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

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2009 AND 2008

INDEPENDENT AUDITORS' REPORT

Board of Directors
Commonwealth Development Authority:

We have audited the accompanying statements of net assets of the Commonwealth Development Authority (CDA), a component unit of the Commonwealth of the Northern Mariana Islands (CNMI), as of September 30, 2009 and 2008, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of CDA's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Commonwealth Development Authority as of September 30, 2009 and 2008, and their changes in net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3 through 14 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board (GASB). This supplementary information is the responsibility of the Commonwealth Development Authority's management. We did not audit and do not express an opinion on such information. However, we have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. As a result of these limited procedures, we believe that the Management's Discussion and Analysis is not in conformity with guidelines established by GASB because it refers to components of CDA and not the basic financial statements and there is insufficient analysis of the basic financial statements.

Our audits were conducted for the purpose of forming an opinion on the Commonwealth Development Authority's basic financial statements. The Combining Statement of Net Assets, the Combining Statement of Revenues, Expenses and Changes in Net Assets and the Combining Statement of Cash Flows as of and for the year ended September 30, 2009 (pages 40 through 42) are presented for purposes of additional analysis and are not a required part of the basic financial statements. This supplementary information is the responsibility of the Commonwealth Development Authority's management. The Combining Statement of Net Assets, the Combining Statement of Revenues, Expenses and Changes in Net Assets and the Combining Statement of Cash Flows as of and for the year ended September 30, 2009 have been subjected to the auditing procedures applied by us in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 18, 2010, on our consideration of internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte & Touche LLC

October 18, 2010



COMMONWEALTH DEVELOPMENT AUTHORITY

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Management's Discussion and Analysis Year Ended September 30, 2009

The Management's Discussion and Analysis of the Commonwealth Development Authority's (CDA) financial performance provides an overview of CDA's financial activity for the fiscal year ended September 30, 2009, with selected comparative information for the fiscal years ended September 30, 2008 and 2007. Please read it in conjunction with the more detailed information contained within the accompanying financial statements.

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

DBD and DCD

DBD generally engages in government and public sector activities while DCD engages in private sector activities. Additionally, on December 1, 2000, CDA was given administrative authority for the Qualifying Certificate Program (QC). The QC is a tax incentive program to encourage new investment within the CNMI.

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

DCD's primary activity relates to the servicing of its direct loan portfolio. As of September 30, 2009, DCD's net loans receivable portfolio was \$12,857,958, which was a decrease of \$331,757 or 3% compared to 2008. As of September 30, 2008, DCD's net loans receivable portfolio was \$13,189,715, which was an increase of \$3,095,492 or 31% compared to the previous year. The cause of the decrease in fiscal year 2009 was due to the relative lack of new loans combined with normal principal reduction via scheduled payments. In fiscal year 2008, the increase was due to several large loans guaranteed by CDA with local banks that were called and subsequently included in DCD's loan portfolio.

DBD maintains a portfolio consisting of loans to various governmental and quasi-governmental agencies of the CNMI government. All of the loans are non-performing and have been fully allowed for. In fiscal year 2007, CDA's Board of Directors consented to a request from the Board of Directors of the Commonwealth Ports Authority to suspend interest payments for a period of two years and principal payments for a period of five years due to difficult financial circumstances. Because of this impairment management has agreed with the auditor's recommendation to fully allow for the principal and accrued interest.

DBD and DCD, Continued

Subsequent to the end of fiscal year 2008, CDA approved the proposed conversion of the Commonwealth Utilities Corporation (CUC) debt into preferred stock in CUC. At the end of fiscal year 2009, CUC's Executive Director, acting in place of the CUC Board of Directors per the Governor's Emergency Declaration, approved the conversion. See note 6 to the financial statements for more detailed information. This conversion will permit CUC to move ahead with greater flexibility in obtaining financing in the future and gives CDA a chance to recover some of the funds loaned CUC through dividends on the preferred stock.

Unfortunately, with the Asian economic crisis in the early 1990s and subsequent "Global Economic Crisis" beginning in late 2007, many of the projects financed by these loans have suffered significantly in value both as commercial enterprises and in terms of the fair market value of the loans' underlying assets and collateral. Events such as the attacks on 9/11, the SARS epidemic, the war in Iraq and sharp increases in fuel prices have had significant negative impacts on the CNMI's tourist-based economy. Local factors such as sharp increases in utility charges and the loss of the major tax base provided by the garment manufacturing industry only served to make weathering the external crises more difficult.

In 2004, the CNMI was swept by two major typhoons, Tingting and Chaba, devastating CDA-funded clients in the Marine and Agriculture loan categories. While these categories of loan are slowly recovering, there continues to be high delinquency rates.

As stated earlier, the net value of DCD's loan portfolio after (bad debts) recoveries was \$12,857,958 in 2009 and \$13,189,715 in 2008. Total (bad debts) recoveries were \$(796,207) and \$862,710 in 2009 and 2008, respectively. These figures represent the estimated potential loss of value of the loans and accrued interest for the respective fiscal years. The increase in bad debts in fiscal year 2009 was primarily due to continued deterioration in the collectability of the loan portfolio and its underlying collateral. The ultimate collection of the earned interest and the principal value of loans is DCD's biggest financial concern.

The Board of Directors has given management greater flexibility in pursuing solutions to the high delinquency rate among CDA borrowers and continues to emphasize the need to work with clients, or within the judicial system when necessary, to resolve delinquent loans.

In response to the difficulties experienced by virtually all of DCD's borrowers, management has been working on solutions that can benefit both CDA and the borrowers. One of the programs initiated was the Debt-Relief Program. Qualified borrowers are encouraged to restructure their delinquent loans at new, less-burdensome interest rates (typically 2%) and the accrued interest is set aside so that the new loan has a chance of being amortized if the new payment schedule is adhered to. This gives borrowers that were previously in seemingly hopeless situations, new hope for paying off their loans. While CDA may potentially lose some of the accrued interest that has been set aside, the reality is those sums would likely have never been recovered if the original loan terms had not been modified.

In cases where borrowers are in default and there is no workable solution for repayment of the loan, CDA has been forced to foreclose on properties that were collateralizing the loans or accept the properties through "deed in lieu of foreclosure". CDA then attempts to sell or lease these properties to recover as much of the loan principal as possible. Given the extremely depressed state of the real estate market in the CNMI, the values realized on foreclosed properties is often significantly less than the balance of the loan. In cases where CDA is unable to obtain a reasonable value for a foreclosed property, management may decide to defer disposal of the property until market conditions improve.

NMHC

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

NMHC, Continued

NMHC finalized the closing of Tottotville and forty-five houses are fully occupied and sold to respective homeowners. With the closure of the Expansion Project, NMHC is in the process of transferring infrastructure values to the Commonwealth Utilities Corporation (CUC) and the Department of Public Works. During fiscal year 2005, homeowners filed complaints with respect to the poor workmanship in the construction of their homes. The designer/construction manager and contractor for the subdivision have been contacted and all parties are addressing the areas of complaints. Mediation was also pursued; however, major issues being disputed are still unresolved by parties involved. Court hearings are ongoing with the latest held on January 5, 2010. In fiscal year 2009, NMHC settled with thirty-five of the forty-five homeowners and has filed a lawsuit against the contractor and the designer/construction manager.

Another major concern is Public Law (PL) 15-48 which Governor Benigno R. Fitial signed into law on March 13, 2007. This law repealed in its entirety, 2 CMC § 4486 and 4498, and amended 2 CMC §4497 to eliminate the moratorium extended to NMHC on the loan made to NMHC by the Marianas Public Land Trust (MPLT). PL 15-48 imposed serious financial burdens as NMHC was required to commence payment to MPLT. During fiscal year 2008, MPLT and NMHC finalized a portfolio transfer and resolved the financial burden imposed on NMHC.

Mortgage & Credit Division

The Mortgage & Credit Division is currently in the process of revamping the HOME Program policies and procedures so that the U.S. Department of Housing and Urban Development (HUD) regulations are properly addressed. The processing of rehabilitation and new construction loans for this specific program has been put on hold until the policies and procedures are in place and reviewed by HUD.

In June 2008, the Agreement Between the Parties, the U.S. Department of Agriculture (USDA) Rural Development (USDA RD) and the Northern Marianas Housing Corporation to Resolve Defaulted USDA Rural Development Loans was executed. This agreement has been established to outline the steps and mutually agreed-upon terms in liquidating defaulted USDA RD loans which NMHC agreed to act as trustee on deeds of trust securing USDA RD housing loans in the CNMI. The loans and properties covered by this agreement are accelerated accounts and accounts that are expected to be accelerated in the near future. This agreement encompasses forty-eight seriously delinquent loans.

On July 30, 2008, PL 110-289, or the Housing and Economic Recovery Act of 2008 (HERA), created the Neighborhood Stabilization Program (NSP). NSP is a HUD program which provides emergency assistance to state and local governments to acquire and redevelop foreclosed properties that might otherwise become sources of abandonment and blight within their respective communities. NSP provides grants to every state and local community to purchase foreclosed or abandoned homes and to rehabilitate, resale, or redevelop these homes in order to stabilize neighborhoods and stem the decline of house values of neighboring homes. NMHC intends to use the grant provided by this program to address the problems created by foreclosed and abandoned homes. Foreclosed homes will be acquired, rehabilitated, and resold to low income families.

Program and Housing Division

A. Saipan Housing Choice Voucher Program

In fiscal year 2009, the Housing Choice Voucher Program utilized 330 vouchers, fifty-three of which were given to applicants on the waiting list. In January 2009, the waiting list was closed due to the number of applicants on the list. Demand for the Housing Choice Voucher Program is high due to the portability of the program and the applicant's ability to select a unit in an area of their choice.

NMHC, Continued

Program and Housing Division, Continued

B. Saipan Multi-Family/New Construction Program

At the end of fiscal year 2009, Mihaville had forty-seven occupants of forty-eight units and Koblerville had thirty-two occupants of thirty-four units. Although Mihaville and Koblerville are almost at full capacity, there has been a turnover of tenants due to tenant requests to relocate. Both properties are well maintained and NMHC will continue its efforts to prepare for future REAC inspections.

C. Short-Term Goals

Goals of the Program and Housing Division are to a) maintain efforts to apply for additional rental vouchers by continuing to monitor HUD's Notices of Funding Availability (NOFA) and/or Super NOFAs for potential opportunities to increase its voucher count in the future; b) improve voucher management by addressing certain performance indicators to potentially increase its Section 8 Management Assessment Program Rating; c) increase customer satisfaction; and d) continue planning efforts towards the development and possible implementation of the Family Self-Sufficiency Program should the severe economic conditions begin to improve in the CNMI.

Rota Field Office

A. Rota Housing Choice Voucher Program

At the end of fiscal year 2009, twenty-five Housing Choice Vouchers (HCV) were utilized on Rota. This figure represents a five voucher decrease in the total number of vouchers utilized in the previous fiscal year, and is half of the total number of HCV (50) that were awarded by HUD to the island of Rota after Typhoon Pongsona. The demand for additional vouchers still exists, especially since qualified families prefer the HCV Program over the Multi-Family/New Construction Program for many reasons. The NMHC Rota Field Office receives numerous calls from interested families inquiring about the availability of vouchers. However, with the knowledge of the limited availability of vouchers and long waiting period, many qualified families choose not to go through the application process. Housing assistance to prospective tenants on the waiting list is on a first-come first-serve basis.

B. Rota Multi-Family/New Construction Program

The NMHC Rota Multi-Family/New Construction Program has been experiencing a low occupancy rate for several years. At the end of fiscal year 2009, eleven of thirty housing units at the Liyo' Housing Subdivision were occupied. This figure translates to a 36.66% occupancy rate. The low occupancy rate could be attributed to the following factors:

1. HCV Program

- a. The existence of the HCV Program has led to many qualified applicants for housing assistance wanting to apply for this program instead;
- b. Applicants qualified for housing assistance prefer the HCV Program because of the ability to choose a housing unit at a preferred location; and
- c. Housing units registered under the HCV Program are typically semi to fully furnished, unlike the housing units under the Multi-Family/New Construction Program.

NMHC, Continued

Rota Field Office, Continued

2. Condition of the Housing Units

- a. Safety concerns have been one of the biggest reasons why the NMHC Rota Field Office struggles to occupy the vacant units under the Multi-Family/New Construction Program. The housing units at the Liyo' Housing Subdivision have undergone and continue to undergo constant repairs due to hairline and severe cracks that are formed on the walls and ceilings due to the condition of rebar which have been slowly deteriorating because of moisture. Maintaining these units is costing NMHC significant amounts of money annually for materials and labor.

3. Utility Security Deposit

- a. Applicants find it very difficult to afford the security deposit required by CUC in order to connect to utilities. NMHC requires a receipt of payment for utility connection prior to moving in a tenant.

Despite the problems that exist within the Multi-Family/New Construction Program, efforts to increase the occupancy rate at the Liyo' Housing Subdivision are ongoing. The Rota Field Office advertises the vacant units and informs the general public of the housing assistance available to qualified applicants. Print advertisements and notices posted on the local television channel are some of the methods used to reach the public. Furthermore, constant repairs and maintenance are being conducted to ensure the units meet HUD's Uniform Physical Condition Standards so that NMHC may continue to provide housing assistance to families in need.

C. Short-Term Goals

The goal of the NMHC Rota Field Office is to increase the occupancy rate at the Liyo' Housing Subdivision. To attain this goal, NMHC must continue with the repairs and maintenance of the units and ultimately find a more adequate long-term solution to the deteriorating conditions. NMHC will have to provide additional amenities to clients, such as providing basic furniture (beds, dining tables, etc.), improving lighting, creating a community garden, providing a small playground or picnic grounds, etc., to attract qualified families. Finally, the NMHC Rota Field Office will continue to work with the Mayor's office and other agencies such as the Department of Community & Cultural Affairs and the Northern Marianas Protection & Advocacy Systems Inc. to promote and educate the local community about the housing assistance available through our Section 8 Program.

Tinian Field Office

A. Tinian Multi-Family/New Construction and Voucher Programs

1. The Tinian Multi-Family/New Construction Program has twenty units. All of the units are fully occupied; however, there is a turnover of tenants due to tenants obtaining employment and preferring to move into an inexpensive residence despite the condition. In the past, people have been reluctant to apply to the program, but with ongoing renovation and maintenance we have managed to keep these units occupied. In addition, people previously visualized the area as a "ghetto", but that outlook has changed.
2. There were five vouchers issued; however, only one is being utilized on Tinian and the other four were transferred to Saipan. There have been inquiries from Tinian students enrolled at the Northern Marianas College who have to relocate to Saipan. People are still encouraged to apply to the program even if there is a shortage of vouchers. This is one way for us to justify requesting for additional vouchers for Tinian. Some applicants request to be included on the waiting list for both programs.

NMHC, Continued

Tinian Field Office, Continued

B. Loans

1. The Tinian Field Office continues to work with applicants whose loans have been approved but not disbursed. There are also new applications for renovation or construction of new homes. The delay was due to changes to the HOME Program policies and procedures which were approved on July 23, 2009 and the additional requirement of environmental assessment on the properties.

One of the goals is to work with management and local leadership to address the needs of the new homesteaders. There were 475 homestead applicants that drew homestead properties in various areas around Tinian, however, the survey for these lots has not been completed.

Community Development Block Grants/Special Purpose Grants/Insular Areas (CDBG)

NMHC received \$1,528,092 in CDBG funding in fiscal year 2009. As stated in the Consolidated Plan, Community Development goals include the following:

- Infrastructure upgrades to provide basic services to the community and encourage economic development;
- Create an environment that is both functional and inviting to businesses, residents, and tourists;
- Provide support for limited clientele and community needs; and
- Promote community health, team work, and sportsmanship.

Because of limited funding in fiscal year 2009, NMHC allocated the entire CDBG grant amount to the following projects:

- Tinian Shelter/Tinian Public Library Public Service
- Garapan Central Market/Susupe Sports Complex
- Tinian Amphitheater Phase I
- Rota Walkway
- Paupau MRR/NMI Japan Cultural Center
- Tinian Amphitheater Phase II
- Susupe Sports Complex
- Marianas High School Building J
- Capitol Hill 1.0 MG Reservoir Rehabilitation

The above projects fulfill the aforementioned goals of promoting community health, team work, and sportsmanship and creating an environment that is both functional and inviting to businesses, residents, and tourists. Despite challenges along the way, such as environmental issues, NMHC continues to work with the CNMI Capital Improvement Projects Office and regulatory agencies to address any set-backs with regards to environmental assessment. NMHC is still working towards fulfilling its goals as stated in the Five-Year Consolidated Plan.

Emergency Shelter Grants Program (ESG)

NMHC received \$52,874 in ESG grants in fiscal year 2009. As in previous years, ESG has been allocated to the Guma Esperansa shelter and the Division of Youth Services (DYS) shelter. The Guma Esperansa shelter serves women and their children who are victims of domestic violence and human trafficking. The DYS Shelter serves youths who are victims of child abuse/neglect and are runaways. ESG funding is used to assist with the operational costs and essential services of both shelters.

**Combined Statements of Net Assets
As of September 30, 2009, 2008 and 2007**

	2009	2008	\$ Change	% Change	2007
Current assets	\$ 5,601,394	\$ 8,487,821	\$ (2,886,427)	-34%	\$ 12,188,230
Other assets	13,822,477	13,604,236	218,241	2%	21,729,620
Capital assets	14,308,503	14,231,597	76,906	1%	14,813,822
Noncurrent assets	<u>12,421,357</u>	<u>11,474,721</u>	<u>946,636</u>	8%	<u>14,550,106</u>
Total assets	\$ <u>46,153,731</u>	\$ <u>47,798,375</u>	\$ <u>(1,644,644)</u>	-3%	\$ <u>63,281,778</u>
Current liabilities	\$ 3,884,224	\$ 3,892,380	\$ (8,156)	-0%	\$ 11,098,399
Noncurrent liabilities	<u>5,705,221</u>	<u>6,079,863</u>	<u>(374,642)</u>	-6%	<u>14,955,840</u>
Total liabilities	<u>9,589,445</u>	<u>9,972,243</u>	<u>(382,798)</u>	-4%	<u>26,054,239</u>
Invested in capital assets	14,308,503	14,231,597	76,906	1%	14,813,822
Restricted	<u>22,255,783</u>	<u>23,594,535</u>	<u>(1,338,752)</u>	-6%	<u>22,413,717</u>
Total net assets	<u>36,564,286</u>	<u>37,826,132</u>	<u>(1,261,846)</u>	-3%	<u>37,227,539</u>
Total liabilities and net assets	\$ <u>46,153,731</u>	\$ <u>47,798,375</u>	\$ <u>(1,644,644)</u>	-3%	\$ <u>63,281,778</u>

**Combined Statements of Revenues, Expenses and Changes in Net Assets
As of September 30, 2009, 2008 and 2007**

	2009	2008	\$ Change	% Change	2007
Operating revenues	\$ 11,154,596	\$ 10,949,005	\$ 205,591	2%	\$ 11,406,911
Bad debts	<u>(1,205,618)</u>	<u>(3,069,279)</u>	<u>1,863,661</u>	-61%	<u>(3,476,736)</u>
Net operating revenues	9,948,978	7,879,726	2,069,252	26%	7,930,175
Operating expenses	<u>10,112,607</u>	<u>8,902,422</u>	<u>1,210,185</u>	14%	<u>14,525,243</u>
Operating loss	(163,629)	(1,022,696)	859,067	-84%	(6,595,068)
Total nonoperating revenues (expenses), net	<u>(237,245)</u>	<u>2,760,676</u>	<u>(2,997,921)</u>	-109%	<u>(239,336)</u>
(Loss) income before transfers	(400,874)	1,737,980	(2,138,854)	-123%	(6,834,404)
Transfers out for capital development grants	<u>(860,972)</u>	<u>(1,139,387)</u>	<u>278,415</u>	-24%	<u>(658,806)</u>
Change in net assets	(1,261,846)	598,593	(1,860,439)	-311%	(7,493,210)
Net assets - beginning	<u>37,826,132</u>	<u>37,227,539</u>	<u>598,593</u>	2%	<u>44,720,749</u>
Net assets - ending	\$ <u>36,564,286</u>	\$ <u>37,826,132</u>	\$ <u>(1,261,846)</u>	-3%	\$ <u>37,227,539</u>

**Combined Statements of Cash Flows
As of September 30, 2009, 2008 and 2007**

	2009	2008	\$ Change	% Change	2007
Cash flows from operating activities	\$ (1,571,290)	\$ 1,536,815	\$ (3,108,105)	-202%	\$ 3,645,783
Cash flows from capital and related financing activities	410,073	(9,481,244)	9,891,317	-104%	(967,081)
Cash flows from investing activities	<u>376,196</u>	<u>8,658,500</u>	<u>(8,282,304)</u>	-96%	<u>(2,103,461)</u>
Net (decrease) increase in cash and cash equivalents	(785,021)	714,071	(1,499,092)	-210%	575,241
Cash and cash equivalents at beginning of year	<u>3,001,746</u>	<u>2,287,675</u>	<u>714,071</u>	31%	<u>1,712,434</u>
Cash and cash equivalents at end of year	\$ <u>2,216,725</u>	\$ <u>3,001,746</u>	\$ <u>(785,021)</u>	-26%	\$ <u>2,287,675</u>

Condensed Comparative Statements of Revenues, Expenses and Changes in Net Assets

Development Banking Division
Years Ended September 30, 2009, 2008 and 2007

	2009	2008	\$ Change	% Change	2007
Operating revenues:					
Interest on fees and loans	\$ 130,386	\$ 152,497	\$ (22,111)	-14%	\$ 164,216
Interest on investments	137,577	270,045	(132,468)	-49%	383,016
Other	<u>1,200</u>	<u>25,368</u>	<u>(24,168)</u>	-95%	<u>2,402</u>
	269,163	447,910	(178,747)	-40%	549,634
Bad debts	<u>(290,200)</u>	<u>(1,710,440)</u>	<u>1,420,240</u>	-83%	<u>-</u>
Net operating revenues	<u>(21,037)</u>	<u>(1,262,530)</u>	<u>1,241,493</u>	-98%	<u>549,634</u>
Operating expenses:					
Professional fees	10,753	-	10,753	100%	-
Other	<u>156,251</u>	<u>23,692</u>	<u>132,559</u>	560%	<u>156,662</u>
Total operating expenses	<u>167,004</u>	<u>23,692</u>	<u>143,312</u>	605%	<u>156,662</u>
Operating income (loss)	<u>(188,041)</u>	<u>(1,286,222)</u>	<u>1,098,181</u>	-85%	<u>392,972</u>
Nonoperating revenues (expenses):					
Other income	259,794	218,572	41,222	19%	208,918
Interest expense	<u>(92,900)</u>	<u>(100,972)</u>	<u>8,072</u>	-8%	<u>(107,818)</u>
Total nonoperating revenues (expenses), net	<u>166,894</u>	<u>117,600</u>	<u>49,294</u>	42%	<u>101,100</u>
Income (loss) before transfers	(21,147)	(1,168,622)	1,147,475	-98%	494,072
Transfers out for capital development grants	<u>(860,972)</u>	<u>(1,139,387)</u>	<u>278,415</u>	-24%	<u>(658,806)</u>
Change in net assets	\$ <u>(882,119)</u>	\$ <u>(2,308,009)</u>	\$ <u>1,425,890</u>	-62%	\$ <u>(164,734)</u>

Development Corporation Division
Years Ended September 30, 2009, 2008 and 2007

	2009	2008	\$ Change	% Change	2007
Operating revenues:					
Interest and fees on loans	\$ 3,049,330	\$ 2,912,148	\$ 137,182	5%	\$ 3,217,211
Interest on investments	60,015	266,464	(206,449)	-77%	320,500
Other	<u>256,238</u>	<u>99,652</u>	<u>156,586</u>	157%	<u>284,614</u>
	3,365,583	3,278,264	87,319	3%	3,822,325
(Bad debts) recoveries	<u>(796,207)</u>	<u>862,710</u>	<u>(1,658,917)</u>	-192%	<u>(2,272,922)</u>
Net operating revenues	<u>2,569,376</u>	<u>4,140,974</u>	<u>(1,571,598)</u>	-38%	<u>1,549,403</u>
Operating expenses:					
Provision for loan guaranty	-	-	-	0%	5,429,690
Salaries and wages	434,591	414,088	20,503	5%	384,683
Depreciation	10,964	13,667	(2,703)	-20%	15,278
Provision for foreclosed real estate	575,889	935,106	(359,217)	-38%	628,663
Employee benefits	138,690	168,138	(29,448)	-18%	239,957
Professional fees	114,060	74,184	39,876	54%	166,649
Office rent	110,234	110,002	232	0%	118,527
Travel	64,479	59,675	4,804	8%	74,661
Other	<u>93,072</u>	<u>193,722</u>	<u>(100,650)</u>	-52%	<u>191,393</u>
Total operating expenses	<u>1,541,979</u>	<u>1,968,582</u>	<u>(426,603)</u>	-22%	<u>7,249,501</u>
Operating income (loss)	<u>1,027,397</u>	<u>2,172,392</u>	<u>(1,144,995)</u>	-53%	<u>(5,700,098)</u>

Condensed Comparative Statements of Revenues, Expenses and Changes in Net Assets, Continued

Development Corporation Division, Continued
Years Ended September 30, 2009, 2008 and 2007

	2009	2008	\$ Change	% Change	2007
Nonoperating revenues (expenses):					
Other income	-	20,000	(20,000)	-100%	-
Interest expense	(46,894)	-	(46,894)	100%	-
Other expense	<u>(11,520)</u>	<u>-</u>	<u>(11,520)</u>	100%	<u>-</u>
Total nonoperating revenues (expenses), net	<u>(58,414)</u>	<u>20,000</u>	<u>(78,414)</u>	-392%	<u>-</u>
Change in net assets	\$ <u>968,983</u>	\$ <u>2,192,392</u>	\$ <u>(1,223,409)</u>	-56%	\$ <u>(5,700,098)</u>

Northern Marianas Housing Corporation
Years Ended September 30, 2009 and 2008

	2009	2008	\$ Change	% Change
Operating revenues	\$ 7,675,423	\$ 7,222,831	\$ 452,592	6%
Bad debts	<u>(279,025)</u>	<u>(2,399,030)</u>	<u>2,120,005</u>	-88%
Net operating revenues	7,396,398	4,823,801	2,572,597	53%
Operating expenses	<u>8,559,197</u>	<u>6,910,148</u>	<u>1,649,049</u>	24%
Operating loss	(1,162,799)	(2,086,347)	923,548	-44%
Nonoperating revenues (expenses), net	<u>(345,725)</u>	<u>2,623,076</u>	<u>(2,968,801)</u>	-113%
Change in net assets	\$ <u>(1,508,524)</u>	\$ <u>536,729</u>	\$ <u>(2,045,253)</u>	-381%

Condensed Comparative Statements of Cash Flows

Development Banking Division
Years Ended September 30, 2009, 2008 and 2007

	2009	2008	\$ Change	% Change	2007
Cash flows from operating activities	\$ 120,521	\$ 496,694	\$ (376,173)	-76%	\$ 404,255
Cash flows from capital and related financing activities	1,363,752	(2,899,258)	4,263,010	-147%	34,859
Cash flows from investing activities	<u>(1,484,273)</u>	<u>2,402,564</u>	<u>(3,886,837)</u>	-162%	<u>(439,114)</u>
Net increase in cash and cash equivalents	-	-	-	0%	-
Cash and cash equivalents at beginning of year	<u>-</u>	<u>-</u>	<u>-</u>	0%	<u>-</u>
Cash and cash equivalents at end of year	\$ <u>-</u>	\$ <u>-</u>	\$ <u>-</u>	0%	\$ <u>-</u>

Development Corporation Division
Years Ended September 30, 2009, 2008 and 2007

	2009	2008	\$ Change	% Change	2007
Cash flows from operating activities	\$ (363,186)	\$ 703,237	\$ (1,066,423)	-152%	\$ 2,302,143
Cash flows from capital and related financing activities	(718,604)	(5,091,559)	4,372,955	-86%	(1,427,589)
Cash flows from investing activities	<u>492,992</u>	<u>4,843,564</u>	<u>(4,350,572)</u>	-90%	<u>(852,586)</u>
Net (decrease) increase in cash and cash equivalents	(588,798)	455,242	(1,044,040)	-229%	21,968
Cash and cash equivalents at beginning of year	<u>1,701,162</u>	<u>1,245,920</u>	<u>455,242</u>	37%	<u>1,223,952</u>
Cash and cash equivalents at end of year	\$ <u>1,112,364</u>	\$ <u>1,701,162</u>	\$ <u>(588,798)</u>	-35%	\$ <u>1,245,920</u>

Condensed Comparative Statements of Cash Flows, Continued

Northern Marianas Housing Corporation
Years Ended September 30, 2009 and 2008

	2009	2008	\$ Change	% Change
Cash flows from operating activities	\$ (1,328,625)	\$ 336,884	\$ (1,665,509)	-494%
Cash flows from capital and related financing activities	(235,075)	(1,490,427)	1,255,352	-84%
Cash flows from investing activities	<u>1,367,477</u>	<u>1,412,372</u>	<u>(44,895)</u>	-3%
Net (decrease) increase in cash and cash equivalents	(196,223)	258,829	(455,052)	-176%
Cash and cash equivalents at beginning of year	<u>1,300,584</u>	<u>1,041,755</u>	<u>258,829</u>	25%
Cash and cash equivalents at end of year	\$ <u>1,104,361</u>	\$ <u>1,300,584</u>	\$ <u>(196,223)</u>	-15%

FINANCIAL HIGHLIGHTS

DBD and DCD

- In 2009, DCD had net operating revenues of \$2,569,376 while DBD had a loss of \$21,037. A significant part of net operating revenues is comprised of bad debts. DCD recorded bad debts expense of \$796,207 in 2009 compared with a recovery of bad debts of \$862,710 in 2008. DBD saw an additional \$290,200 charged to bad debts in 2009 which brought the allowance for its loans to 100% of the principal. Interest and fees earned on loans for DCD for the year increased by \$137,182, or 5%. DBD had a decrease of \$22,111, or 14%, compared to 2008.
- Another area of concern is the decrease in earnings on investments suffered by each division as interest rates on short-term investments hover near zero. DCD's invested funds decreased from \$2,835,938 at September 30, 2008 to \$641,050 at September 30, 2009, a decrease of \$2,194,888, or 77%. Related earnings on investments decreased from \$266,464 for the year ended September 30, 2008 to \$60,015 for the year ended September 30, 2009, a decrease of \$206,449, or 77%. DBD's invested funds increased by \$1,133,283, or 17%, from \$6,550,922 at September 30, 2008 to \$7,684,205 at September 30, 2009. Earnings on these investments decreased from \$270,045 for the year ended September 30, 2008 to \$137,577 for the year ended September 30, 2009, a decrease of \$132,468, or 49%. The increase in DBD's investments and decrease in DCD's investments in fiscal year 2009 reflect liquidity provided by DBD to DCD in fiscal 2008 to pay off loan guarantees called by several banks, and the subsequent repayment of the borrowings with longer-term time certificates of deposit held by DCD that matured in fiscal 2009. CDA's management must keep these negative trends in mind when creating budgets and making commitments for its limited funds.
- In fiscal year 2009, operating expenses for DCD, omitting the provisions for loan guaranty and foreclosed real estate, decreased by \$67,386, or 7%, from 2008. DBD's operating expenses increased by \$143,312 over fiscal year 2008 as DCD recouped expenses charged for DBD operations for both fiscal years 2008 and 2009. CDA is placing increasing emphasis on reducing expenses in order to reach a positive cash flow from operations.
- As noted above, DCD's bad debts and the provisions for loan guaranty and foreclosed real estate losses continue to be highly volatile and reflect a negative trend. Only through renewed efforts by CDA to work with loan clients finding innovative ways to restore their loans to "performing" status and to pursue realization of value from collateralizing assets for loans that have no hope of recovery can this trend be reversed.
- The above changes resulted in a decrease of the combined net assets of CDA by \$1,261,846, or 3%, from 2008 to 2009.

FINANCIAL HIGHLIGHTS, CONTINUED

NMHC

- Total assets decreased by 9% from \$21,420,983 in fiscal year 2008 to \$19,407,494 in fiscal year 2009 mainly due to housing assistance payments (HAP) equity being utilized to fund the deficiency in revenues received from the grantor over actual HAP payments made for fiscal year 2009. In addition, all disaster vouchers from Typhoons Tingting and Chaba were converted to regular vouchers bringing the total to 363 voucher units that NMHC now administers and monitors for compliance.
- Total liabilities decreased by 6% from \$7,932,161 in fiscal year 2008 to \$7,427,196 in fiscal year 2009 and total net assets decreased by 11% from \$13,488,822 in fiscal year 2008 to \$11,980,298 in fiscal year 2009.
- Net operating revenues increased by 53% from \$4,823,801 in fiscal year 2008 to \$7,396,398 in fiscal year 2009. A significant component of this change is bad debts, which decreased by 88% from \$2,399,030 in fiscal year 2008 to \$279,025 in fiscal year 2009.
- Total operating expenses increased by 24% from \$6,910,148 in fiscal year 2008 to \$8,559,197 in fiscal year 2009. The increase is primarily attributable to the provision for loan guaranty and - increases in Section 8 rental expenses, repairs and maintenance, salaries and wages, utilities, travel and ESG Program Grant expenses.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At September 30, 2009 and 2008, CDA had \$14,308,503 and \$14,231,597, respectively, invested in capital assets, net of depreciation where applicable. This represents a net increase of \$76,906, or 1%, during fiscal year 2009.

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Property and equipment, net	\$ 1,968,305	\$ 2,303,333	\$ 2,703,108
Land	9,747,313	9,650,313	10,409,682
Foreclosed real estate	<u>2,592,885</u>	<u>2,277,951</u>	<u>1,701,032</u>
	<u>\$ 14,308,503</u>	<u>\$ 14,231,597</u>	<u>\$ 14,813,822</u>

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

Long-Term Debt

At September 30, 2009 and 2008, CDA had \$1,374,243 and \$1,494,243, respectively, in long-term debt outstanding. At September 30, 2009 and 2008, NMHC had \$510,656 in long-term debt outstanding. See notes 5 and 9 to the financial statements for more detailed information on CDA's long-term debt and changes therein.

ECONOMIC OUTLOOK

DBD and DCD

CDA is being affected by the negative economic forces at play globally as well as locally. If the recent trend in the performance of CDA's assets were to continue, a question of CDA's viability to continue operating as an independent entity must be addressed. CDA is currently not able to fund its ongoing operations from earnings generated by the loan portfolio and investments and must use its cash reserves to cover this shortfall. The budget for fiscal year 2010 also reflects a significant shortfall. Management has begun to recognize this situation and to address it. As mentioned above, management is continuing the "Debt-Relief Program" to bring qualified borrowers from a delinquent, non-paying status to a performing, paying status. The "price" to CDA of this program is to reduce the rate of interest on these loans to 2%, a rate that does not go far in generating income for CDA. However, management believes that if enough of the delinquent borrowers see hope for paying off their loans and preserve their collateral they will begin to make regular payments. Once these payments are added back to the loan fund and re-lent to qualified borrowers the interest earned will rise to a point where CDA can operate "in the black." Of course, beyond these revenue-side enhancements, management is pursuing meaningful expense reductions.

While there is no simple solution to reverse the deterioration of CDA's loan portfolio, CDA believes there is still time and are still steps that can be taken to improve the likelihood of CDA's continuing existence as a contributing member of the CNMI Government and be a beneficial part of the economy of the CNMI.

NMHC

NMHC's CDBG grant allocation was reduced by \$506,421 for FY 2009 resulting in a CDBG administrative loss of \$101,284. This is due to a HUD funding reduction. NMHC has a five-year plan for all community planning and development programs and is committed to its current allocations. NMHC will lower expenses following the cost reduction approach in the future. With regards to the Section 8 Multifamily project on Rota, the revenue will decrease due to the thirty-three percent occupancy rate, which resulted in applicants relocating to the U.S. mainland to look for better opportunities and make additional income for their families. This will result in another decrease of revenue in the amount of \$215,000.

The CNMI's economic outlook continues to be uncertain. Austerity measures continue to be in effect government wide in fiscal year 2010 to compensate for decreased revenues. The tourism industry and the garment industry, which played material roles in driving the CNMI's economy, have been in decline for a number of years. A series of unfortunate events hindered the return of tourist arrival levels to that enjoyed in the 1990's and thus the industry and the economy continue to suffer. Tourism overall appears to be on the rebound and partially stabilized. The garment industry has declined almost entirely, compounding the CNMI's economic woes. While several efforts are underway to look at alternative industries to revive the economy no immediate appreciable growth is anticipated in the foreseeable future.

As a result of the dwindling resources available for NMHC, the budget of federal funds will also be affected and is expected to decrease until recovery. As such, NMHC continues to apply the cost reduction approach to lower the deficit for every fiscal year. NMHC continues to take internal measures to ensure that this would not result in a deficit. The continuing economic challenges may result in further budget reductions in fiscal year 2011 but NMHC has mechanisms in place to closely monitor such actions and is actively pursuing alternative funding opportunities to compensate for reductions in the traditional sources of funding.

CONTACTING CDA'S AND NMHC'S MANAGEMENT

This financial report is designed to provide a general overview of CDA's financial condition and to demonstrate its accountability for monies received. The Management's Discussion and Analysis for the year ended September 30, 2008 is set forth in the report on the audit of CDA's financial statements which is dated May 7, 2010. That Discussion and Analysis explains the major factors impacting the 2008 financial statements. If you have questions about this report or the 2008 or 2007 reports or need additional financial information, contact Mr. Stuart Smith, CDA Comptroller, P.O. Box 502149, Saipan, MP 96950-2149, or call (670) 234-7145/6293 or send email to executive@cda.gov.mp or Mr. Joshua T. Sasamoto, NMHC Corporate Director, P.O. Box 500514, Saipan, MP 96950-0514, or call (670) 234-6866/9447 or send email to jtsasamoto@nmhc.gov.mp.

COMMONWEALTH DEVELOPMENT AUTHORITY

Statements of Net Assets
September 30, 2009 and 2008

<u>ASSETS</u>	<u>2009</u>	<u>2008</u>
Current assets:		
Cash and cash equivalents	\$ 2,216,725	\$ 3,001,746
Time certificates of deposit	-	579,448
Receivables:		
Current portion of loans receivable, net	2,644,196	4,521,475
Rent, net	89,142	72,323
Accrued interest, net of allowance for doubtful accounts of \$24,688,477 and \$15,788,934 as of September 30, 2009 and 2008, respectively	482,925	161,456
Other, net	145,241	123,919
Prepaid expenses	23,165	27,454
Total current assets	<u>5,601,394</u>	<u>8,487,821</u>
Other assets:		
Cash and cash equivalents, restricted	5,497,222	4,796,824
Time certificates of deposit, restricted	8,325,255	8,807,412
Total other assets	<u>13,822,477</u>	<u>13,604,236</u>
Noncurrent assets:		
Loans receivable, net	12,421,357	11,474,721
Property and equipment, net	1,968,305	2,303,333
Land	9,747,313	9,650,313
Foreclosed real estate	2,592,885	2,277,951
Total noncurrent assets	<u>26,729,860</u>	<u>25,706,318</u>
	<u>\$ 46,153,731</u>	<u>\$ 47,798,375</u>
<u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Current installment of note payable to related party	\$ 122,100	\$ 111,754
Accounts payable and accrued expenses	977,932	1,180,922
Due to related party	387,488	-
Deferred revenues	11,002	14,020
Due to grantor agency	783,795	1,756,057
Reserve for loan guaranty	1,601,907	829,627
Total current liabilities	<u>3,884,224</u>	<u>3,892,380</u>
Note payable to related party, net of current installments	1,252,143	1,382,489
Deferred revenues, net of current portion	4,453,078	4,697,374
Total liabilities	<u>9,589,445</u>	<u>9,972,243</u>
Commitments and contingencies		
Net assets:		
Invested in capital assets	14,308,503	14,231,597
Restricted	22,255,783	23,594,535
Total net assets	<u>36,564,286</u>	<u>37,826,132</u>
	<u>\$ 46,153,731</u>	<u>\$ 47,798,375</u>

See accompanying notes to financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Operating revenues:		
Interest and fees on loans	\$ 3,689,485	\$ 3,935,370
Section 8 income:		
Federal housing assistance rentals	4,964,888	3,748,003
Tenant share	81,547	115,430
Interest on investments	197,592	536,509
HOME Investment Partnership Program grants	-	48,073
CDBG Program Grant	1,528,092	2,345,446
ESG Program Grant	52,874	28,213
Other	640,118	191,961
	<u>11,154,596</u>	<u>10,949,005</u>
Bad debts	<u>(1,205,618)</u>	<u>(3,069,279)</u>
Net operating revenues	<u>9,948,978</u>	<u>7,879,726</u>
Operating expenses:		
Section 8 rental	3,406,966	2,370,234
CDBG Program Grant	1,528,092	2,345,446
Salaries and wages	1,016,147	954,511
Repairs and maintenance	942,372	302,559
Provision for loan guaranty	772,280	-
Provision for foreclosed real estate	575,889	935,106
Depreciation	406,602	447,377
Employee benefits	322,691	353,239
Utilities	318,942	271,340
Professional fees	264,914	261,374
Travel	162,670	103,628
Office rent	114,473	118,402
HOME Investment Partnership Program grants	-	48,073
ESG Program Grant	52,435	28,213
Other	228,134	362,920
Total operating expenses	<u>10,112,607</u>	<u>8,902,422</u>
Operating loss	<u>(163,629)</u>	<u>(1,022,696)</u>
Nonoperating revenues (expenses):		
Gain on settlement with MPLT	-	3,340,823
Settlement expense	(286,062)	-
Other income	212,900	238,572
Interest income	14,989	34,442
Impairment loss on land	-	(620,869)
Interest expense	(93,440)	(198,942)
Other expense	(85,632)	(33,350)
Total nonoperating revenues (expenses), net	<u>(237,245)</u>	<u>2,760,676</u>
(Loss) income before transfers	<u>(400,874)</u>	<u>1,737,980</u>
Transfers out for capital development grants	<u>(860,972)</u>	<u>(1,139,387)</u>
Change in net assets	<u>(1,261,846)</u>	<u>598,593</u>
Net assets - beginning	<u>37,826,132</u>	<u>37,227,539</u>
Net assets - ending	<u>\$ 36,564,286</u>	<u>\$ 37,826,132</u>

See accompanying notes to financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

Statements of Cash Flows
Years Ended September 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Cash flows from operating activities:		
Cash received from interest and fees on loans receivable	\$ 724,324	\$ 2,059,066
Cash received from interest and fees on capital development loans	-	162,743
Interest and dividends on investments	236,349	641,258
Cash payments to suppliers for goods and services	(1,238,258)	(789,389)
Cash received from customers	576,715	(107,772)
Cash payments to employees for services	(1,156,562)	(1,122,649)
Cash received from federal grant awards	5,573,592	6,603,865
Cash payments from federal grant awards	<u>(6,287,450)</u>	<u>(5,910,307)</u>
Net cash (used for) provided by operating activities	<u>(1,571,290)</u>	<u>1,536,815</u>
Cash flows from capital and related financing activities:		
Acquisition of property and equipment	(71,574)	(47,602)
Acquisition of land	(97,000)	-
Proceeds from sale of land	-	100,000
Net receipts (disbursements) of loans receivable	1,424,365	(1,153,974)
Net proceeds of capital development loans receivables	-	109,409
Proceeds from sale of foreclosed properties	-	105,000
Payments to MPLT	-	(2,025,000)
Interest paid on notes payable	(540)	-
Payments for claims and settlements	(286,062)	-
Payments for guaranteed loans	(74,112)	(5,429,690)
Payments received on capital development loans	-	-
Transfers for capital development grants	<u>(485,004)</u>	<u>(1,139,387)</u>
Net cash provided by (used for) capital and related financing activities	<u>410,073</u>	<u>(9,481,244)</u>
Cash flows from investing activities:		
Net proceeds from restricted cash and cash equivalents and time certificates of deposit	361,207	8,624,058
Interest received	<u>14,989</u>	<u>34,442</u>
Net cash provided by investing activities	<u>376,196</u>	<u>8,658,500</u>
Net (decrease) increase in cash and cash equivalents	(785,021)	714,071
Cash and cash equivalents at beginning of year	<u>3,001,746</u>	<u>2,287,675</u>
Cash and cash equivalents at end of year	<u>\$ 2,216,725</u>	<u>\$ 3,001,746</u>
Reconciliation of operating loss to net cash (used for) provided by operating activities:		
Operating loss	\$ (163,629)	\$ (1,022,696)
Adjustments to reconcile operating loss to net cash (used for) provided by operating activities:		
Bad debts	1,205,618	3,069,279
Provision for loan guaranty	772,280	-
Provision for foreclosed real estate	575,889	935,106
Depreciation	406,602	447,377
(Increase) decrease in assets:		
Receivables:		
Rent	(81,589)	(51,400)
Other	(50,896)	(349,743)
Accrued interest	(2,926,404)	(1,608,812)
Prepaid expenses	4,289	(21,466)
Increase (decrease) in liabilities:		
Accounts payable and accrued expenses	(202,990)	(280,940)
Deferred revenues	(138,198)	(14,020)
Due to grantor agency	<u>(972,262)</u>	<u>434,130</u>
Net cash (used for) provided by operating activities	<u>\$ (1,571,290)</u>	<u>\$ 1,536,815</u>

See accompanying notes to financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

Statements of Cash Flows, Continued
Years Ended September 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Supplemental disclosure of noncash capital and related financing activities:		
Recognition of foreclosed properties:		
Noncash increase in foreclosed real estate	\$ 948,823	\$ 1,513,606
Noncash decrease in loans receivable	(948,823)	(1,513,606)
	<u>\$ -</u>	<u>\$ -</u>
Settlement agreement with MPLT:		
Noncash decrease in notes payable to related party	\$ -	\$ 8,996,623
Noncash decrease in interest payable	-	1,927,030
Noncash interest expense	-	97,970
Noncash decrease in loans receivables	-	(9,142,426)
Write-off of allowance for loan losses	-	3,660,578
Noncash decrease in interest receivables	-	(1,479,469)
Write-off of allowance for uncollectible interests	-	1,305,517
Cash payment to MPLT	-	(2,025,000)
Noncash gain on settlement with MPLT	-	(3,340,823)
	<u>\$ -</u>	<u>\$ -</u>
Loan restructuring:		
Noncash increase in loans receivable	\$ 724,689	\$ -
Noncash decrease in accrued interest	(719,409)	-
Noncash decrease in other receivables	(5,280)	-
	<u>\$ -</u>	<u>\$ -</u>
Loan payable to MPLT:		
Noncash decrease in note payable to related party	\$ 120,000	\$ -
Noncash interest expense	92,900	-
Noncash other income	(212,900)	-
	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(1) Reporting Entity

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

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

Development Banking Division:

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

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

Development Corporation Division:

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

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(1) Reporting Entity, Continued

Development Corporation Division, Continued:

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

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

Northern Marianas Housing Corporation:

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

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

(2) Summary of Significant Accounting Policies

The accounting policies of CDA conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities, specifically proprietary funds. Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. CDA has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

Basis of Accounting

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

Budgets

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

Cash and Cash Equivalents and Time Certificates of Deposit

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

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

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, CDA's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. CDA does not have a deposit policy for custodial credit risk.

For purposes of the statements of net assets and cash flows, cash and cash equivalents is defined as cash held in demand deposits, savings and unrestricted time certificates of deposit with a maturity date within three months of the date acquired. Deposits maintained in time certificates of deposit with original maturity dates greater than ninety days are separately classified. At September 30, 2009 and 2008, total cash and cash equivalents and time certificates of deposit were \$16,039,202 and \$17,185,430, respectively, and the corresponding bank balances were \$16,594,050 and \$17,333,025, respectively. Of the bank balance amounts, \$16,594,050 and \$17,333,025 are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance as of September 30, 2009 and 2008, respectively. Bank deposits in the amount of \$842,382 and \$397,476 were FDIC insured as of September 30, 2009 and 2008, respectively. CNMI law does not require component units to collateralize their bank accounts and thus CDA's deposits in excess of FDIC insurance are uncollateralized. Accordingly, the deposits are exposed to custodial credit risk.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

Prepaid Expenses

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

Property and Equipment

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

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

Land

Land is recorded at fair market value at the date of acquisition. Valuations are periodically performed by management and adjustments are made to reflect the land at the lower of the carrying amount or fair market value. The carrying amount of land is evaluated on an annual basis to determine impairment by estimating the recoverable value. Recoverable value is based on management's historical knowledge and changes in market conditions from the time of valuation. An impairment loss is recognized in the period in which it arises. For the fiscal years ended September 30, 2009 and 2008, NMHC recorded impairment loss on land of \$0- and \$620,869, respectively.

Foreclosed Real Estate

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

Loans Receivable, Interest Receivable and Allowance for Loan Losses

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

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

Restricted Cash and Cash Equivalents and Time Certificates of Deposit

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

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

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

Revenue Recognition

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

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

Federal grant revenues are recognized when allowable expenses are incurred.

Non-operating revenues result from capital and financing activities.

Deferred Revenues

Deferred revenue is recognized when cash, receivables or other assets are recorded prior to their being earned. Deferred revenues include prepaid lease income on foreclosed real estate held for lease and recorded loans receivable from individuals eligible under the HOME Investment Partnerships program administered by NMHC.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

Compensated Absences

Vested or accumulated vacation leave is recorded as benefits accrue to employees. No liability is recorded for nonvesting rights to receive sick pay benefits. Accumulated sick pay benefits as of September 30, 2009 and 2008 was approximately \$198,305 and \$184,792, respectively.

Retirement Plan

CDA contributes to the Northern Mariana Islands Retirement Fund's (the Fund) defined benefit plan (DB Plan) and defined contribution plan (DC Plan), a cost sharing, and multi-employer plan (the Plan) established and administered by the CNMI.

The Plan provides retirement, security and other benefits to employees, and their spouses and dependents, of the CNMI Government and CNMI agencies, instrumentalities and public corporations. Benefits are based on the average annual salary of the beneficiary over the term of credited service. Public Law No. 6-17, the Northern Mariana Islands Retirement Fund Act of 1988, is the authority under which benefit provisions are established. Public Law No. 6-17 was subsequently amended by Public Law Nos. 6-41, 8-24, 8-30, 8-31, 8-39, 9-25, 9-45, 10-8, 10-19 and 11-9.

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

The Fund issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the Northern Mariana Islands Retirement Fund, P.O. Box 501247, Saipan, MP, 96950-1247.

Defined Benefit Plan (DB Plan)

DB Plan members are required to contribute 6.5% and 9% of their annual covered salary for Class I and Class II members, respectively. On June 14, 2007, Public Law No. 15-70 was enacted to amend the NMIRF Act to improve the DB Plan's fiscal solvency. Public Law No. 15-70 provides for increasing employee contributions to the DB Plan by 1% per year beginning in fiscal year 2008 until reaching 10.5% for Class I members and 11% for Class II members. CDA is required to contribute at an actuarially determined rate. The actuarially determined contribution rate for the fiscal year ended September 30, 2008 is 29.9665% of covered payroll based on an actuarial valuation as of October 1, 2007 issued in December 2008. The actuarially determined contribution rate for the fiscal year ended September 30, 2009 has not been determined. The established statutory rate at September 30, 2009 and 2008 is 36.6667% of covered payroll.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

Defined Contribution Plan (DC Plan)

On June 16, 2006, Public Law No. 15-13 was enacted which created the DC Plan, a multi-employer pension plan and is the single retirement program for all employees whose first time CNMI government employment commences on or after January 1, 2007. Each member of the DC Plan is required to contribute to the member's individual account an amount equal to 10% of the member's compensation. CDA is required to contribute to each member's individual account an amount equal to 4% of the member's compensation. The DC Plan by its nature is fully funded on a current basis from employer and member contributions.

CDA's contributions to the Fund for the years ended September 30, 2009, 2008 and 2007 were \$263,263, \$266,396 and \$409,185, respectively, which were equal to the required contributions for each year.

Net Assets

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

- Invested in capital assets; capital assets, net of accumulated depreciation.
- Restricted:
 - Nonexpendable - Net assets subject to externally imposed stipulations that CDA maintain them permanently. At September 30, 2009 and 2008, CDA does not have nonexpendable net assets.
 - Expendable - Net assets whose use by CDA is subject to externally imposed stipulations that can be fulfilled by actions of CDA pursuant to those stipulations or that expire by the passage of time. As described in note 1, CDA considers all assets, except investments in capital assets, to be restricted for economic development.
- Unrestricted; net assets that are not subject to externally imposed stipulations. As CDA considers all assets, except investments in capital assets, to be restricted for economic development, CDA does not have unrestricted net assets of September 30, 2009 and 2008.

New Accounting Standards

During fiscal year 2009, CDA implemented the following pronouncements:

- GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, which provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

- GASB Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*, which improves the quality of financial reporting by requiring endowments to report their land and other real estate investments at fair value, creating consistency in reporting among similar entities that exist to invest resources for the purpose of generating income.
- GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which improves financial reporting by contributing to the GASB's efforts to codify all GAAP for state and local governments so that they derive from a single source.
- GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*, which incorporates accounting and financial reporting guidance previously only contained in the American Institute of Certified Public Accountants (AICPA) auditing literature into the GASB's accounting and financial reporting literature for state and local governments, and addresses three issues from the AICPA's literature - related party transactions, going concern considerations, and subsequent events.

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

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

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which is intended to improve how state and local governments report information about derivative instruments - financial arrangements used by governments to manage specific risks or make investments - in their financial statements. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of CDA.

In December 2008, GASB issued Technical Bulletin No. 2008-1, *Determining the Annual Required Contribution Adjustment for Postemployment Benefits*, which clarifies the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, for calculating the annual required contribution (ARC) adjustment. The provisions of this statement are effective for periods beginning after December 15, 2008. Management does not believe that the implementation of this statement will have a material effect on the financial statements of CDA.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In March 2009, GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The provisions of this statement are effective for periods beginning after June 15, 2010. Management does not believe that the implementation of this statement will have a material effect on the financial statements of CDA.

Off-Balance Sheet Financial Instruments

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

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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

Development Banking Division

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

At September 30, 2009 and 2008, restricted cash and cash equivalents and time certificates of deposit amounting to \$8,088,925 and \$6,604,652, respectively, consist of time certificates of deposit with maturity periods ranging from seven to sixteen months and amounts held in demand deposit accounts. These investments are presented at fair value in the accompanying financial statements, in accordance with GASB Statement No. 31.

Development Corporation Division

At September 30, 2009 and 2008, restricted cash and cash equivalents and time certificates of deposit consist of time certificates of deposit with maturity periods ranging from six to nine months and amounts held in demand deposit accounts. Restricted cash and cash equivalents and time certificates of deposit amounted to \$2,342,946 and \$2,256,490 at September 30, 2009 and 2008, respectively, and comprise amounts maintained as a guarantee against loans issued by the bank and for loan activities. These investments are presented at fair value in the accompanying financial statements in accordance with GASB Statement No. 31.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

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

Northern Marianas Housing Corporation

NMHC maintains depository accounts with financial institutions in the CNMI which are restricted for various purposes, as detailed below. At September 30, 2009 and 2008, restricted cash and cash equivalents consist of amounts held in demand deposit accounts and time certificates of deposit with sixty days maturity.

	<u>2009</u>	<u>2008</u>
<u>Restricted cash and cash equivalents:</u>		
Escrow account maintained as a guarantee for any deficiency in foreclosure proceeds related to USDA Rural Development loans, including \$1,521,923 restricted for forty-eight seriously delinquent guaranteed loans	\$ 2,163,848	\$ 2,223,115
Savings account restricted for Koblerville Section 8 project repairs and maintenance expenses, per contract with the U.S. Department of Housing and Urban Development	197,214	196,819
Savings account maintained as a guarantee of housing loans made by a savings and loan in the CNMI	26,430	58,851
Checking account maintained for Section 8 Housing Choice Vouchers Program expenses	832,543	2,028,317
Other depository accounts reserved for various purposes	<u>170,571</u>	<u>235,992</u>
	<u>\$ 3,390,606</u>	<u>\$ 4,743,094</u>

CDA's investments in time certificates of deposit had the following maturities at September 30, 2009:

	<u>Fair Value</u>	<u>Investment Maturities (In Years)</u>			
		<u>Less Than 1</u>	<u>1 - 5</u>	<u>6 - 10</u>	<u>More Than 10</u>
DBD	\$ 7,684,205	\$ 7,175,981	\$ 508,224	\$ -	\$ -
DCD	<u>641,050</u>	<u>641,050</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ 8,325,255</u>	<u>\$ 7,817,031</u>	<u>\$ 508,224</u>	<u>\$ -</u>	<u>\$ -</u>

(4) Loans Receivable

Development Corporation Division

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

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(4) Loans Receivable

Development Corporation Division, Continued

Outstanding loans are due within various periods not to exceed thirty (30) years. The interest rates charged are based on the economic purpose of the loan. Production development loans bear interest at 7% to 9%, marine and agriculture loans bear interest at 4.5%, commercial development loans bear interest at 7% to 9%, and microloans bear interest at 7% to 12%. In October 2007, CDA initiated a "Debt Relief Program" (the Program) to address increasing delinquent loans. The Program provides for reduction of interest to two percent and extension of term up to thirty years with a mandated three year callable provision where warranted and justified.

Northern Marianas Housing Corporation

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

Major classifications of economic development loans as of September 30, 2009 and 2008 (with combining information as of September 30, 2009), are as follows:

	Development Corporation Division	Northern Marianas Housing Corporation	2009	2008
General	\$ 29,439,681	\$ 753,345	\$ 30,193,026	\$ 32,755,724
Direct family home loans	-	3,122,978	3,122,978	3,187,107
Marine	4,782,096	-	4,782,096	5,560,903
Agriculture	2,458,593	-	2,458,593	2,562,530
HOME Investment Partnerships Act grant	-	3,632,866	3,632,866	3,807,611
Housing construction	-	453,397	453,397	461,014
Tinian turnkey	-	531,440	531,440	498,040
Home revenue bond	-	80,370	80,370	80,370
Section 8	-	166,063	166,063	167,943
Housing preservation grant	-	33,020	33,020	59,173
Trust Territory Guaranteed	1,484	-	1,484	4,764
Loan principal receivable	36,681,854	8,773,479	45,455,333	49,145,179
Less allowance for loan losses	(23,823,896)	(6,565,884)	(30,389,780)	(33,148,983)
Net loans receivable	<u>\$ 12,857,958</u>	<u>\$ 2,207,595</u>	<u>\$ 15,065,553</u>	<u>\$ 15,996,196</u>

Maturities of the above principal balances subsequent to September 30, 2009, will be as follows:

	Development Corporation Division	Northern Marianas Housing Corporation	Total
Fully matured and others	\$ 23,448,735	\$ 537,815	\$ 23,986,550
1 - 6 months	418,013	65,275	483,288
7 - 18 months	821,792	117,431	939,223
19 months - 3 years	1,174,283	143,733	1,318,016
After 3 years	<u>10,819,031</u>	<u>1,343,341</u>	<u>12,162,372</u>
	<u>\$ 36,681,854</u>	<u>\$ 2,207,595</u>	<u>\$ 38,889,449</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(4) Loans Receivable, Continued

Allowance for Loan Losses

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

	<u>Development Corporation Division</u>	<u>Northern Marianas Housing Corporation</u>	<u>2009</u>	<u>2008</u>
Balance - beginning of year	\$ 26,930,650	\$ 6,218,333	\$ 33,148,983	\$ 30,786,848
Provision for loan losses	(983,227)	347,551	(635,676)	6,030,710
Write-off of loans	<u>(2,123,527)</u>	<u>-</u>	<u>(2,123,527)</u>	<u>(3,668,575)</u>
Balance - end of year	<u>\$ 23,823,896</u>	<u>\$ 6,565,884</u>	<u>\$ 30,389,780</u>	<u>\$ 33,148,983</u>

(5) Due from/to Other Funds

Due from/to balances between NMHC and DBD result from loans made by CDA to the former MIHA. The year end balances are summarized as follows:

	<u>2009</u>	<u>2008</u>
Housing construction loan. On February 3, 1999, CNMI Public Law 11-57 authorized CDA to write off the portion of this loan not considered recoverable through sale of housing construction units. Interest has therefore been suspended pending sales of the units.	\$ 456,611	\$ 456,611
Operating expenses	<u>54,045</u>	<u>54,045</u>
	<u>\$ 510,656</u>	<u>\$ 510,656</u>

DBD provided an allowance of \$456,611 and \$296,797 for the outstanding balance of the due from NMHC at September 30, 2009 and 2008, respectively.

Due from/to balances between DBD and DCD result from the use of restricted funding between the two divisions. These balances result from the time lag between the dates that 1) reimbursable expenditure occur, 2) transactions are recorded in the accounting system, and 3) payments between funds are made and are scheduled to be collected in the subsequent year.

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

(6) Capital Development Loans Receivable From Related Parties

As described in note 2, DBD is required to establish a revolving fund into which repayments of principal and interest from revenue-producing projects shall be deposited. The revolving fund consists of the following notes receivable as of September 30, 2009 and 2008:

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

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

	<u>2009</u>	<u>2008</u>
Note receivable from the Commonwealth Utilities Corporation (CUC), bearing interest at 7% per annum, with quarterly principal and interest payments due February 17, 1992 in the amount of \$658,469, with a maturity date of February 17, 2013. Proceeds are used for certain power generation and distribution projects within the CNMI.	\$ -	\$ 30,000,000
Note receivable from CUC, bearing interest at 5% per annum, with quarterly principal and interest payments due January 12, 1994 in the amount of \$359,514, with a maturity date of January 12, 2014. Proceeds are used for certain water projects within the CNMI.	-	16,068,750
Due from CUC, bearing interest at 7% per annum, with monthly principal and interest payments of \$58,509. No promissory agreement related to this note has been signed.	-	10,000,000
Note receivable from CUC, bearing interest at 7% per annum, with quarterly principal and interest payments due two years after January 30, 1990 in the amount of \$276,471, with a maturity date of January 30, 2000. Proceeds are used for Saipan Power Plant expansion.	-	5,500,000
Note receivable from the Commonwealth Ports Authority (CPA), bearing interest at 2.5% per annum, with quarterly principal and interest payments in the amount of \$204,113, with maturity date of November 16, 2014. Proceeds are used for the Saipan Harbor Project. On June 29, 2010, the note was revised with monthly principal and interest payments in the amount of \$31,000, with maturity date of June 15, 2030.	<u>5,803,610</u>	<u>6,085,380</u>
Total capital development loans receivable	5,803,610	67,654,130
Less allowance for loan losses	<u>(5,803,610)</u>	<u>(67,654,130)</u>
Net capital development loans receivable	\$ <u>-</u>	\$ <u>-</u>

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

	<u>2009</u>	<u>2008</u>
Balance - beginning of year	\$ 67,654,130	\$ 66,159,100
Provision for loan losses	-	1,495,030
Reclassification	(281,770)	-
Write-off of loans	<u>(61,568,750)</u>	<u>-</u>
Balance - end of year	\$ <u>5,803,610</u>	\$ <u>67,654,130</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

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

At September 30, 2009, estimated proceeds from principal and interest repayments of loans receivable for the following years ending September 30, are as follows:

<u>Year ending September 30,</u>	<u>Principal Amount</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 87,640	\$ 36,360	\$ 124,000
2011	231,744	140,256	372,000
2012	237,605	134,395	372,000
2013	243,613	128,387	372,000
2014	249,774	122,226	372,000
2015 - 2019	1,346,871	513,129	1,860,000
2020 - 2024	1,526,007	333,993	1,860,000
2025 - 2029	1,728,967	131,033	1,860,000
2030	<u>151,389</u>	<u>547,405</u>	<u>698,794</u>
	<u>\$ 5,803,610</u>	<u>\$ 2,087,184</u>	<u>\$ 7,890,794</u>

A Memorandum of Agreement (MOA) was established between CDA and CUC on November 21, 2002, as amended in January 2004, to waive a portion of the capital development loans receivable and to provide for the conversion into equity ownership of the balance. Public Laws 13-35, 13-36 and 16-17 were enacted to effectuate the settlement of disputes between CDA and CUC as required by the MOA.

On May 7, 2009, CUC and CDA, entered into a Preferred Stock Agreement (the Agreement) to effectuate the terms and conditions of the MOA by requiring CUC to issue shares of cumulative, non-convertible and non-transferrable preferred stock to CDA amounting to \$45,000,000 and yielding annual dividends of two percent per annum. The Commonwealth Public Utilities Commission approved the Agreement on September 3, 2009. The Agreement provides CUC the right to purchase from CDA up to \$16,200,000 of the \$45,000,000 preferred stock through offset against CUC's future, internally-funded capital improvement projects. Subject to CUC purchase exception, CDA shall not transfer any of its rights, title or interest to such preferred stocks. Further, the Agreement provides for deferral of the dividend payments for the first three years after issuance, with such deferred dividend payments being amortized, interest free, over a fifteen-year period. Dividends are to be paid to CDA beginning October 1, 2012. The Agreement cancels and discharges the indebtedness of CUC to CDA amounting to \$61,568,750 in principal and \$138,670,797 in accrued interest, including related late charges and any other charges owed by CUC on the capital development loans.

CUC issued to CDA forty-five shares of preferred stock with a par value of \$1,000,000 per share for a total aggregate value of \$45,000,000 dated September 28, 2009. The preferred stock yields guaranteed annual dividends at two percent per annum payable quarterly in advance. The dividends of the preferred stock are cumulative from and after October 1, 2009 and bear no interest. CDA has taken the position that the value of the preferred stock represents the net present value of the future stream of dividend payments required by CUC and not the face value of the stock itself. At September 30, 2009, CDA has recorded an investment of \$18,379,266, with a corresponding 100% valuation allowance, based on the discounted cash flows of the future dividend payments at 6.27% per annum.

Future receipts (which do not factor in CUC's right to purchase up to \$16,200,000 of preferred stock through offset against CUC's future, internally-funded capital improvement projects) for subsequent fiscal years are as follows:

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

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

<u>Year ending September 30,</u>	<u>Principal Balance</u>
2010	\$ -
2011	-
2012	-
2013	900,000
2014	900,000
2015 - 2039	<u>67,500,000</u>
	<u>\$ 69,300,000</u>

(7) Property and Equipment

Property and equipment consist of the following at September 30, 2009 and 2008:

Development Corporation Division

	<u>Estimated Useful Lives</u>	<u>Balance at October 1, 2008</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at September 30, 2009</u>
Structure and improvements	7 years	\$ 475,959	\$ -	\$ -	\$ 475,959
Vehicles/office equipment	3 - 5 years	123,860	16,599	-	140,459
Computer equipment	3 - 5 years	124,123	2,099	-	126,222
Furniture and fixtures	7 years	<u>125,619</u>	<u>-</u>	<u>-</u>	<u>125,619</u>
		849,561	18,698	-	868,259
Less accumulated depreciation		<u>(824,150)</u>	<u>(10,964)</u>	<u>-</u>	<u>(835,114)</u>
		<u>\$ 25,411</u>	<u>\$ 7,734</u>	<u>\$ -</u>	<u>\$ 33,145</u>

	<u>Estimated Useful Lives</u>	<u>Balance at October 1, 2007</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at September 30, 2008</u>
Structure and improvements	7 years	\$ 469,125	\$ 6,834	\$ -	\$ 475,959
Vehicles/office equipment	3 - 5 years	112,168	11,692	-	123,860
Computer equipment	3 - 5 years	123,278	845	-	124,123
Furniture and fixtures	7 years	<u>125,619</u>	<u>-</u>	<u>-</u>	<u>125,619</u>
		830,190	19,371	-	849,561
Less accumulated depreciation		<u>(810,481)</u>	<u>(13,669)</u>	<u>-</u>	<u>(824,150)</u>
		<u>\$ 19,709</u>	<u>\$ 5,702</u>	<u>\$ -</u>	<u>\$ 25,411</u>

Northern Marianas Housing Corporation

	<u>Estimated Useful Lives</u>	<u>Balance at October 1, 2008</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at September 30, 2009</u>
Residential Housing Development Projects:					
Section 8 Mihaville Housing	30 years	\$ 2,467,456	\$ 13,414	\$ -	\$ 2,480,870
Section 8 Koblerville Housing	30 years	1,937,998	6,076	-	1,944,074
Section 8 Rota Housing	30 years	1,176,787	-	-	1,176,787
Section 8 Tinian Housing	30 years	1,065,154	4,871	-	1,070,025
Section 8 Housing Phase II	30 years	635,929	-	-	635,929
Section 8 Housing Phase I	30 years	<u>600,515</u>	<u>-</u>	<u>-</u>	<u>600,515</u>
		<u>7,883,839</u>	<u>24,361</u>	<u>-</u>	<u>7,908,200</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(7) Property and Equipment, Continued

Northern Marianas Housing Corporation, Continued

	Estimated Useful Lives	Balance at October 1, 2008	Additions	Deletions	Balance at September 30, 2009
Other:					
Koblerville infrastructure	30 years	2,214,991	-	-	2,214,991
Tinian infrastructure	30 years	608,500	-	-	608,500
Building and improvements	20 years	478,231	-	-	478,231
Equipment and computers	3 - 8 years	535,862	28,515	-	564,377
Vehicles	3 years	150,477	-	-	150,477
		<u>3,988,061</u>	<u>28,515</u>	<u>-</u>	<u>4,016,576</u>
		11,871,900	52,876	-	11,924,776
Less accumulated depreciation		<u>(9,593,978)</u>	<u>(395,638)</u>	<u>-</u>	<u>(9,989,616)</u>
		<u>\$ 2,277,922</u>	<u>\$ (342,762)</u>	<u>\$ -</u>	<u>\$ 1,935,160</u>
	Estimated Useful Lives	Balance at October 1, 2007	Additions	Deletions	Balance at September 30, 2008
Residential Housing Development Projects:					
Section 8 Mihaville Housing	30 years	\$ 2,463,531	\$ 3,925	\$ -	\$ 2,467,456
Section 8 Koblerville Housing	30 years	1,933,153	4,845	-	1,937,998
Section 8 Rota Housing	30 years	1,176,787	-	-	1,176,787
Section 8 Tinian Housing	30 years	1,065,154	-	-	1,065,154
Section 8 Housing Phase II	30 years	635,229	700	-	635,929
Section 8 Housing Phase I	30 years	600,515	-	-	600,515
		<u>7,874,369</u>	<u>9,470</u>	<u>-</u>	<u>7,883,839</u>
Other:					
Koblerville infrastructure	30 years	2,214,991	-	-	2,214,991
Tinian infrastructure	30 years	608,500	-	-	608,500
Building and improvements	20 years	478,231	-	-	478,231
Equipment and computers	3 - 8 years	517,213	18,649	-	535,862
Vehicles	3 years	150,477	-	-	150,477
		<u>3,969,412</u>	<u>18,649</u>	<u>-</u>	<u>3,988,061</u>
		11,843,781	28,119	-	11,871,900
Less accumulated depreciation		<u>(9,160,382)</u>	<u>(433,596)</u>	<u>-</u>	<u>(9,593,978)</u>
		<u>\$ 2,683,399</u>	<u>\$ (405,477)</u>	<u>\$ -</u>	<u>\$ 2,277,922</u>

NMHC also holds title to approximately 339,000 square meters of land acquired at no cost which was originally held for development of low income rental housing or resale to low income families for construction of housing. The land is recorded on NMHC's financial statements at estimated fair value of \$9,747,313 and \$9,650,313 at September 30, 2009 and 2008, respectively. For the fiscal year ended September 30, 2008, NMHC recorded an impairment loss on land of \$620,869. Public Law 6-34 provides NMHC, subject to certain terms and conditions, the authority to lease for commercial development certain land situated in the North Garapan Subdivision Annex No. 2. NMHC is currently in the process of promoting the development of the abovementioned land to allow NMHC to meet its future commitments.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(8) Foreclosed Real Estate

A summary of the changes in foreclosed real estate and the related valuation allowance as of September 30, 2009 and 2008 is as follows:

	<u>Development Corporation Division</u>		<u>Northern Marianas Housing Corporation</u>	<u>2009</u>	<u>2008</u>
	<u>For Sale</u>	<u>For Lease</u>			
Foreclosed Real Estate					
Balance at beginning of year	\$ 2,113,274	\$ 1,584,400	\$ 429,114	\$ 4,126,788	\$ 3,021,369
Additions	378,282	570,541	-	948,823	1,683,883
Deletions	(31,000)	(27,000)	-	(58,000)	(221,858)
Reclassifications	(102,000)	102,000	-	-	-
Decline in market value	<u>(293,096)</u>	<u>(388,400)</u>	<u>-</u>	<u>(681,496)</u>	<u>(356,606)</u>
	2,065,460	1,841,541	429,114	4,336,115	4,126,788
Valuation allowance	<u>(963,230)</u>	<u>(780,000)</u>	<u>-</u>	<u>(1,743,230)</u>	<u>(1,848,837)</u>
Balance at end of year	\$ <u>1,102,230</u>	\$ <u>1,061,541</u>	\$ <u>429,114</u>	\$ <u>2,592,885</u>	\$ <u>2,277,951</u>
Valuation Allowance					
Balance at beginning of year	\$ 1,056,637	\$ 792,200	\$ -	\$ 1,848,837	\$ 1,320,337
Recoveries	(93,407)	(12,200)	-	(105,607)	(50,000)
Provision	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>578,500</u>
Balance at end of year	\$ <u>963,230</u>	\$ <u>780,000</u>	\$ <u>-</u>	\$ <u>1,743,230</u>	\$ <u>1,848,837</u>

(9) Note Payable to Related Party

Development Banking Division

Note payable at September 30, 2009 and 2008, is as follows:

	<u>2009</u>	<u>2008</u>
Note payable to Marianas Public Land Trust (MPLT), bearing interest at 6.5% per annum, due over a fifteen-year term, beginning June, 2003. The note is collateralized by the full faith and credit of the CNMI Government held in trust by MPLT, for the purpose of development and maintenance of the American Memorial Park, and is being repaid from earnings of the investments pursuant to CNMI Public Law 11-72.	\$ <u>1,374,243</u>	\$ <u>1,494,243</u>

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

<u>Year ending September 30,</u>	<u>Principal Balance</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 122,100	\$ 85,358	\$ 207,458
2011	120,000	77,489	197,489
2012	120,000	69,689	189,689
2013	120,000	61,889	181,889
2014	120,000	54,089	174,089
2015 - 2018	<u>772,143</u>	<u>124,397</u>	<u>896,540</u>
	\$ <u>1,374,243</u>	\$ <u>472,911</u>	\$ <u>1,847,154</u>

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(9) Note Payable to Related Party, Continued

Changes in notes payable for the years ended September 30, 2009 and 2008, are as follows:

	Balance October 1, 2008	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2009	Due Within One Year
DBD	\$ <u>1,494,243</u>	\$ <u>-</u>	\$ <u>(120,000)</u>	\$ <u>1,374,243</u>	\$ <u>122,100</u>
	Balance October 1, 2007	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2008	Due Within One Year
DBD	\$ 1,611,843	\$ -	\$ (117,600)	\$ 1,494,243	\$ 111,754
NMHC (MPLT)	<u>8,996,623</u>	<u>-</u>	<u>(8,996,623)</u>	<u>-</u>	<u>-</u>
	\$ <u>10,608,466</u>	\$ <u>-</u>	\$ <u>(9,114,223)</u>	\$ <u>1,494,243</u>	\$ <u>111,754</u>

(10) Transfers for Capital Development Grants

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

Transfers for capital development grants consist of transfers to (a) the CNMI Office of the Governor for matching funds for grants from the U.S. Department of the Interior amounted to \$0 and \$639,387 for the years ended September 30, 2009 and 2008, respectively, (b) transfers to the CNMI Second Senatorial District for various programs and projects pursuant to Public Law No. 15-111 amounted to \$0 and \$500,000 for the years ended September 30, 2009 and 2008, respectively, and (c) transfers to the CNMI for capital projects of the CNMI First and Second Senatorial Districts pursuant to Public Law No. 13-56 amounted to \$860,972 and \$0 for the years ended September 30, 2009 and 2008, respectively.

(11) Related Party Transactions

CDA maintains depository accounts in FDIC insured financial institutions. A Board member of CDA is currently the President/Regional Manager of one of these financial institutions. CDA's deposits in this financial institution amounted to \$15,931,361 and \$14,305,349 as of September 30, 2009 and 2008, respectively. Management is of the opinion that transactions with this financial institution are of similar terms and conditions as with unrelated parties.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(12) Claims and Settlement Expense

In November and December 2006, thirty-five homeowners filed a lawsuit against NMHC, architects, the construction manager and the contractor for deficiencies in the design and construction of homes in the Tottotville Subdivision. On February 25, 2009, NMHC entered into settlement agreements with the thirty-five homeowners for \$6,200 each to remove NMHC from the lawsuit. NMHC paid a total of \$286,062 of settlement fees including legal and professional fees which is recorded as settlement expense in the accompanying statements of revenues, expenses and changes in net assets.

(13) Commitments and Contingencies

Commitments

CDA leases certain foreclosed real estate properties for periods ranging from one to fifty-five years. On December 14, 2007, CDA entered into a sublease agreement for a portion of its office space in Saipan. The sublease is for a period of two years commencing from December 1, 2007 for annual rental of \$24,000. The sublease was extended up to June 1, 2010 for a total rental of \$9,878 from December 1, 2009 to June 1, 2010. Lease income for the years ended September 30, 2009 and 2008 amounted to \$71,364 and \$43,770, respectively. Minimum future lease income is as follows:

<u>Year ending September 30,</u>	<u>Minimum Lease Income Due</u>
2010	\$ 89,128
2011	73,751
2012	69,751
2013	64,151
2014	68,651
Thereafter	<u>1,480,519</u>
	<u>\$ 1,845,951</u>

Under a lease agreement beginning April 30, 2003 and expiring September 30, 2020, CDA leases office space in Saipan. The lease agreement provides for an annual rental of \$96,000 during the term of the lease. Also, CDA leases its office space in Tinian for an annual rental of \$7,200. The related lease agreement is expiring on February 28, 2012. Rental expense for these leases for each of the years ended September 30, 2009 and 2008 is \$104,400.

Total minimum future rentals under these operating leases as of September 30, 2008 are as follows:

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(13) Commitments and Contingencies, Continued

Commitments, Continued

<u>Year ending</u> <u>September 30,</u>	
2010	\$ 103,700
2011	103,200
2012	99,000
2013	96,000
2014	96,000
2015 - 2019	480,000
2020	<u>96,000</u>
	\$ <u>1,073,900</u>

Contingencies

CDA is authorized to guarantee up to 90% of the principal of loans and lines of credit made by financial institutions to qualified borrowers, in addition to approving direct loans. The amounts for which CDA was contingently liable under this arrangement at September 30, 2009 and 2008, was \$25,980 and \$94,197, respectively. As of September 30, 2009, no provision for any liability or potential loss that may result from this matter has been recorded in the accompanying financial statements.

NMHC participates in a number of federally assisted grant programs funded by the United States Government. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. Cumulative questioned costs of \$1,179,101 have been set forth in NMHC's Single Audit Report for the year ended September 30, 2009. The ultimate disposition of these questioned costs can be determined only by final action of the respective grantor agencies. Therefore, no provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

NMHC has entered into an agreement with the USDA Rural Development (RD) (formerly the U.S. Farmers Home Administration or FmHA) whereby NMHC assists borrowers in obtaining RD financing for housing construction. The agreement requires NMHC to guarantee any deficiency in foreclosure proceeds should borrowers default on the RD loans. As security under the agreement, NMHC is required to maintain an escrow account of \$286,436. Beginning September 30, 1993, the amount in the escrow account will be reduced each year by the product of \$1,500 multiplied by the number of loans paid in full for that particular year, or 4% of the total outstanding balance, whichever is less. As of September 30, 2009 and 2008, NMHC has guaranteed outstanding loans of approximately \$14,779,100 and \$12,277,300, respectively. As of September 30, 2009 and 2008, the balance in the escrow account was \$259,793 and \$259,144, respectively. These amounts are included in "restricted cash and cash equivalents" in the accompanying financial statements. As of September 30, 2009 and 2008, the amount of defaulted loans related to the agreement was \$5,893,782 and \$4,550,555, respectively. Of the total defaulted loans, the amount with demand notices from RD was \$1,260,205 and \$546,597 at September 30, 2009 and 2008, respectively, for which NMHC recorded a liability included in "reserve for loan guaranty" in the accompanying financial statements. NMHC management cannot presently determine any additional liability on the remaining defaulted loans of \$4,633,577 at September 30, 2009 and \$4,279,126 at September 30, 2008 and, accordingly, no provision for any liability or potential loss that may result from this matter has been recorded in the accompanying financial statements.

COMMONWEALTH DEVELOPMENT AUTHORITY

Notes to Financial Statements
September 30, 2009 and 2008

(13) Commitments and Contingencies, Continued

Contingencies, Continued

In June 2008, NMHC entered into an agreement with RD to resolve defaulted RD loans. The agreement has been established to outline the steps and mutually agreed-upon terms in liquidating defaulted RD loans. The agreement encompasses forty-eight seriously delinquent guaranteed loans totaling \$3,126,371. However, this number may decline if any accounts cure before the related auction dates. On June 5, 2008, NMHC's Board of Directors approved a resolution to restrict \$1,521,923 of NMHC's funds for the purpose of paying any amount due and payable to RD pursuant to the agreement. The eventual outcome of this matter cannot be presently determined and, accordingly, no provision for any liability or potential loss that may result from this matter has been recorded in the accompanying financial statements.

NMHC entered into a loan agreement and related loan purchase agreement with a savings and loan in the CNMI whereby the savings and loan will make available up to \$6,000,000 for housing loans. Under the agreements, NMHC is responsible for administering the loan purchase program and the savings and loan agrees to purchase qualified loans from NMHC. NMHC guarantees the first 25% of the principal balance plus interest on each loan sold to the savings and loan. As of September 30, 2009 and 2008, NMHC was contingently liable for \$1,102,655 of the balance of loans purchased by the savings and loan. In addition, NMHC is required to maintain an account at the savings and loan equal to the lesser of 5% of all loans sold to the savings and loan or \$100,000. The balance in the account at September 30, 2009 and 2008 was \$26,430 and \$58,851, respectively, which is included in "restricted cash and cash equivalents" in the accompanying financial statements.

NMHC also has similar arrangements with other financial institutions whereby NMHC guarantees a varying percentage of loans issued by the banks for housing construction. At September 30, 2009 and 2008, NMHC was contingently liable to these institutions for \$2,463,509 and \$1,646,480, respectively. As of September 30, 2009 and 2008, the total amount of defaulted loans on these arrangements was \$-0-.

(14) Risk Management

CDA is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees; and natural disasters. CDA has elected to purchase commercial insurance from independent third parties for the risks of loss to which it is exposed. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

COMMONWEALTH DEVELOPMENT AUTHORITY

Combining Statement of Net Assets
September 30, 2009

<u>ASSETS</u>	Development Banking Division	Development Corporation Division	Northern Marianas Housing Corporation	Elimination Entries	Total
Current assets:					
Cash and cash equivalents	\$ -	\$ 1,112,364	\$ 1,104,361	\$ -	\$ 2,216,725
Receivables:					
Loans	-	1,770,727	873,469	-	2,644,196
Rent, net	-	-	89,142	-	89,142
Accrued interest, net	47,480	24,170	411,275	-	482,925
Other, net	-	59,194	86,047	-	145,241
Prepaid expenses	-	16,284	6,881	-	23,165
Total current assets	<u>47,480</u>	<u>2,982,739</u>	<u>2,571,175</u>	<u>-</u>	<u>5,601,394</u>
Other assets:					
Cash and cash equivalents, restricted	404,720	1,701,896	3,390,606	-	5,497,222
Time certificates of deposit, restricted	7,684,205	641,050	-	-	8,325,255
Total other assets	<u>8,088,925</u>	<u>2,342,946</u>	<u>3,390,606</u>	<u>-</u>	<u>13,822,477</u>
Noncurrent assets:					
Loans receivable, net	-	11,087,231	1,334,126	-	12,421,357
Due from other funds	456,894	-	-	(456,894)	-
Property and equipment, net	-	33,145	1,935,160	-	1,968,305
Land	-	-	9,747,313	-	9,747,313
Foreclosed real estate	-	2,163,771	429,114	-	2,592,885
Total noncurrent assets	<u>456,894</u>	<u>13,284,147</u>	<u>13,445,713</u>	<u>(456,894)</u>	<u>26,729,860</u>
	<u>\$ 8,593,299</u>	<u>\$ 18,609,832</u>	<u>\$ 19,407,494</u>	<u>\$ (456,894)</u>	<u>\$ 46,153,731</u>
<u>LIABILITIES AND NET ASSETS</u>					
Current liabilities:					
Current installment of notes payable to related party	\$ 122,100	\$ -	\$ -	\$ -	\$ 122,100
Accounts payable and accrued expenses	18,963	322,874	636,095	-	977,932
Due to related party	375,968	11,520	-	-	387,488
Deferred revenues	-	11,002	-	-	11,002
Due to grantor agency	-	-	783,795	-	783,795
Reserve for loan guaranty	-	-	1,601,907	-	1,601,907
Total current liabilities	<u>517,031</u>	<u>345,396</u>	<u>3,021,797</u>	<u>-</u>	<u>3,884,224</u>
Notes payable to related party, net of current installments	1,252,143	-	-	-	1,252,143
Deferred revenues, net of current portion	-	558,335	3,894,743	-	4,453,078
Due to other funds	-	402,849	510,656	(913,505)	-
Total liabilities	<u>1,769,174</u>	<u>1,306,580</u>	<u>7,427,196</u>	<u>(913,505)</u>	<u>9,589,445</u>
Net assets:					
Invested in capital assets	-	2,196,916	12,111,587	-	14,308,503
Restricted	6,824,125	15,106,336	(131,289)	456,611	22,255,783
Total net assets	<u>6,824,125</u>	<u>17,303,252</u>	<u>11,980,298</u>	<u>456,611</u>	<u>36,564,286</u>
	<u>\$ 8,593,299</u>	<u>\$ 18,609,832</u>	<u>\$ 19,407,494</u>	<u>\$ (456,894)</u>	<u>\$ 46,153,731</u>

See Accompanying Independent Auditors' Report.

COMMONWEALTH DEVELOPMENT AUTHORITY

Combining Statement of Revenues, Expenses and Changes in Net Assets
Year Ended September 30, 2009

	Development Banking Division	Development Corporation Division	Northern Marianas Housing Corporation	Elimination Entries	Total
Operating revenues:					
Interest and fees on loans	\$ 130,386	\$ 3,049,330	\$ 509,769	\$ -	\$ 3,689,485
Section 8 income:					
Federal housing assistance rentals	-	-	4,964,888	-	4,964,888
Tenant share	-	-	81,547	-	81,547
Interest on investments	137,577	60,015	-	-	197,592
CDBG Program Grant	-	-	1,528,092	-	1,528,092
ESG Program Grant	-	-	52,874	-	52,874
Other	1,200	256,238	538,253	(155,573)	640,118
	269,163	3,365,583	7,675,423	(155,573)	11,154,596
Bad debts	(290,200)	(796,207)	(279,025)	159,814	(1,205,618)
Net operating revenues	(21,037)	2,569,376	7,396,398	4,241	9,948,978
Operating expenses:					
Section 8 rental	-	-	3,406,966	-	3,406,966
CDBG Program Grant	-	-	1,528,092	-	1,528,092
Salaries and wages	-	434,591	581,556	-	1,016,147
Repairs and maintenance	-	10,832	931,540	-	942,372
Provision for loan guaranty	-	-	772,280	-	772,280
Provision for foreclosed real estate	-	575,889	-	-	575,889
Depreciation	-	10,964	395,638	-	406,602
Employee benefits	-	138,690	184,001	-	322,691
Utilities	-	25,379	293,563	-	318,942
Professional fees	10,753	114,060	140,101	-	264,914
Travel	-	64,479	98,191	-	162,670
Office rent	-	110,234	4,239	-	114,473
ESG Program Grant	-	-	52,435	-	52,435
Other	156,251	56,861	170,595	(155,573)	228,134
Total operating expenses	167,004	1,541,979	8,559,197	(155,573)	10,112,607
Operating income (loss)	(188,041)	1,027,397	(1,162,799)	159,814	(163,629)
Nonoperating revenues (expenses):					
Settlement expense	-	-	(286,062)	-	(286,062)
Other income	259,794	-	-	(46,894)	212,900
Interest income	-	-	14,989	-	14,989
Interest expense	(92,900)	(46,894)	(540)	46,894	(93,440)
Other expense	-	(11,520)	(74,112)	-	(85,632)
Total nonoperating revenues (expenses), net	166,894	(58,414)	(345,725)	-	(237,245)
Income (loss) before transfers	(21,147)	968,983	(1,508,524)	159,814	(400,874)
Transfers out for capital development grants	(860,972)	-	-	-	(860,972)
Change in net assets	(882,119)	968,983	(1,508,524)	159,814	(1,261,846)
Net assets - beginning	7,706,244	16,334,269	13,488,822	296,797	37,826,132
Net assets - ending	\$ 6,824,125	\$ 17,303,252	\$ 11,980,298	\$ 456,611	\$ 36,564,286

See Accompanying Independent Auditors' Report.

COMMONWEALTH DEVELOPMENT AUTHORITY

Combining Statement of Cash Flows
Year Ended September 30, 2009

	Development Banking Division	Development Corporation Division	Northern Marianas Housing Corporation	Elimination Entries	Total
Cash flows from operating activities:					
Cash received from interest and fees on loans receivable	\$ -	\$ 590,990	\$ 133,334	\$ -	\$ 724,324
Interest and dividends on investments	136,270	100,079	-	-	236,349
Cash payments to suppliers for goods and services	(16,949)	(510,794)	(710,515)	-	(1,238,258)
Cash received from customers	1,200	31,545	543,970	-	576,715
Cash payments to employees for services	-	(575,006)	(581,556)	-	(1,156,562)
Cash received from federal grant awards	-	-	5,573,592	-	5,573,592
Cash payments from federal grant awards	-	-	(6,287,450)	-	(6,287,450)
Net cash provided by (used for) operating activities	<u>120,521</u>	<u>(363,186)</u>	<u>(1,328,625)</u>	<u>-</u>	<u>(1,571,290)</u>
Cash flows from capital and related financing activities:					
Net interdivisional transactions	1,848,756	(1,848,756)	-	-	-
Acquisition of property and equipment	-	(18,698)	(52,876)	-	(71,574)
Acquisition of land	-	-	(97,000)	-	(97,000)
Net receipts of loans receivable	-	1,148,850	275,515	-	1,424,365
Interest paid on notes payable	-	-	(540)	-	(540)
Payments for claims and settlements	-	-	(286,062)	-	(286,062)
Payments for guaranteed loans	-	-	(74,112)	-	(74,112)
Transfers for capital development grants	(485,004)	-	-	-	(485,004)
Net cash provided by (used for) capital and related financing activities	<u>1,363,752</u>	<u>(718,604)</u>	<u>(235,075)</u>	<u>-</u>	<u>410,073</u>
Cash flows from investing activities:					
Net proceeds from restricted cash and cash equivalents and time certificates of deposit	(1,484,273)	492,992	1,352,488	-	361,207
Interest received	-	-	14,989	-	14,989
Net cash (used for) provided by investing activities	<u>(1,484,273)</u>	<u>492,992</u>	<u>1,367,477</u>	<u>-</u>	<u>376,196</u>
Net decrease in cash and cash equivalents	-	(588,798)	(196,223)	-	(785,021)
Cash and cash equivalents at beginning of year	-	1,701,162	1,300,584	-	3,001,746
Cash and cash equivalents at end of year	<u>\$ -</u>	<u>\$ 1,112,364</u>	<u>\$ 1,104,361</u>	<u>\$ -</u>	<u>\$ 2,216,725</u>
Reconciliation of operating income (loss) to net cash provided by (used for) operating activities:					
Operating income (loss)	\$ (188,041)	\$ 1,027,397	\$ (1,162,799)	\$ 159,814	\$ (163,629)
Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities:					
Bad debts	290,200	796,207	279,025	(159,814)	1,205,618
Expenses allocated from DCD to DBD	155,573	(155,573)	-	-	-
Provision for foreclosed real estate	-	575,889	-	-	575,889
Provision for loan guaranty	-	-	772,280	-	772,280
Depreciation	-	10,964	395,638	-	406,602
(Increase) decrease in assets:					
Receivables:					
Rent	-	-	(81,589)	-	(81,589)
Other	-	(56,656)	5,760	-	(50,896)
Accrued interest	(131,693)	(2,418,276)	(376,435)	-	(2,926,404)
Prepaid expenses	-	(3,335)	7,624	-	4,289
Increase (decrease) in liabilities:					
Accounts payable and accrued expenses	(5,518)	(1,605)	(195,867)	-	(202,990)
Deferred revenues	-	(138,198)	-	-	(138,198)
Due to grantor agency	-	-	(972,262)	-	(972,262)
Net cash provided by (used for) operating activities	<u>\$ 120,521</u>	<u>\$ (363,186)</u>	<u>\$ (1,328,625)</u>	<u>\$ -</u>	<u>\$ (1,571,290)</u>
Supplemental disclosure of noncash capital and related financing activities:					
Recognition of foreclosed properties:					
Noncash increase in foreclosed real estate	\$ -	\$ 948,823	\$ -	\$ -	\$ 948,823
Noncash decrease in loans receivable	-	(948,823)	-	-	(948,823)
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Loan restructuring:					
Noncash increase in loans receivable	\$ -	\$ 724,689	\$ -	\$ -	\$ 724,689
Noncash decrease in accrued interest	-	(719,409)	-	-	(719,409)
Noncash decrease in other receivables	-	(5,280)	-	-	(5,280)
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Loan payable to MPLT:					
Noncash decrease in note payable to related party	\$ -	\$ 120,000	\$ -	\$ -	\$ 120,000
Noncash interest expense	-	92,900	-	-	92,900
Noncash other income	-	(212,900)	-	-	(212,900)
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

See Accompanying Independent Auditors' Report.

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

INDEPENDENT AUDITORS' REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2009

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, 2009, and have issued our report thereon dated October 18, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

For purposes of this report, our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts and grants, and other matters did not include the Northern Marianas Housing Corporation (NMHC) which was audited by us. We have issued separate reports on our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts and grants, and other matters for NMHC that was audited by us. The findings included in those reports are not included herein.

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 the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying Schedule Findings and Responses (pages 3 through 7) to be significant deficiencies in internal control over financial reporting as items 2009-1 and 2009-2.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiencies described above are 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 Responses as item 2009-3.

We noted certain matters that we reported to management of CDA in a separate letter dated October 18, 2010.

CDA's responses to the findings identified in our audit are described in the accompanying Schedule Findings and Responses. 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

October 18, 2010

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule Findings and Responses Year Ended September 30, 2009

DCD Loans Receivable

Finding No. 2009-1

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 to demonstrate that the borrower can meet the revised debt service requirements.

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

1. An analysis of DCD's past due loans was performed to determine the propriety of the allowance for doubtful loans as of September 30, 2009. This analysis revealed that loans which are six months or more in arrears amounted to \$28,279,955 or 77.1% of the total loans receivable outstanding of \$36,681,854 as of September 30, 2009. The related accrued interest on loans that are six months or more in arrears amounted to \$17,102,152 or 99.6% of the total accrued interest receivable outstanding of \$17,166,710 as of September 30, 2009.
2. For two restructured loans (#s CD 70347 and CD 70332) classified as less than six months in arrears in the receivables aging report as of September 30, 2009, an analysis of the loan ledger subsequent to September 30, 2009 indicated that borrowers did not meet revised debt service requirements. An audit adjustment was proposed to record an additional allowance of \$1,444,387.
3. For two restructured loans (#s RE 70325 and CD 70349), allowances were calculated in the same manner for loans that are over 12 months past due. However, an analysis of the loan ledger prior and subsequent to restructuring indicated that loans should be classified as less than six months.

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 the 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.

Recommendation: We recommend that CDA continue to follow-up on past due loans, continue to evaluate these loans and develop corrective action plans. Future results may be compared against action plans and other actions taken by management as deemed necessary. Legal action should be considered for loans considered unlikely to be serviceable by the borrower. We further recommend that CDA review the aging of restructured loans and revisit the allowance calculation for these loans. In addition, we recommend that CDA perform periodic review of the calculation of the 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 2008.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule Findings and Responses, Continued
Year Ended September 30, 2009

Finding No. 2009-1, Continued

Auditee Response and Corrective Action Plan:

Name of Contact Person: Stuart Smith, Comptroller

Corrective Action: Ensuring collection of loans is a complex problem exacerbated by difficult financial times in the CNMI. Inadequate levels of staffing in the Loan Department also reduce the ability to monitor and work with clients closely. If loans are monitored more closely perhaps there would be fewer delinquent loans and the valuation of the loans would have less negative impact.

CDA has continued to make improvements in fiscal year 2010 to make sure loans are valued in a manner consistent with the guidelines set forth by CDA in conjunction with the auditors. Restructured loans that have insufficient time (one year) to establish payment histories based on the restructured status are valued in the same manner as their status dictated prior to restructuring. Miscellaneous charges are fully allowed for.

In the third quarter of fiscal year 2010, CDA adopted a commercial-bank-like policy of accruing interest in the general ledger only up to 120 days for delinquent loans. While this method gives CDA a financial picture that is similar to accrual of all interest regardless of length of delinquency but with a correspondingly high allowance for bad debts, it is better in that it treats each loan on its own merits versus portfolio totals only.

Management has taken various actions to work with clients; restructuring with set-aside or write-off of accrued interest and foreclosures when no other viable solutions are available. Most of the restructured loans are maintaining a current payment status. The Loan Department has had the services of an additional staff member since May 2010. His efforts in collections and working with clients have yielded positive results. Management is also continuing to explore different ways to assist clients in making their loans more manageable. These steps will likely involve concessions on the part of CDA regarding accrued interest, but management feels it is critical to recover loan principal and give borrowers every chance possible to avoid bankruptcy, foreclosure and other expensive or painful options.

Proposed Completion Date: Improving the delinquency rate of the loan portfolio is an ongoing process that will never be "completed" but progress has been noted since the second half of fiscal year 2010.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule Findings and Responses, Continued
Year Ended September 30, 2009

DCD Loans Receivable

Finding No. 2009-2

Criteria: Loan reclassifications should be timely recorded in the general ledger.

Condition: Tests of loans receivable noted the following:

1. A summary judgment was ordered prior to the current fiscal year for one loan (ref. CD 70340); however, a reclassification as a judgment loan was only recorded during fiscal year 2009. The related loan, interest and miscellaneous charges receivable amounted to \$841,875, \$154,532 and \$3,025, respectively, as of September 30, 2009;
2. A summary judgment was ordered prior to the current fiscal year for one loan (ref. CD 70346); however, a reclassification as a judgment loan was only recorded during fiscal year 2009. The related interest and miscellaneous charges receivable amounted to \$934 and \$3,520, respectively, as of September 30, 2009. In addition, CDA acquired related foreclosed property in July 2008 for \$32,541 but only recorded the property in fiscal year 2009; and
3. Write-offs of three loans receivable (ref. JV 2121) were recorded in the general ledger ten months subsequent to Board approval.

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

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

Recommendation: We recommend that CDA ensure that adjustments resulting from loan reclassifications are timely recorded.

Prior Year Status: The lack of monitoring procedures to ensure that all loan reclassification adjustments are recorded in the general ledger was reported as a finding in the Single Audits of CDA for fiscal years 2007 and 2008.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Stuart Smith, Comptroller

Corrective Action: The legal machinations involved with judgments against borrowers are not a black-and-white process. While a summary judgment may be obtained against a borrower as a last resort to recovering a loan, CDA has a high rate of experience with the summary judgment NOT being the final judgment. Often, the judgment includes a period where actions by either party may render the judgment void. This is one reason the Loan Department may not ask the Accounting Department to immediately reclassify a judgment loan. The other reason for delays in the past is simply due to understaffing in both the Loan and Accounting Departments for much of the past two years.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule Findings and Responses, Continued
Year Ended September 30, 2009

Finding No. 2009-2, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

In fiscal year 2010, CDA is doing a better job of reviewing all loans to judge appropriateness of the valuation and classification. There continues to be gray areas for loans subject to summary judgment but staffs are doing their best to weigh the circumstances when making reclassification decisions.

Proposed Completion Date: Beginning in late fiscal year 2009, the Loan and Accounting Departments have been more diligent in booking judgment loans in a timely manner. Beginning in fiscal year 2010, CDA will record loans as judgment loans as soon as there is a court order and if there are any subsequent modifications to the judgment, they will be recorded as they occur.

COMMONWEALTH DEVELOPMENT AUTHORITY

Schedule Findings and Responses, Continued
Year Ended September 30, 2009

Local Noncompliance

Finding No. 2009-3

Criteria: Pursuant to the "Trust Fund Use and Management Agreement" dated May 31, 1994, the remaining trust funds and accumulated earnings earned by CDA from bond issues shall be made available for appropriation by the Commonwealth Legislature for capital improvement projects (CIP) and economic development activities consistent with Part II, 3(a) of the Special Representative Agreement.

Condition: As of September 30, 2009, DBD's investments in time certificates of deposit of \$7,684,205 were restricted for CIP activities and capital development purposes. These funds represent the proceeds of Covenant funding and liquidated revenue bonds derived from pledged Covenant funding. Of the total funds, CDA is unable to identify amounts previously appropriated and amounts available for future CIP appropriation. CDA is in the process of reconciling DBD funds to determine availability.

Cause: The cause of the above condition is the lack of established policies and procedures to monitor appropriated and available funds.

Effect: The effect of the above condition is the potential for misappropriation of DBD funds.

Recommendation: We recommend CDA reconcile DBD funds and identify amounts appropriated and available. Further, we recommend CDA monitor actual CIP drawdowns against appropriations on a per project basis.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Stuart Smith, Comptroller

Corrective Action: This has been a problem since fiscal year 2001 when the responsibility for CIP tracking and bond fund reconciliations was transferred from the assistant to the Executive Director to the Accounting Department. The Accounting Department was without a Comptroller for eight years and did not have the adequate manpower, skills, guidance or supervision to maintain the task.

Proposed Completion Date: In fiscal year 2010, the task of catching up the tracking was assigned to various staff members in CDA in addition to their regular duties. Catching up eight years of activity and follow actions by the Legislature is not a process that can occur in a short period of time. The staff is making progress on the task and the Executive Director has asked that it be made a priority.

COMMONWEALTH DEVELOPMENT AUTHORITY

Unresolved Prior Year Comments
Year Ended September 30, 2009

Unresolved Findings

The status of unresolved findings is discussed in the Schedule Findings and Responses section of this report (pages 3 through 7).