanying Schedule of Findings and Questioned Costs, CDA did not comply with requirements regarding allowable costs/cost principles, cash management, Davis-Bacon Act, eligibility, matching, level of effort, earmarking, procurement and suspension and debarment, program income, reporting and special tests and provisions that are applicable to its CFDA 14.225 Community Development Block Grants/Special Purpose Grants/Insular Areas, CFDA 14.239 HOME Investment Partnerships Program and CFDA 14.871 Section 8 Housing Choice Vouchers programs. Compliance with such requirements is necessary, in our opinion, for CDA to comply with the requirements applicable to that program.

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, 2007.

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 the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of CDA's internal control over compliance.

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

A *control deficiency* in CDA's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects CDA's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by CDA's internal control. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 2007-9 through 2007-28 to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected in CDA's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs, we consider items 2007-9, 2007-10, 2007-14, 2007-17 and 2007-25 to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of CDA as of and for the year ended September 30, 2007, and have issued our report thereon dated December 29, 2008. Our audit was performed for the purpose of forming our opinion on CDA's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards (page 6) is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

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

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.

DeBate + Touche LLC

December 29, 2008

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Schedule of Expenditures of Federal Awards
Year Ended September 30, 2007

| Federal Grantor/ Program Title | Federal CFDA Number | Federal Cumulative Amount of Grant Award | Receivable (Deferred Revenue) from Grantor at October 1, 2006 | Federal Funds Received in Fiscal Year 2007 | Federal Funds Expended in Fiscal Year 2007 | Receivable (Deferred Revenue) from Grantor at September 30, 2007 |
|-----------------------------------------------------------------------------------------------------------------------------|---------------------------|---------------------------------------------------|------------------------------------------------------------------------------|--------------------------------------------------------|--------------------------------------------------------|---------------------------------------------------------------------------------|
| Direct Programs: | | | | | | |
| U.S. Department of Housing and Urban Development /Section 8 Housing Choice Vouchers | 14.871 | \$ 3,755,134 | \$ (764,291) | \$ 3,958,149 | \$ 3,167,587 | \$ (1,554,853) |
| U.S. Department of Housing and Urban Development /Section 8 New Construction and Substantial Rehabilitation | 14.182 | 480,416 | - | 319,504 | 480,416 | 160,912 |
| | 14.182 | 262,173 | - | 218,243 | 262,173 | 43,930 |
| | 14.182 | 160,967 | - | 160,967 | 160,967 | - |
| | 14.182 | 183,783 | - | 121,302 | 183,783 | 62,481 |
| Subtotal CFDA #14.182 | | 1,087,339 | - | 820,016 | 1,087,339 | 267,323 |
| U.S. Department of Housing and Urban Development/Community Development Block Grants/Special Purpose Grants/Insular Areas | 14.225 | 165,559 | - | 30,339 | 30,339 | - |
| Tinian Shelter/Tinian Outdoor Stage Public Library Phase II | 14.225 | 64,000 | - | 28,055 | 28,055 | - |
| Living Transitional Model Homes | 14.225 | 300,000 | - | 184,340 | 184,340 | - |
| Rota Baseball Field | 14.225 | 328,000 | - | 142,478 | 142,478 | - |
| Sugar King Cultural Center | 14.225 | 250,000 | - | 2,200 | 2,200 | - |
| Public Restroom in Rota | 14.225 | 247,000 | - | 168,210 | 168,210 | - |
| Administrative Fee | 14.225 | | | | | |
| Subtotal CFDA #14.225 | | 1,354,559 | - | 555,622 | 555,622 | - |
| U.S. Department of Housing and Urban Development /Emergency Shelter Grants Program | 14.231 | 342,006 | 8,239 | 28,250 | 26,184 | 6,173 |
| U.S. Department of Housing and Urban Development /HOME Investment Partnerships Program | 14.239 | 569,024 | - | 84,511 | 89,986 | 5,475 |
| | 14.239 | 414,778 | (96,625) | 249,228 | 299,808 | (46,045) |
| | 14.239 | 3,224,471 | - | 575,083 | 575,083 | - |
| Subtotal CFDA #14.239 | | 4,208,273 | (96,625) | 908,822 | 964,877 | (40,570) |
| | | \$ 10,747,311 | \$ (852,677) | \$ 6,270,859 | \$ 5,801,609 | \$ (1,321,927) |
| 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 | | | | | \$ 3,167,587 | |
| U.S. Department of Housing and Urban Development /Section 8 New Construction and Substantial Rehabilitation | | | | | 1,087,339 | |
| | | | | | \$ 4,254,926 | |
| 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 | | | | | \$ 2,788,538 | |
| Utilities | | | | | 174,660 | |
| Salaries and wages | | | | | 125,109 | |
| Employee benefits | | | | | 22,563 | |
| Travel | | | | | 38,842 | |
| Professional fees | | | | | 4,000 | |
| Property and equipment acquisition | | | | | 13,875 | |
| | | | | | 3,167,587 | |
| U.S. Department of Housing and Urban Development /Section 8 New Construction and Substantial Rehabilitation: | | | | | | |
| Salaries and wages | | | | | 191,456 | |
| Employee benefits | | | | | 88,338 | |
| Professional fees | | | | | 233,590 | |
| Repairs and maintenance | | | | | 346,792 | |
| Office rent | | | | | 8,400 | |
| Travel | | | | | 21,820 | |
| Utilities | | | | | 93,166 | |
| Other | | | | | 103,777 | |
| | | | | | 1,087,339 | |
| | | | | | \$ 4,254,926 | |

See accompanying notes to schedule of expenditures of federal awards.

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Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2007

(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 2007 and administers the funds and is responsible for ensuring compliance with laws and regulations.

U.S. Department of HUD - Section 8 New Construction and Substantial 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.

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Notes to Schedule of Expenditures of Federal Awards, Continued Year Ended September 30, 2007

(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, 2007, such funds amounting to \$658,806 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, 2007, \$1,642,368 (net of the allowance for doubtful accounts of \$66,159,100) 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, 2007, \$10,094,223 (net of the allowance for doubtful accounts of \$23,388,320) 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, 2007, \$2,596,145 (net of the related allowance for doubtful accounts of \$1,575,811 and out of total NMHC net loans receivable of \$11,032,733) of loans made out of this revolving fund were outstanding.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs
Year Ended September 30, 2007

A. SUMMARY OF AUDITOR'S RESULTS

1. The auditors' report expresses an unqualified opinion on the financial statements of CDA.
2. Significant deficiencies in internal control were disclosed by the audit of the financial statements, some of which are considered to be material weaknesses.
3. One instance of noncompliance considered material to the financial statements of CDA was disclosed during the audit.
4. Significant deficiencies in internal control were disclosed by the audit of the major federal award programs, some of which are considered to be material weaknesses.
5. The auditors' report on compliance for the major federal award programs for CDA expresses a qualified opinion.
6. There were audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133.
7. The programs tested as major programs were:

| <u>Name 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 |
| Section 8 Housing Choice Vouchers | 14.871 |

8. The threshold for distinguishing Types A and B programs was \$300,000.
9. CDA was determined not to be a low-risk auditee.

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

| <u>Reference Number</u> | <u>Findings</u> | <u>Refer Page #</u> |
|-----------------------------|--------------------------------|-------------------------|
| 2007-1 - 2 | DCD Loans Receivable | 11 - 14 |
| 2007-3 | NMHC Loans Receivable | 15 |
| 2007-4 | NMHC Land | 16 |
| 2007-5 | DCD Foreclosed Real Estate | 17 - 18 |
| 2007-6 | DCD Lease Transactions | 19 - 20 |
| 2007-7 | NMHC Loan Guarantee Agreements | 21 |
| 2007-8 | Local Noncompliance | 22 |

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007**C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS
AUDIT**

| <u>Reference Number</u> | <u>Findings</u> | <u>Questioned Costs</u> | <u>Refer Page #</u> |
|-----------------------------|------------------------------------------|-------------------------|-------------------------|
| 2007-9 | Allowable Costs/Cost Principles | \$ 1,211 | 23 - 24 |
| 2007-10 | Allowable Costs/Cost Principles | \$ - | 25 |
| 2007-11 | Cash Management | \$ - | 26 |
| 2007-12 | Davis-Bacon Act | \$ - | 27 |
| 2007-13 | Eligibility | \$ - | 28 |
| 2007-14 | Matching, Level of Effort, Earmarking | \$ - | 29 |
| 2007-15 | Procurement and Suspension and Debarment | \$ - | 30 |
| 2007-16 - 18 | Program Income | \$ - | 31 - 33 |
| 2007-19 - 20 | Reporting | \$ - | 34 - 36 |
| 2007-21 - 28 | Special Tests and Provisions | \$ - | 37 - 47 |

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

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

DCD Loans Receivable

Finding No. 2007-1

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, 2007. This analysis revealed that loans which are six months or more in arrears had increased from \$27,682,659 at September 30, 2006 to \$29,712,801 as of September 30, 2007. The related accrued interest on loans that are six months or more in arrears has also increased from \$13,946,053 at September 30, 2006 to \$14,362,485 as of September 30, 2007. As such, the collateral for these loans is decreasing as a percentage of the total loan and interest portfolio.
- For one delinquent account (# SB 70154), the final notice of delinquency was sent on April 8, 2003. No written evidence was noted in the loan file that subsequent action was taken to address the delinquency status of the loan.
- For three restructured loans (#s RE 70260, RE 70265 and CD 70257), which were past due for more than six months in arrears prior to the restructuring were classified as less than six months in arrears in the receivables aging report since the original due dates and past due balances were revised. As such, the related allowance was calculated based on the revised terms. An audit adjustment was proposed to record an additional allowance of \$900,292 relating to these three loans.
- As of September 30, 2007, CDA has recorded loans receivables miscellaneous charges (GL # 1208-00) of \$426,456 with a related allowance of \$228,970. This receivable account was excluded in CDA's calculation of the loan loss reserve at September 30, 2007. Further, CDA did not perform a separate assessment of the collectability of the account balance. This condition was corrected through a proposed audit adjustment for an additional allowance of \$195,321.

Cause: The cause of the above condition is the increase in past due loans and lack of adequate review of the reasonableness of the calculation of allowance for loan losses and other related receivables.

Effect: The effect of the above condition is an increased possibility of loan losses due to non-payment by borrowers and potential misstatement of loans receivable and related accounts.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-1, Continued

Recommendation: We recommend that CDA continue to follow-up on past due loans, continue to evaluate these loans and develop corrective action plans. We recommend that corrective action plans be documented accordingly. 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. We further recommend CDA review the aging of restructured loans and revisit allowance calculation for these loans. In addition, we recommend CDA perform periodic review of the calculation of allowance for loan losses and other related receivables for accuracy, completeness and reasonableness.

Prior Year Status: Past due loans was reported as a finding in the Single Audits of CDA for fiscal years 1994 through 2006.

Auditee Response and Corrective Action Plan:

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

Corrective Action: Responses provided for audit year 2006 are hereby incorporated and extended as our 2007 response to the same general findings. As of October 2006, CDA adopted a Strategic Mission Plan which became the working document on which to address the identified deficiencies. The Board adopted a debt relief program which has only recently 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 for an additional 30 years for purposes of amortization only with a mandated three (3) year callable (balloon payment) provision where warranted and justified; and the accrued interest 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.

In addition, we are making recommendations to the CDA Board to adopt a policy and rule that interest will stop accruing after 120 days of being delinquent for all new loans extended since the lifting of the moratorium and all future loans. This will prompt CDA to work with the borrower more closely since interest after the 120th day will not be counted as revenue. CDA and the borrower must reach a workable arrangement on how to treat the account. If an arrangement is reached, interest may accrue. Otherwise, any payments received will be applied to principal and the loan will be referred to the Legal Counsel for collection and/or foreclosure.

- For loan # SB 70154, Gung Ho, Inc., attempts were made by the Loan Manager in 2005 and 2006 to prompt the borrower, Ambrosio Ogomoro, to make payments. Payments were made in 2004 and 2005. Further attempts were made to convince the borrower to avail of the 2% debt relief but were unsuccessful. We will attempt again and take a more drastic approach by referring the account to our Legal Counsel for collection and/or foreclosure should our attempts fail. This should be done within the next couple of weeks.
- For loan #s 70260, 07265 and 70257, the allowances as suggested by the auditor are accepted.

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Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-1, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

The total loan portfolio decreased in 2007 from 2006. In 2007, 86% of total outstanding loans were six months or more in arrears while in 2006, the rate was 75%. Between 2004 and 2005, the rate was 61%. We need to do more to improve the conditions of the loans. However, increases in accrued interest between 2006, 2005 and 2004 remained relatively the same at 16%. In 2007, accrued interest increased by only by 3%. 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. Our primary objective is to reduce the delinquency through this debt relief program while protecting CDA's interest 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 the mounting accrued interest and will not improve if the objectives mentioned above are not met.

Proposed Completion Date: A new bank or classification has been created in 2007 dedicated only to accounts under this debt relief program. Under this bank, the arrested accrued interest is identified and removed and will be presented to the Board to be written-off only when warranted. Currently, CDA dumps all arrested accrued interest into the "write-off" bank classification. This allows CDA to identify how much has accrued, should be written-off and/or expended as loss. However, this classification does not necessarily absolve or forgive the borrower. The amounts are still legally required to be paid and collected.

A Rights to Possession Agreement as prelude to either a DILOF or actual judicial foreclosure proceeding will be a requisite to this debt relief program. This agreement entitles CDA to take possession and control of the RE collateral and business operations while foreclosure proceedings or DILOF are pursued. Since this program is a last ditch effort to assist borrowers, loans that become 60 days delinquent will be foreclosed.

Should borrowers adhere to the program, 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 a higher interest rate, CDA may negotiate to increase the interest rate at 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 are given this opportunity but not all will qualify since individual conditions are 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 foreclosure and losing their collateral.

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Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

DCD Loans Receivable

Finding No. 2007-2

Criteria: Identified adjustments to loan balances arising from loan reclassifications should be recorded in the general ledger in a timely manner.

Condition: During tests of loans receivables, we noted CDA adjustments in the current fiscal year to reclassify interest receivable, late and miscellaneous charges receivable to principal balance relating to six judgment loans. The related judgment, however, was ordered prior to the current fiscal year. As such, the reclassification should have been recorded in the fiscal year the judgment was ordered. An audit adjustment is not necessary as judgment loans are 100% allowed for. Details are as follows:

| <u>New Loan #</u> | <u>Old Loan #</u> | <u>Interest Receivables</u> | <u>Late Charges Receivables</u> | <u>Miscellaneous Charges Receivables</u> | <u>Total</u> |
|-------------------|-------------------|-----------------------------|---------------------------------|------------------------------------------|---------------------|
| CD 70273 | CD 31857 | \$ 896,443 | \$ 36,812 | \$ 9,887 | \$ 943,142 |
| CD 70270 | CD 33302 | 471,324 | 24,537 | - | 495,861 |
| RE 70268 | RE 70014 | 220,140 | 12,086 | 28,467 | 260,693 |
| CD 70275 | CD 33940 | 137,729 | 7,496 | 28,700 | 173,925 |
| CD 70271 | CD 70064 | 103,127 | 9,302 | 15,978 | 128,407 |
| CD 70274 | CD 3315 | 218,134 | 9,216 | - | 227,350 |
| | | <u>\$ 2,046,897</u> | <u>\$ 99,449</u> | <u>\$ 83,032</u> | <u>\$ 2,229,378</u> |

Cause: The cause of the above condition is the lack of monitoring procedures to ensure that all loan reclassification adjustments are recorded timely in the general ledger.

Effect: The effect of the above condition is incorrect classification of receivables and a potential misstatement of interest income from loans.

Recommendation: We recommend that CDA ensure that adjustments resulting from loan reclassifications are recorded in the general ledger in a timely manner.

Auditee Response and Corrective Action Plan:

Name of Contact Persons: Oscar C. Camacho, CDA Acting Chief Executive Officer, Elaine Benjamin, CDA Accounting Manager and Christy Kintol, CDA Office Manager

Corrective Action: Timely submission to Accounting will be emphasized and a process will be instituted. The Acting Chief Executive Officer will forward all judgments to Accounting, Administration and the Loan Manager. The Loan Manager and Administration will follow-up with Accounting if adjustments and reclassifications have been recorded 30 days after the submission to Accounting.

Proposed Completion Date: Particular findings were resolved via adjustments by the auditor learned in the discussions.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

NMHC Loans Receivable

Finding No. 2007-3

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 uncollectible should be adequately allowed for. Additionally, calculations of the allowance for loan losses should be regularly reviewed for accuracy, completeness and reasonableness.

Condition: An analysis of NMHC's allowance for delinquent loans revealed that loans which are over one hundred twenty days past due has increased from \$6,588,611 at September 30, 2006 to \$7,813,636 as of September 30, 2007. The related accrued interest on loans that are over one hundred twenty days past due has also increased from \$1,488,643 at September 30, 2006 to \$1,837,541 as of September 30, 2007. As such, the collateral for these loans is decreasing as a percentage of the total loan and interest portfolio. Further, as of September 30, 2007, a total of fifty-seven loans amounting to \$2,908,660 are inactive. The accrued interest on these inactive loans amounted to \$882,734.

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

Effect: The effect of the above condition is the increased possibility of loan losses due to nonpayment of borrowers.

Recommendation: We recommend that follow-up procedures be adhered to. We recommend that evaluations be performed on these loans and a corrective action 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.

Prior Year Status: NMHC's increase in past due loans was reported as a finding in the Single Audit of CDA for fiscal year 2006.

Auditee Response and Corrective Action Plan:

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

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

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

NMHC Land

Finding No. 2007-4

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

Condition: As of September 30, 2007, NMHC has land with recorded values of \$10,409,602. The last appraisal of the land occurred during fiscal year 2003. However, a November 2008 appraisal of two lots with a carrying value of \$256,000 resulted in an \$84,000 decrease in recorded values. Currently, the land is not for sale and is recorded by NMHC based on the most recent appraised values. In the event that the land will be marketed, NMHC will adjust to reflect the carrying amount or fair market value, whichever is lower.

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

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

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

Prior Year Status: The lack of established policies and procedures of periodic review of recorded values of real property and the high cost of obtaining appraisal services was reported as a finding in the Single Audit of CDA for fiscal year 2006.

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, 2007

DCD Foreclosed Real Estate

Finding No. 2007-5

Criteria: Valuations of real estate property acquired through, or in lieu of, loan foreclosures should be periodically performed by management and adjustments should be made to reflect real estate at the lower of the carrying amount or fair value less estimated costs to sell.

Condition: During tests of foreclosed real estate, we noted the following:

- At September 30, 2007, CDA has recorded six (reference lot #s 001 T 38, 1691-11-1, 1625 NEW-9-R1, TR22845-11, TR22845-13 and 016 H 47) foreclosed properties held for lease in which a long term leasehold interest was purchased by individuals or companies that are not of Northern Marianas decent; thus CDA still holds title to the properties. These properties were not valued at the lower of carrying amount or fair value less estimated costs to sell. This condition was corrected through a proposed audit adjustment.
- For one property (reference lot # 024 L 02), consisting of land and a building, CDA estimated a total market value of \$331,400 as of September 30, 2007. CDA valued the land and building at 100% and 30%, respectively, of the appraised values indicated in the latest independent appraisal report dated December 28, 2005. However, assumptions used and the basis of determination of the rates to estimated market values were not adequately documented or justified.

Cause: The cause of the above condition is the improper valuation of real estate properties held for lease and failure to maintain adequate documentation of assumptions used for in-house appraisals performed.

Effect: The effect of the above condition is the potential misstatement of foreclosed real estate properties.

Recommendation: We recommend that CDA management ensure that foreclosed properties, whether held for sale or lease, are valued at the lower of carrying amount or fair value less estimated costs to sell. Further, we recommend that CDA management perform periodic valuations of foreclosed properties, by obtaining independent appraisals or through the performance of in-house appraisals. Additionally, where in-house appraisals are performed, we recommend that CDA ensure that assumptions and the basis used are adequately documented and supported.

Auditee Response and Corrective Action Plan:

Name of Contact Persons: Oscar C. Camacho, CDA Acting Chief Executive Officer and Christy Kintol, CDA Office Manager

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-5, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action: CDA adopted a Schedule of Real Estate Evaluation using the lower market valuations of appraisals and agrees with the auditor's recommendation to provide for a 50% allowance. Should an in-house valuation be performed, it will be documented in memo form describing the approach to derive at a value. Otherwise, restricted appraisals will be obtained from appraisal companies every two years for properties needing valuation. Administration has supervision over CDA's assets, thus administering a process to obtain appraisals and valuations will come from this department. Accounting will be informed of periodic valuations and a similar process as above will be instituted.

Proposed Completion Date: A cut-off date of no later than June 30 of every year, should be established for appraisals and valuations to be completed.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

DCD Lease Transactions

Finding No. 2007-6

Criteria: Lease arrangements and related transactions should be evaluated for proper accounting.

Condition: During tests of existing lease agreements, the following were noted:

- CDA maintains foreclosed property in which long term leasehold interests were purchased by individuals or companies that are not of Northern Marianas decent, thus CDA still holds title to the property. CDA recorded full payments received at the date of sale as reductions of the foreclosed real estate account (for property initially purchased by CDA). For such arrangements, CDA should have recorded the advance payments as deferred lease revenues and should have recognized lease revenues over the term of the lease. This condition was corrected through a proposed audit adjustment. As of September 30, 2007 deferred lease revenues relating to these transactions amounted to \$721,555.
- Subsequent to September 30, 2007, CDA entered into a ground lease and option to purchase agreement for one foreclosed property (ref. lot # 024 L 02). CDA has not evaluated whether the arrangement qualifies as a capital lease.
- CDA leases one foreclosed property at \$1,500 per month. The lease agreement, however, does not specify the term of the lease. Further, the lease agreement was an assignment pursuant to the buy back of the original loan from a financial institution. The agreement has not been updated from the time it was assigned to CDA.

Cause: The cause of the above condition is failure to evaluate underlying lease arrangements.

Effect: The effect of the above condition is the potential misstatement of lease revenues and related accounts.

Recommendation: We recommend that CDA management ensure that lease arrangements are evaluated as to whether they constitute capital or operating leases.

Auditee Response and Corrective Action Plan:

Name of Contact Persons: Oscar C. Camacho, CDA Acting Chief Executive Officer and Christy Kintol, CDA Office Manager

Corrective Action:

- Initially, the Acting Chief Executive Officer disagreed with the auditor's suggestion to treat payments received from prepaid leases as deferred revenues. This is because prepaid lease was believed to be similar to how payments are treated when REs are sold fee simple. The auditor clarified that with such prepaid leases, CDA will still record the underlying fee simple residual interest as assets, thus treatment of payments received should be deferred. As such, CDA will start treating such leases as recommended.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-6, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

- On the finding with regards to a ground lease agreement qualifying as a capital lease for purposes of recording or accounting for lease revenues, CDA hereby agrees with auditor and has made the evaluation of the lease agreement. This particular lease meets the criteria set forth to qualify as a capital lease rather than as an operating lease. This ground lease is the current arrangement with Covenant Church on the former Pacific Islands Castle building in Koblerville near Coral Ocean Point.
- On the particular lease assignment where it does not specify the terms of the lease agreement, CDA opted to continue the month to month rental arrangement. CDA management at the time believed that with such a short-term rental arrangement, CDA could easily notify the tenant that it is terminating the lease. The tenant happens to be the same person with whom CDA and the bank foreclosed on and entered into the house rental arrangement in Rota. The arrangement proved difficult and the tenant was offered the option for a lease to own at a set price, but the offer was not immediately accepted. Therefore, CDA management took a strong position to terminate the rental arrangement, demand full payment on all back rents due and evict the tenant. However, the CDA Board continues to extend options to the tenant.

Proposed Completion Date: Evaluations to classify leases will be performed when executing new leases and Accounting will be notified of such classification. At the next CDA Board meeting, the CDA Board will make its final decision on the lease to own arrangement with the tenant in Rota.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

NMHC Loan Guarantee Agreements

Finding No. 2007-7

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 and purchase agreements with certain financial institutions. As of September 30, 2007, NMHC's related loan guarantees amounted to \$18,657,558. Of the total, approximately \$5,178,510 is delinquent and past due. Further, of the \$5,178,510, approximately \$3,285,260 is more than one hundred twenty days past due. NMHC has received demand notices of \$667,045. NMHC has recorded a reserve for loan guaranty for the \$667,045. However, NMHC is unable to determine if any additional reserve should be established for the remaining defaulted loans of \$4,511,465 and has no basis for an additional reserve due to limitations in existing information provided by the financial institutions. NMHC is currently working with related financial institutions to obtain sufficient information to determine a better estimate of the reserve for loan guarantees.

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 that NMHC ensure that the reserve for guaranteed loans is assessed and reviewed for adequacy. Further, we recommend that NMHC establish policies and procedures to assess the adequacy of the reserve for guaranteed loans, both past due and current. Additionally, we recommend that NMHC continue to obtain sufficient information from 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.

Prior Year Status: The lack of established policies and procedures to assess and review the adequacy of the reserve for guaranteed loans and the lack of relevant and sufficient information from financial institutions to estimate probable losses was reported as a finding in the Single Audit of CDA for fiscal year 2006.

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, 2007

Local Noncompliance

Finding No. 2007-8

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 was 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 is solely 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 that NMHC ensure compliance with Public Law 12-27 and the loan agreement with MPLT.

Prior Year Status: Noncompliance with P.L. 12-27 and the loan agreement with MPLT were reported as a finding in the Single Audit of CDA for fiscal year 2006.

Auditee Response and Corrective Action Plan:

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

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 2008 will resolve the issue due to the final transfer of the portfolio to MPLT.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

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

Allowable Costs/Cost Principles

Finding No. 2007-9

| Program | Reason for Questioned Costs | Questioned Costs | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
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| U.S. Department of Housing and Urban Development / Section 8 Housing Choice Vouchers / CFDA #14.871 / Federal Award # TQ901 / Federal Award Period 10/01/06 - 09/30/07 | <p>Criteria: In accordance with 24 CFR Section 982.158 and 982 subpart K, the PHA must pay monthly housing assistance payments (HAP) on behalf of the family that corresponds with the amount on line 12u of the HUD-50058. This HAP amount must be reflected on the HAP contract and HAP register.</p> <p>Condition: Of thirty HAP rental disbursements and six utility reimbursements tested, we noted the following:</p> <ul style="list-style-type: none"> The HAP disbursement relating to three participants did not correspond with the required HAP indicated in form HUD-50058 and HAP contract. Details are as follow: <table border="1" style="margin-left: 40px;"> <thead> <tr> <th style="text-align: left;">GL Date</th> <th style="text-align: left;">Tenant</th> <th style="text-align: left;">Landlord</th> <th style="text-align: right;">HAP Disbursement</th> <th style="text-align: right;">HAP per HUD 50058 and HAP Contract</th> <th style="text-align: right;">Variance</th> </tr> </thead> <tbody> <tr> <td>12/05/06</td> <td>John, Benri S.</td> <td>Soo San Corporation</td> <td style="text-align: right;">\$ 698</td> <td style="text-align: right;">\$ 642</td> <td style="text-align: right;">\$ 56</td> </tr> <tr> <td>01/05/07</td> <td>Masga, Rosemarie B.</td> <td>Mary Faith G. Villanueva</td> <td style="text-align: right;">\$ 2,200</td> <td style="text-align: right;">\$ 1,100</td> <td style="text-align: right;">1,100</td> </tr> <tr> <td>09/04/07</td> <td>Cruz, Erwin C.</td> <td>Guillermina C. Cepeda</td> <td style="text-align: right;">\$ 950</td> <td style="text-align: right;">\$ 940</td> <td style="text-align: right;">10</td> </tr> <tr> <td colspan="5"></td> <td style="text-align: right;">\$ 1,166</td> </tr> </tbody> </table> <ul style="list-style-type: none"> The actual utility reimbursement made to one participant did not agree to the utility allowance indicated in form HUD-50058. Details are as follow: <table border="1" style="margin-left: 40px;"> <thead> <tr> <th style="text-align: left;">Reference No.</th> <th style="text-align: left;">Name of Participant</th> <th style="text-align: right;">Actual Reimbursement</th> <th style="text-align: right;">Utility Allowance Per HUD 50058</th> <th style="text-align: right;">Variance</th> </tr> </thead> <tbody> <tr> <td>Check # 2803</td> <td>Ogo, Ignacio S.</td> <td style="text-align: right;">\$ 315</td> <td style="text-align: right;">\$ 270</td> <td style="text-align: right;">\$ 45</td> </tr> </tbody> </table> | GL Date | Tenant | Landlord | HAP Disbursement | HAP per HUD 50058 and HAP Contract | Variance | 12/05/06 | John, Benri S. | Soo San Corporation | \$ 698 | \$ 642 | \$ 56 | 01/05/07 | Masga, Rosemarie B. | Mary Faith G. Villanueva | \$ 2,200 | \$ 1,100 | 1,100 | 09/04/07 | Cruz, Erwin C. | Guillermina C. Cepeda | \$ 950 | \$ 940 | 10 | | | | | | \$ 1,166 | Reference No. | Name of Participant | Actual Reimbursement | Utility Allowance Per HUD 50058 | Variance | Check # 2803 | Ogo, Ignacio S. | \$ 315 | \$ 270 | \$ 45 | <p>\$ 1,211</p> |
| GL Date | Tenant | Landlord | HAP Disbursement | HAP per HUD 50058 and HAP Contract | Variance | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 12/05/06 | John, Benri S. | Soo San Corporation | \$ 698 | \$ 642 | \$ 56 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 01/05/07 | Masga, Rosemarie B. | Mary Faith G. Villanueva | \$ 2,200 | \$ 1,100 | 1,100 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 09/04/07 | Cruz, Erwin C. | Guillermina C. Cepeda | \$ 950 | \$ 940 | 10 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | | | | | \$ 1,166 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| Reference No. | Name of Participant | Actual Reimbursement | Utility Allowance Per HUD 50058 | Variance | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| Check # 2803 | Ogo, Ignacio S. | \$ 315 | \$ 270 | \$ 45 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| <p>Cause: The cause of the above condition is the lack of adequate monitoring procedures to ensure that HAP amounts are updated and adjusted to the system for any changes resulting from annual and/or interim reexaminations or other related actions taken.</p> <p>Effect: The effect of the above condition is the misstatement of HAP payments and questioned costs of \$1,211. This matter is reportable as the projected questioned costs exceed the threshold.</p> <p>Recommendation: We recommend NMHC establish adequate monitoring procedures to ensure that changes to HAP amounts are updated and adjusted in the system. Additionally, we recommend NMHC establish policies and procedures for the timely identification and reconciliation of variances between actual HAP disbursements and HAP per HUD 50058 and HAP contract.</p> <p>Auditee Response and Corrective Action Plan:</p> <p>Name of Contact Person: Kimo M. Rosario, NMHC Manager, Program & Housing</p> <p>Corrective Action:</p> <ol style="list-style-type: none"> John, Benri S.: No HAP check was issued to the landlord on 12/05/06. The landlord was owed \$3,210 in HAP checks representing five (5) months of payment at \$642 per month in HAPs. | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-9, Continued

| Program | Reason for Questioned Costs | Questioned Costs |
|----------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------|
| <u>Auditee Response and Corrective Action Plan, Continued:</u> | | |
| Corrective Action, Continued: | | |
| | 2. Masga, Rosemarie B.: The HAP check in the amount of \$2,200 for landlord Mary Faith G. Villanueva was voided twice on January 5, 2007 and check # 2803 is nowhere to be found in the system. | |
| | 3. Cruz, Erwin C.: The tenant was holding a disaster voucher that expired on September 30, 2007. The tenant underwent an interim reexamination on August 2007 after reporting to us that he was recently employed on July 25, 2007; however, since his voucher was set to expire a month later, NMHC could not change the contract to reflect the change of payment. | |
| | 4. Ogo, Ignacio S.: On April 16, 2007 after transferring a unit from Rota to Saipan, this tenant was owed a prorated amount of \$45 in URP (half of the \$90 URP amount due to tenant). This amount was disbursed on July 3, 2007. Moreover, the tenant was not paid \$90 for the subsequent months of May, June and July. As a result, on July 3, 2007, NMHC issued a check in the amount of \$315 ($\$90 \times 3 + \$45 = \315.00). | |
| Proposed Completion Date: Fiscal year 2009 | | |

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Allowable Costs/Cost Principles - All Major Programs

Finding No. 2007-10

Criteria: OMB Circular A-87, Cost Principles for State and Local Government, Attachment B, Section 11.h (4) states that when employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation unless a statistical sampling system or other substitute system has been approved by the cognizant Federal agency. Such documentary report will be required where employees work on more than one Federal award or a Federal award and a non-Federal award.

Condition: Payroll expenses charged to the CDBG, HOME and Section 8 voucher programs amounting to \$150,335, \$89,986 and \$147,672, respectively for the fiscal year ended September 30, 2007 were determined by NMHC's Chief Accountant through an estimated percentage of work spent by employees working on these programs. Of thirteen, ten, and eleven employees tested under the CDBG, HOME and Section 8 voucher programs, respectively, we noted that all employees worked on more than one federal program. However, we did not note any personnel activity report supporting the distribution of time spent on each federal program. Further, we noted that NMHC employees only started maintaining payroll activity reports subsequent to fiscal year 2007 and thus, we are unable to quantify any questioned costs that may result from this condition.

Cause: The cause of the above condition is the lack awareness by NMHC of the requirements of OMB Circular A-87, attachment B, Section 11.h (4).

Effect: The effect of the above condition is noncompliance with the allowable costs/cost principle requirements.

Recommendation: We recommend NMHC ensure that personnel activity reports or equivalent documentation to reflect after-the-fact distributions of the actual activity of each employee are prepared and maintained for all employees who work on more than one federal award or a federal award and a non-federal award.

Auditee Response and Corrective Action Plan:

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

Corrective Action: NMHC will ensure that personnel activity reports or equivalent documentation to reflect after-the-fact distributions of the actual activity of employee are prepared and maintained for all employees who work on more than one federal award or a federal award and a non-federal award. Corrective action been applied by requiring all employees to submit a timesheet once every quarter as per HUD's recommendation.

Proposed Completion Date:

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Cash Management - Community Development Block Grants/Special Purpose Grants/Insular Areas
CFDA #14.225, Federal Award # B-05-ST-69-0001
Federal Award Period 10/01/05 - 09/30/10

Finding No. 2007-11

Criteria: In accordance with applicable cash management requirements, when funds are advanced, recipients must use and follow procedures to minimize the time elapsing between the transfer of grant funds from the U.S. Treasury and disbursement for program activities. The allowable clearance pattern is three days. The recipient shall be liable for interest on federal funds from the date the federal funds are credited to the recipient's bank account until those funds are paid out and are deducted from that bank account for program purposes.

Condition: For four of seventeen disbursements tested relating to the CDBG program, the following were cleared between two to twelve days after the allowable clearance pattern from the date federal funds were credited to NMHC's account. Details are as follows:

| <u>Check #</u> | <u>Check Amount</u> | <u>Check Clearance Date</u> | <u>Cash Receipts Date</u> | <u>Days Elapsed After the Allowable Clearance Pattern</u> |
|----------------|---------------------|-----------------------------|---------------------------|-----------------------------------------------------------|
| 122 | \$ 6,505 | 06/15/07 | 06/08/07 | 2 |
| 23858 | \$ 56,168 | 05/15/07 | 05/04/07 | 6 |
| 13 | \$ 68,366 | 06/04/07 | 05/25/07 | 5 |
| 22547 | \$ 30,339 | 11/14/06 | 10/26/06 | 12 |

Cause: The cause of the above condition is the failure of payees to present the checks to the bank within the allowable three day clearance pattern.

Effect: The effect of the above condition is a possible interest liability of \$144. 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 that NMHC review existing cash management procedures to ensure that cash advances are disbursed and cleared within the allowable clearance pattern.

Auditee Response and Corrective Action Plan:

Name of Contact Persons: Roger A. Dris, NMHC Chief Accountant and Edith C. Fejeran, NMHC Office Manager

Corrective Action: NMHC has reviewed existing cash management procedures to ensure that cash advances are disbursed and cleared within the allowable clearance pattern. Corrective action will be applied by mailing all checks issued from CDBG, HOME and ESG funds via certified mail and recording them in a certified mail log documenting compliance regarding checks for these programs. Vendors will be informed that checks can no longer be picked-up at the NMHC payment window.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Davis-Bacon Act - Community Development Block Grants/Special Purpose Grants/Insular Areas
CFDA #14.225, Federal Award # B-04-ST-69-0001
Federal Award Period 10/01/04 - 09/30/09

Finding No. 2007-12

Criteria: As part of NMHC's control procedures in monitoring compliance with the requirements of the Davis-Bacon Act, interviews of contractor workers at job sites are performed.

Condition: During tests of NMHC's controls over compliance with the Davis-Bacon Act, the records of employee interviews to support job site interviews of contractor employees were not made available for the following CDBG funded projects:

| <u>Project Name</u> | <u>Contract Number</u> | <u>Contract Amount</u> |
|-------------------------------|------------------------|------------------------|
| Sugar King Cultural Center | NMHC 2006-004 | \$ 119,500 |
| Tinian Outdoor Stage | NMHC 2005-008 | \$ 165,559 |
| Independent Living Model Home | NMHC 2006-003 | \$ 90,000 |

Cause: The cause of the above condition is the lack of established monitoring procedures to ensure the job site interviews are performed and are properly documented.

Effect: The effect of the above condition is noncompliance with NMHC's control procedures to ensure that the requirements of the Davis-Bacon Act are complied with.

Recommendation: We recommend NMHC establish monitoring controls to ensure that required procedures relating to job site interviews are strictly performed and are properly documented.

Auditee Response and Corrective Action Plan:

Name of Contact Persons: Zenie P. Mafnas, NMHC Grant Writer/Planner and Clemente Sablan, NMHC CDBG Technical Coordinator

Corrective Action: Though job site interviews were performed for these projects by its retired employee, NMHC could not locate the files that were under his custody, which were turned over to the Administration for file and maintenance. With the hiring of a CDBG Technical Coordinator, who currently interviews workers at each job site and ensures compliance to Davis-Bacon Act, job interview reports will now be adequately maintained.

Proposed Completion Date: Immediately

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Eligibility - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M-05-ST-69-0001
Federal Award Period 10/01/04 - 09/30/09

Finding No. 2007-13

Criteria: Under NMHC's Policies and Procedures for Home Rehabilitation, one of the requirements to be eligible for Home Program Financial assistance is that the "after-rehabilitation" value of the property must not exceed 95% of the HUD prescribed median purchase price for the type of unit. Additionally, the 95% after-rehabilitation value is described under CFR 92.254 as affordable housing for rehabilitation of property not involving acquisition.

Condition: Of fourteen individuals tested for compliance with eligibility requirements, we were not provided any documentation that the after rehabilitation value of the property for two (ref. loan #s DHL-235 and HL- 237) individuals was determined.

Cause: The cause of the above condition is failure to ensure that all eligibility documentation are properly maintained.

Effect: The effect of the above condition is noncompliance with eligibility requirements.

Recommendation: We recommend NMHC ensure that relevant eligibility documentation are properly maintained in the files.

Auditee Response and Corrective Action Plan:

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

Corrective Action: For loan # DHL-235, a drive-by property appraisal was not completed. A completed appraisal will be included in this response. In regard to loan # HL-237, a drive-by property appraisal was completed and is included in this response. MCD will ensure that all after-rehabilitated homes are valued and be less than 95% of the HUD prescribed median purchase price.

Proposed Completion Date: Immediately

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Matching, Level of Effort, Earmarking - Community Development Block Grants/Special Purpose
Grants/Insular Areas
CFDA #14.225, Federal Award # B-04-ST-69-0001
Federal Award Period 10/01/04 - 09/30/09

Finding No. 2007-14

Criteria: In accordance with 24 CFR Section 570.200 (a)(3), not less than 70 percent of the funds must be used over a period of up to three years, as specified by the grantee in its certification, for activities that benefit low- and moderate-income persons.

Condition: For program year 2004, NMHC was approved CDBG grant funds of \$1,235,000. As of September 30, 2007, the cumulative total expenditures relating to program year 2004 amounted to \$792,898 equivalent only to 64% of the grant funds.

Cause: The cause of the above condition is the lack of adequate controls to ensure that the 70% earmarking requirement is strictly adhered to.

Effect: The effect of the above condition is noncompliance with earmarking requirements.

Recommendation: We recommend NMHC strengthen controls to ensure that grant funds are expended within the required period.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Zenie P. Mafnas, NMHC Grant Writer/Planner

Corrective Action: The above regulation, cited by the auditors, states that not less than 70% of the aggregate of CDBG fund expenditures shall be for activities meeting the criteria under Section 570.208(a) or under Section 570.208(d)(5) or (6) for benefiting low and moderate income persons. The citation does not specify that not less than 70% of the total grant amount should be expended over a period of three years, as stated by the auditors under "Condition". Therefore, 2007-19 should not be a finding.

Proposed Completion Date:

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Procurement and Suspension and Debarment - Community Development Block Grants/Special
Purpose Grants/Insular Areas
CFDA #14.225, Federal Award # B-04-ST-69-0001
Federal Award Period 10/01/04 - 09/30/09

Finding No. 2007-15

Criteria: In accordance with OMB Circular A-87, Attachment B, Section 43, costs incurred by employees and officers for travel, including costs of lodging, other subsistence and incidental expenses shall be considered reasonable and allowable only to the extent such costs do not exceed charges normally allowed by the governmental unit in its regular operations as the result of the governmental unit's written travel policy. In the absence of an acceptable, written governmental unit policy regarding travel costs, the rates and amounts established under Subchapter 1 of Chapter 57, Title 5, United States Code or by the Administrator of General Services or by the President (or his or her designee) pursuant to any provisions of such subchapter shall apply to travel under Federal awards (48 CFR 31.205-46(a)).

Condition: During tests of compliance with procurement regulations, we noted that for one item, relating to the purchase of airline ticket, (ref. CV23720), there were no relevant documentation in the file to support that competitive procurement procedures were utilized.

Cause: The cause of the above condition is the lack of a written procurement policy concerning travel and related expenditures. Existing procurement regulations followed by NMHC do not include procurement procedures relating to airfare.

Effect: The effect of the above condition is noncompliance with federal regulations on federally funded travel and related expenditures.

Recommendation: We recommend NMHC adhere to federal travel regulations in the absence of a local procurement policy and/or incorporate procedures relating to the procurement of travel and related expenditures in local procurement regulations.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Roger A. Dris, NMHC Chief Accountant and Edith C. Fejeran, NMHC Office Manager

Corrective Action: NMHC is following the CNMI Government Travel Policies. NMHC does provide equal opportunity to and utilizes several travel agencies to book reservations and procure airline tickets for the Board and staff. Some travel agencies have their respective policies to 1) prefer upfront payment before actually issuing airline tickets; 2) process and issue ticketed reservations upon request with subsequent billing; or 3) accept a purchase order for each ticketed transaction. NMHC's request for inspections on projects are not foreseen in advance as it depends on the progress of the project for example, when cement pouring schedules are made and NMHC is notified by the contractor within several days notice to fly to Rota or Tinian. Immediate corrective action will be taken to solicit quotations directly from airlines and/or travel agencies and document such contacts in the file for audit and inspection.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Program Income - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M-07-ST-69-0203
Federal Award Period 10/01/06 - 09/30/11

Finding No. 2007-16

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.

Prior Year Status: Improper accounting of HOME loan disbursements and program income generated from HOME funds was reported as a finding in the Single Audit of CDA for fiscal year 2006.

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, 2007

U.S. Department of Housing and Urban Development
Program Income - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M-07-ST-69-0203
Federal Award Period 10/01/06 - 09/30/11

Finding No. 2007-17

Criteria: Under the Code of Federal Regulations (CFR) Title 24 Part 92.502 (c) (3), HOME funds in the local account of the HOME Investment Trust Fund must be disbursed before requests are made for HOME funds in the United States Treasury account. Further, under CFR Title 24 Part 92.2, HOME funds include program income.

Condition: NMHC receives payments of principal and interest on loans made with HOME funds and deposits these into its local account and reports these receipts in the Integrated Disbursement and Information System as program income. During fiscal year 2007, NMHC's drawdown from the U.S. Treasury of Home funds amounted to \$659,442. Further, during fiscal year 2007, NMHC reported total program income of \$249,856 and reported disbursements from the program income of \$203,811. As of September 30, 2007, NMHC has \$46,045 of undisbursed program income in its local account.

Cause: The cause of the above condition is the earmarking of program income received for loan assistance to eligible applicants. NMHC's records shows that no program income is available for drawdown.

Effect: The effect of the above condition is noncompliance with program income compliance requirements.

Recommendation: We recommend that NMHC ensure that program income is disbursed before requests are made for HOME funds in the U.S. Treasury account. Additionally, we recommend that NMHC review existing procedures of earmarking program income and ensure that procedures are designed to support compliance of the program requirements.

Auditee Response and Corrective Action Plan:

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

Corrective Acton: NMHC will ensure that program income is disbursed before requests are made for HOME funds in the U.S. Treasury account. NMHC will review existing procedures of earmarking program income and ensure that procedures are designed to support compliance of the program requirements. NMHC agreed with the grantor agency in recording program income by drawing down 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, 2007

U.S. Department of Housing and Urban Development
Program Income - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M-07-ST-69-0203
Federal Award Period 10/01/06 - 09/30/11

Finding No. 2007-18

Criteria: Under 24 CFR Section 85.20(b)(1), accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant.

Condition: During fiscal year 2007, NMHC reported program income receipts and drawdowns of \$249,856 and \$300,435, respectively, in the IDIS. However, these amounts did not agree with NMHC's accounting records which reflected program income received and expended during fiscal year 2007 of \$220,093 and \$299,808, respectively.

Cause: The cause of the above condition is the lack of timely reporting in the IDIS of program income received and the lack of reconciliation of program income and drawdowns reported in the IDIS and amounts recorded in the general ledger.

Effect: The effect of the above condition is inaccurate reporting of program income and drawdowns.

Recommendation: We recommend that NMHC strengthen controls in monitoring and ensuring that program income receipts and drawdowns are identified on a timely manner and are accurately reported to the IDIS.

Auditee Response and Corrective Action Plan:

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

Corrective Action: NMHC will strengthen controls in monitoring and will ensure that program income receipts and drawdown are identified in a timely manner and are accurately reported in IDIS. NMHC will record program income on a spreadsheet for tracking purposes and input on IDIS every first week of the following month.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Reporting - Community Development Block Grants/Special Purpose Grants/Insular Areas
CFDA #14.225, Federal Award # B-04-ST-69-0001
Federal Award Period 10/01/04 - 09/30/09

U.S. Department of Housing and Urban Development
Reporting - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M-07-ST-69-0203
Federal Award Period 10/01/06 - 09/30/11

Finding No. 2007-19

Criteria: In accordance with 24 CFR 135.3(a) and 135.90, for each grant over \$200,000 that involves housing rehabilitation, housing construction, or other public construction, the prime recipient must submit Form HUD 60002, "*Section 3 Summary Report, Economic Opportunities for Low-and Very Low-Income Persons*". Where the program providing Section 3 covered assistance requires submission of an annual performance report, the Section 3 report will be submitted with the annual performance report.

Condition: The annual performance report submitted by NMHC for fiscal year 2007 did not include form HUD 60002, Section 3 Summary Report, Economic Opportunities for Low-and Very Low-Income Persons.

Cause: The cause of the above condition is management's oversight of the reporting requirements specified under 24 CFR Section 135.90.

Effect: The effect of the above is noncompliance with grant reporting requirements.

Recommendation: We recommend that NMHC ensure that all grant reporting requirements are strictly adhered to.

Auditee Response and Corrective Action Plan:

Name of Contact Persons: Jesse S. Palacios, NMHC Manager, Mortgage Credit Division (HOME) and Clemente S. Sablan, NMHC CDBG Technical Coordinator

Corrective Action: In regard to the HOME Program, NMHC is not required to submit the Section 3 Summary Report since the maximum loan amount for this program is \$50,000. With respect to Section 3 compliance called for under the Community Development Block Grant (CDBG) Program, bid packages do include the Section 3 Summary Report for compliance "to the maximum extent possible", "to the greatest extent feasible" for contractors awarded CDBG projects to provide employment and training opportunities to low-income persons. In projects inspected for compliance, actual job sites do include a Job Information Poster that contractors are required to post for interested job seekers to apply. With the CNMI's limited labor pool, and particularly, the absence of a qualified, skilled and available journey-level workforce (carpenters, cement masons, electricians, steel workers, etc.) contractors have reported to NMHC that the Department of Labor has no local applicants to refer for these occupations. With the recent hiring of a CDBG Technical Coordinator to monitor field compliance, NMHC will move towards collaboration with the Work Investment Partnership (WIA) and Food Stamp Programs including the Department of Labor.

Proposed Completion Date: Ongoing

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Reporting - Section 8 Housing Choice Vouchers
CFDA #14.871, Federal Award # TQ901
Federal Award Period 10/01/06 - 09/30/07

Finding No. 2007-20

Criteria: In accordance with 24 CFR part 908 and 24 CFR section 982.158, the PHA is required to submit form HUD-50058, Family Report (OMB No. 2577-0083) electronically to HUD each time the PHA completes an admission, annual reexamination, interim reexamination, portability move-in, or other change of unit for a family. The PHA must also submit the Family Report when a family ends participation in the program or moves out of the PHA's jurisdiction under portability.

Condition: Of thirty participants tested, we noted the following:

- The submission transaction lists supporting online submission of form HUD-50058 for three participants were not made available for review. As such, we were unable to verify if the form HUD-50058 was indeed submitted. Details are as follow:

| <u>Participant's Name</u> | <u>Type of Change</u> | <u>Effective Date</u> |
|---------------------------|-----------------------|-----------------------|
| Delos Santos, Joaquin S. | Interim reexamination | 09/01/07 |
| Kenio, Inos K. | Interim reexamination | 12/01/06 |
| Teregeyo, Loyola R. | Annual reexamination | 09/01/07 |

- The submission transaction list made available for one item did not reflect the name of the following participant:

| <u>Ticket #</u> | <u>Participant's Name</u> | <u>Type of Change</u> | <u>Effective Date</u> |
|-----------------|---------------------------|-----------------------|-----------------------|
| 2206094 | Cruz, Erwin D. | Annual reexamination | 09/01/07 |

Cause: The cause of the above condition is the lack of adequate review procedures to ensure that all grant reporting requirements are submitted completely.

Effect: The effect of the above condition is noncompliance with federal reporting requirements.

Recommendation: We recommend that NMHC establish and implement review procedures to ensure that all grant reporting requirements are completely submitted and properly supported and documented.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Kimo M. Rosario, NMHC Manager, Program & Housing

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-20, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action:

1. **Delos Santos, Joaquin S.:** An Interim Reexamination Certification with an effective date of 09/01/07 does not exist. The only record NMHC has on Interim Reexaminations for this family is dated on 02/01/08 and 05/01/08, both of which were submitted on the same dates, respectively.
2. **Kenio, Inos K.:** This tenant's Interim Reexamination with an effective date of 12/01/06 was not submitted.
3. **Teregeyo, Loyola R.:** This tenant's Annual Reexamination with an effective date of 09/01/07 was not submitted.
4. **Cruz, Erwin D.:** This tenant's Annual Reexamination with an effective date of 09/01/07 was submitted on 10/05/07.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Special Tests and Provisions - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M-07-ST-69-0203
Federal Award Period 10/01/06 - 09/30/11

Finding No. 2007-21

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, 2007, 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 the NMHC 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 that NMHC determine with the grantor agency whether NMHC should record deferred HOME loans receivable and monitor HOME loans under a deferment agreement.

Prior Year Status: Lack of monitoring of loans under deferment agreement was reported as a finding in the Single Audit of CDA for fiscal year 2006.

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, 2007

U.S. Department of Housing and Urban Development
Special Tests and Provisions - HOME Investment Partnerships Program
CFDA #14.239, Federal Award # M-07-ST-69-0203
Federal Award Period 10/01/06 - 09/30/11

Finding No. 2007-22

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 period 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 an 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 for Homeowner Rehabilitation.

Recommendation: We recommend NMHC management ensure that the annual recertification of borrowers with deferment agreements is strictly performed.

Prior Year Status: Failure to perform annual re-certifications of borrowers with deferment agreements was reported as a finding in the Single Audit of CDA for fiscal year 2006.

Auditee Response and Corrective Action Plan:

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

Corrective Action: NMHC will ensure that the annual recertification of borrowers with deferment agreements is strictly performed. The Accounting Division will work closely with Loan Division in compliance with established policies and procedures on Homeowner Rehabilitation.

NMHC will ensure that the annual re-certification requirement wherein borrowers who have their monthly loan payments deferred will be adhered to. Should the borrower's financial situation remain the same then MCD will recommend to the Board to allow the borrower to continue his/her deferment status for another year. NMHC is also in the process of revising the Homeowner Rehabilitation Policies and Procedures. In the loan deferment section, it will have documentation requirements (e.g., affidavit, NAP certification) to show proof that the borrower is for example, unemployed.

Proposed Completion Date: Strict compliance of the re-certification requirement will be exercised immediately.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Special Tests and Provisions - Section 8 Housing Choice Vouchers
CFDA #14.871, Federal Award # TQ901
Federal Award Period 10/01/06 - 09/30/07

Finding No. 2007-23

Criteria: In accordance with CFR Part 24 Section 982.503(a)(1), the PHA must adopt a payment standard schedule that establishes voucher payment standard amounts for each fair market rent (FMR) area in the PHA jurisdiction. Under NMHC's Section 8 Administrative Plan for Rental Assistance Program Section 10.1, NMHC currently administers a payment standard that is at 90% of the published FMR set for Guam and the Pacific Islands.

Condition: During fiscal year 2007, NMHC's payment standard schedule was based on 90% of published 2006 FMR instead of the 2007 FMR which is effective October 1, 2006.

Cause: The cause of the above condition is the lack of strict monitoring procedures to ensure that payment standard schedules are updated.

Effect: The effect of the above condition is the potential misstatement of payment standard amounts used to calculate the monthly housing assistance payment.

Recommendation: We recommend NMHC ensure that payment standard schedules are updated to reflect current fair market rents published by HUD.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Kimo M. Rosario, NMHC Manager, Program & Housing

Corrective Action: NMHC based its 2007 payment standard schedule on the published 2007 FMR and the same has been inputted into the system.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Special Tests and Provisions - Section 8 Housing Choice Vouchers
CFDA #14.871, Federal Award # TQ901
Federal Award Period 10/01/06 - 09/30/07

Finding No. 2007-24

Criteria: Under 24 CFR 982.405(a), the Public Housing Agency (PHA) must inspect the unit leased to a family prior to the initial term of the lease, at least annually during assisted occupancy, and at other times as needed, to determine if the unit meets the Housing Quality Standards (HQS). Further, under CFR Part 24 sections 982.158(d), the PHA must prepare a unit inspection report.

Condition: Of thirty items tested for HQS inspections, the annual HQS inspection reports for three items were not made available. Details are as follow:

| <u>Participant's Name</u> | <u>Date of HQS Inspection per HUD 50058</u> |
|---------------------------|---------------------------------------------|
| Delos Santos, Joaquin S. | 07/26/07 |
| John, Benri S. | 07/19/07 |
| Pangelinan, Livia Mae T. | 07/26/07 |

Additionally, the annual HQS inspection for one item was performed more than 12 months after the previous HQS inspection performed on 08/25/06. Details follow:

| <u>Participant's Name</u> | <u>Date of HQS Inspection per HUD 50058</u> |
|---------------------------|---------------------------------------------|
| Cruz, Erwin D. | 10/03/07 |

Cause: The cause of the above condition is the lack of systematic filing of HQS inspection reports and the lack of strict monitoring to ensure that all HQS inspections are performed on a timely manner.

Effect: The effect of the above condition is possible noncompliance with the HQS inspections requirement under the federal regulations.

Recommendation: We recommend that NMHC ensure that all HQS inspections are supported with HQS inspection reports and are performed at least annually. Additionally, we recommend that NMHC ensure that all HQS inspection reports are maintained in participant files.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Kimo M. Rosario, NMHC Manager, Program & Housing

Corrective Action:

1. **Delos Santos, Joaquin:** This tenant's Annual Reexamination date is May 1, 2007 and his Annual HQS inspection was performed on April 23, 2007.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-24, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

2. **John, Benri S.:** This tenant's Annual Reexamination date is December 31, 2007 and his Annual HQS Inspection was performed on October 24, 2007.
3. **Pangelinan, Livia Mae T.:** This tenant's Annual HQS Inspection was not timely completed since she requested to transfer to another unit.
4. **Cruz, Erwin D.:** This tenant's Admission Date was September 14, 2006; hence, the HQS inspection date of August 25, 2006 could not possibly be late since admission was just a month away.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Special Tests and Provisions - Section 8 Housing Choice Vouchers
CFDA #14.871, Federal Award # TQ901
Federal Award Period 10/01/06 - 09/30/07

Finding No. 2007-25

Criteria: Under CFR Part 24 section 982.405(b), the PHA must conduct supervisory quality control Housing Quality Standards (HQS) inspections. Further, NMHC's Section 8 Administrative Plan for Rental Assistance Program Section 6.3 states that NMHC's manager for the program and housing manager division must re-inspect a sample of units under contract during the last fiscal year. Additionally, completed HQS inspections included in the sample must be no older than three months at the time of the re-inspection. The sample must represent a cross section of neighborhoods where the program units are located and inspections completed by all HQS inspectors.

Condition: During fiscal year 2007, NMHC performed the required supervisory quality control HQS inspections only for "failed" unit inspections and was not based on the required sample of all completed HQS inspections.

Cause: The cause of the above condition is the lack of adequate NMHC personnel to independently perform the required unit inspections and quality control re-inspections.

Effect: The effect of the above condition is noncompliance with the specific requirements of the federal regulation.

Recommendation: We recommend that NMHC ensure that adequate personnel are available to perform the unit inspections and quality control re-inspections and ensure that compliance requirement on supervisory control HQS inspection is strictly adhered to.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Kimo M. Rosario, NMHC Manager, Program & Housing

Corrective Action: Since February 2007 to the end of FY 2007, the Program and Housing Division Manager has been performing HQS inspections on all units especially after the agency's HQS inspector resigned in late July 2007.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Special Tests and Provisions - Section 8 Housing Choice Vouchers
CFDA #14.871, Federal Award # TQ901
Federal Award Period 10/01/06 - 09/30/07

Finding No. 2007-26

Criteria: In accordance with 24 CFR 982.204(a), except for special admissions, participants must be selected from the Public Housing Agency (PHA) waiting list. The PHA must select participants from the waiting list in accordance with admission policies in the PHA administrative plan.

Condition: During tests of compliance with the selection from the waiting list requirement, we noted the following:

- Of two new admissions during fiscal year 2007 tested, the waiting list relating to one admission (ref. Participant: Lorna Alcalá admitted to the program on 10/23/06) was not made available. We are unable to determine if the participant was selected from the waiting list.
- The files for three applicants, reaching the top of the waiting list but not admitted to the program, were not made available. We are unable to determine whether these applicants were provided the opportunity to be admitted to the program and whether the non-admission was properly documented. Details are as follow:

| <u>Application #</u> | <u>Applicant's Name</u> |
|----------------------|-------------------------|
| RV06-03 | Apatang, Bernard |
| RV06-04 | Hocog, Barbara Ogo |
| RV06-05 | Atalig, Lisa Jeannette |

Cause: The cause of the above condition is lack of adherence to established policies and procedures to ensure that the selection of participants is completely documented.

Effect: The effect of the above condition is noncompliance with the waiting list requirements under federal regulations.

Recommendation: We recommend that NMHC ensure that selections of applicants from the waiting list are properly documented and maintained in the files.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Kimo M. Rosario, NMHC Manager, Program & Housing

Corrective Action:

1. **Lorna Alcalá:** This participant was improperly selected and admitted to the program.
2. **Apatang, Bernard:** This applicant cancelled his application on May 30, 2006. This report is in the SEMAP Indicator No. 1 Folder.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-26, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

3. **Hocog, Barbara:** This applicant was transferred to the New Construction Program on March 8, 2006.
4. **Atalig, Lisa:** This applicant cancelled her application on April 15, 2006.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Special Tests and Provisions - Section 8 Housing Choice Vouchers
CFDA #14.871, Federal Award # TQ901
Federal Award Period 10/01/06 - 09/30/07

Finding No. 2007-27

Criteria: As provided under 24 CFR section 982.404, for units under Housing Assistance Payment (HAP) contracts that fail to meet Housing Quality Standards (HQS), the PHA must require the owner to correct any life threatening HQS deficiencies within 24 hours after the inspections and all other HQS deficiencies within 30 calendar days or within a specified PHA-approved extension. If the owner does not correct the cited HQS deficiencies within the specified correction period, the PHA must stop (abate) HAPs beginning no later than the first of the month following the specified correction period or must terminate the HAP contract.

Condition: Of ten unit re-inspections tested, we noted the following:

- For two items, the information on the deficiency report does not clearly indicate whether the corrective action has been addressed by the owner within the prescribed period:

| <u>Participant's Name</u> | <u>Inspection Date</u> |
|---------------------------|------------------------|
| Takao, Theresita | 03/19/07 |
| Mangatinag, Rosemary | 04/24/07 |

- For one item (ref. Participant name: Theresita Takao), the re-inspection was re-scheduled from 04/04/07 to 05/17/07 which is 59 days from the annual inspection date of 03/19/07.

Cause: The cause of the above condition is the lack of proper documentation of the results of re-inspections performed and the lack of monitoring to ensure that deficiencies are timely addressed.

Effect: The effect of the above condition is noncompliance with the HQS enforcement requirement under the federal regulations.

Recommendation: We recommend NMHC ensure that results of HQS enforcements are properly documented in the deficiency reports and re-inspections are performed on a timely manner.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Kimo M. Rosario, NMHC Manager, Program & Housing

Corrective Action:

1. **Takao, Therisita:** The unit for this tenant was re-inspected on May 17, 2007 and it passed the re-inspection; however, the HQS inspector failed to fill in the deficiency report indicating that the deficiencies found on the unit were addressed and cured.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

Finding No. 2007-27, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

2. **Mangatinag, Rosemary:** The unit for this tenant was reinspected on May 11, 2007 and it passed the HQS inspection; however, the HQS inspector failed to fill in the deficiency report indicating that the deficiencies found on the unit were addressed and cured.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2007

U.S. Department of Housing and Urban Development
Special Tests and Provisions - Section 8 Housing Choice Vouchers
CFDA #14.871, Federal Award # TQ901
Federal Award Period 10/01/06 - 09/30/07

Finding No. 2007-28

Criteria: In accordance with CFR Part 24 Section 982.517 (c)(1), a PHA must review its schedule of utility allowances each year, and must revise its allowance for a utility category if there has been a change of 10 percent or more in the utility rate since the last time the utility allowance schedule was revised. The PHA must maintain information supporting its annual review of utility allowances and any revisions made in its utility allowance schedule.

Condition: During fiscal year 2007, the utility allowance was based on the fiscal year 2005 utility schedule. The utility allowance schedule was only revised subsequent to fiscal year 2007. However, we did not note any documentation of the annual review of the utility allowance schedule subsequent to fiscal year 2005 through fiscal year 2007.

Cause: The cause of the above condition is the lack of monitoring to ensure that the required annual review of the utility allowance schedule is performed.

Effect: The effect of the above condition is noncompliance with the provisions of CFR Part 24 Section 982.517(c)(1).

Recommendation: We recommend that NMHC implement monitoring procedures to ensure that the required annual review of the utility allowance schedule is being performed.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Kimo M. Rosario, NMHC Manager, Program & Housing

Corrective Action: At the time, the CUC surcharge, according to HUD Field Office Representative (Darlene Kaholokula), was not considered as a "rate increase." Nonetheless, NMHC has since provided a utility allowance schedule for fiscal year 2007.

Proposed Completion Date: Fiscal year 2009

COMMONWEALTH DEVELOPMENT AUTHORITY

Unresolved Prior Year Findings and Questioned Costs
Year Ended September 30, 2007

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, 2007:

| | |
|---------------------------------------------------|------------------|
| Questioned costs as previously reported | \$ 13,406 |
| Questioned costs of fiscal year 2007 Single Audit | <u>1,211</u> |
| Unresolved questioned costs at September 30, 2007 | \$ <u>14,617</u> |

Unresolved Findings

The status of unresolved findings is discussed in the Schedule of Findings and Questioned Costs section of this report (pages 9 through 47).



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, 2006:

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

- Finding No. 2006-1 - Not corrected. See corrective action plan to Finding No. 2007-1.
- Finding No. 2006-2 - Not corrected. See corrective action plan to Finding No. 2007-3.
- Finding No. 2006-3 - Not corrected. See corrective action plan to Finding No. 2007-4.
- Finding No. 2006-4 - Not corrected. See corrective action plan to Finding No. 2007-7.
- Finding No. 2006-5 - Corrective action was taken.
- Finding No. 2006-6 - Not corrected. See corrective action plan to Finding No. 2007-8.

FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS AUDIT

- Finding No. 2006-7 - Corrective action was taken.
- Finding No. 2006-8 - Not corrected. See corrective action plan to Finding No. 2007-16.
- Finding No. 2006-9 - Not corrected. See corrective action plan to Finding No. 2007-21.
- Finding No. 2006-10 - Not corrected. See corrective action plan to Finding No. 2007-22.