

COMMONWEALTH UTILITIES CORPORATION

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

YEAR ENDED SEPTEMBER 30, 2000

COMMONWEALTH UTILITIES CORPORATION

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2000 AND 1999

INDEPENDENT AUDITORS' REPORT

Board of Directors
Commonwealth Utilities Corporation:

We have audited the accompanying balance sheets of the Commonwealth Utilities Corporation (CUC), a component unit of the Commonwealth of the Northern Mariana Islands (CNMI), as of September 30, 2000 and 1999, and the related statements of (loss) earnings and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of CUC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

Except as discussed in the following paragraph, 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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.

Because of inadequacies in the accounting records and internal control, we were unable to determine that utility receivables, inventory, due from grantor agencies, utility plant and obligations under capital lease were fairly stated as of September 30, 2000 and 1999. Furthermore, in our judgment, the balances of utility receivables, inventory, due from grantor agencies and utility plant materially affect the determination of results of operations and cash flows for the years ended September 30, 2000 and 1999. In addition, CUC management was unable to provide minutes of Board of Directors meetings subsequent to December 14, 2004. Accordingly, there was an incomplete record of management and Board of Directors' actions and decisions.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had the propriety of utility receivables, inventory, due from grantor agencies, utility plant and obligations under capital lease as of September 30, 2000 and 1999 been determined, and their effect on the results of operations and cash flows, been determinable, and had we received minutes of the Board of Directors meetings subsequent to December 14, 2004 as discussed in the third paragraph, such financial statements present fairly, in all material respects, the financial position of CUC as of September 30, 2000 and 1999, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As described in note 2 to the financial statements, CUC changed its method of accounting for contributions in aid in 2000 to conform with the provisions of Governmental Accounting Standards Board Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*.

As described in note 8 to the financial statements, CUC implemented the accounting guidance included in Emerging Issues Task Force Issue No. 01-8, which clarifies the accounting treatment for energy purchase agreements.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Statement of Revenues and Expenses on a Divisional Basis for the year ended September 30, 2000 (page 18) is presented for purposes of additional analysis and is not a required part of the basic financial statements of CUC. This statement is the responsibility of the management of CUC. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, except as discussed in the third paragraph above, is fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 21, 2005, on our consideration of CUC's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte & Touche

March 21, 2005

COMMONWEALTH UTILITIES CORPORATION

Balance Sheets
September 30, 2000 and 1999

ASSETS

	<u>2000</u>	<u>1999</u> <u>As Restated</u>
Utility plant:		
Electric plant	\$ 105,998,553	\$ 99,999,933
Water plant	50,297,630	45,821,455
Sewer plant	16,783,489	16,763,605
Administrative equipment	4,032,335	3,801,897
Construction work in progress	<u>18,487,641</u>	<u>19,640,384</u>
	195,599,648	186,027,274
Less accumulated provision for depreciation	<u>(81,452,997)</u>	<u>(73,358,249)</u>
Net utility plant	<u>114,146,651</u>	<u>112,669,025</u>
Current assets:		
Cash and cash equivalents	<u>12,947,921</u>	<u>9,315,758</u>
Accounts receivable:		
Utility	24,349,732	20,791,911
Other	<u>2,054,663</u>	<u>1,633,124</u>
	26,404,395	22,425,035
Less accumulated provision for uncollectible accounts	<u>(15,493,253)</u>	<u>(4,635,163)</u>
Net accounts receivable	<u>10,911,142</u>	<u>17,789,872</u>
Inventory, less allowance for obsolescence of \$1,159,467 in 2000 and 1999	<u>9,630,880</u>	<u>9,387,283</u>
Due from grantor agencies	<u>534,709</u>	<u>790,826</u>
Total current assets	<u>34,024,652</u>	<u>37,283,739</u>
Restricted assets:		
Cash and cash equivalents	<u>6,184,244</u>	<u>5,174,782</u>
	<u>\$ 154,355,547</u>	<u>\$ 155,127,546</u>

See accompanying notes to financial statements.

COMMONWEALTH UTILITIES CORPORATION

Balance Sheets, Continued
September 30, 2000 and 1999

CAPITALIZATION AND LIABILITIES

	<u>2000</u>	<u>1999</u> <u>(As Restated)</u>
Capitalization:		
Retained earnings	\$ <u>6,272,038</u>	\$ <u>18,503,331</u>
Long-term debt:		
Obligations under capital lease, less current maturities	8,788,557	9,306,865
Loan payable less current maturities	326,664	363,203
Compensated absences, less current portion	<u>254,248</u>	<u>431,180</u>
	<u>9,369,469</u>	<u>10,101,248</u>
Commitments and contingencies		
Current liabilities:		
Current maturities of long-term debt	61,605,289	61,603,180
Current obligations under capital lease	518,306	433,136
Accounts payable	11,573,078	7,474,262
Accrued liabilities	279,193	279,273
Accrued payroll	679,475	449,833
Compensated absences, current portion	650,748	565,829
Customer deposits	7,294,615	7,120,347
Payable to CNMI Office of the Public Auditor	2,777,222	2,158,854
Interest payable	<u>53,336,114</u>	<u>46,438,253</u>
Total current liabilities	<u>138,714,040</u>	<u>126,522,967</u>
	<u>\$ 154,355,547</u>	<u>\$ 155,127,546</u>

See accompanying notes to financial statements.

COMMONWEALTH UTILITIES CORPORATION

Statements of (Loss) Earnings and Retained Earnings
Years Ended September 30, 2000 and 1999

	<u>2000</u>	<u>1999</u> <u>(As Restated)</u>
Operating revenues:		
Power	\$ 54,403,356	\$ 54,592,641
Water	8,348,516	7,060,230
Sewer	2,155,419	2,073,597
Franchise income	559,093	558,160
Other	<u>883,088</u>	<u>501,727</u>
Total operating revenues	<u>66,349,472</u>	<u>64,786,355</u>
Operating expenses:		
Production fuel	27,956,569	17,452,854
General and administrative	18,023,381	17,557,100
Bad debts	10,870,454	321,062
Depreciation	8,106,414	6,746,939
Maintenance	7,543,525	9,245,029
Other production	3,042,334	2,967,842
Supplies	704,080	763,029
Other	<u>196,207</u>	<u>136,138</u>
Total operating expenses	<u>76,442,964</u>	<u>55,189,993</u>
(Loss) earnings from operations	<u>(10,093,492)</u>	<u>9,596,362</u>
Nonoperating revenues (expenses):		
Interest income	813,257	633,082
Federal grant income	-	52,470
Foreign exchange gain	-	97
Interest expense	(8,624,724)	(7,800,229)
CNMI Office of the Public Auditor funding	<u>(683,368)</u>	<u>(664,365)</u>
Total nonoperating revenues (expenses), net	<u>(8,494,835)</u>	<u>(7,778,945)</u>
Net (loss) earnings before capital contributions	(18,588,327)	1,817,417
Capital contributions	<u>6,357,034</u>	<u>4,305,351</u>
Net (loss) earnings	(12,231,293)	6,122,768
Retained earnings - beginning	<u>18,503,331</u>	<u>12,380,563</u>
Retained earnings - ending	\$ <u><u>6,272,038</u></u>	\$ <u><u>18,503,331</u></u>

See accompanying notes to financial statements.

COMMONWEALTH UTILITIES CORPORATION

Statements of Cash Flows
Years Ended September 30, 2000 and 1999

	<u>2000</u>	<u>1999</u>
Cash flows from operating activities:		
(Loss) earnings from operations	\$ (10,093,492)	\$ 9,596,362
Adjustments to reconcile (loss) earnings from operations to net cash provided by operating activities:		
Depreciation	8,106,414	6,746,939
Bad debts	10,870,454	321,062
(Increase) decrease in assets:		
Accounts receivable:		
Utility	(3,557,821)	(6,871,328)
Other	(421,539)	372,950
Inventory	(243,597)	(2,589,329)
Increase (decrease) in liabilities:		
Accounts payable	4,098,816	2,359,747
Accrued liabilities	(92,093)	279,788
Accrued payroll	229,642	(92,348)
Customer deposits	<u>174,268</u>	<u>198,426</u>
Net cash provided by operating activities	<u>9,071,052</u>	<u>10,322,269</u>
Cash flows from noncapital financing activities:		
Payments to CNMI Office of the Public Auditor	(65,000)	(55,000)
Operating grants received	<u>-</u>	<u>52,470</u>
Net cash used for noncapital financing activities	<u>(65,000)</u>	<u>(2,530)</u>
Cash flows from capital and related financing activities:		
Acquisition and construction of capital assets	(9,596,404)	(17,390,584)
Capital contributions	6,357,034	4,305,351
Proceeds from issuance of debt	-	9,959,000
Principal repayment of debt	(467,568)	(3,246,426)
Interest paid on outstanding debt	(1,726,863)	(1,141,520)
Net disbursements for capital grants	256,117	(319,691)
(Increase) decrease in restricted assets	<u>(1,009,462)</u>	<u>1,156,123</u>
Net cash used for capital and related financing activities	<u>(6,187,146)</u>	<u>(6,677,747)</u>
Cash flows from investing activities:		
Interest received on time certificates of deposit	<u>813,257</u>	<u>633,082</u>
Net cash provided by investing activities	<u>813,257</u>	<u>633,082</u>
Net increase in cash and cash equivalents	3,632,163	4,275,074
Cash and cash equivalents at beginning of year	<u>9,315,758</u>	<u>5,040,684</u>
Cash and cash equivalents at end of year	\$ <u>12,947,921</u>	\$ <u>9,315,758</u>

See accompanying notes to financial statements.

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(1) Organization

The Commonwealth Utilities Corporation (CUC), a component unit of the Commonwealth of the Northern Mariana Islands (CNMI), was established as a Public Corporation by CNMI Public Law 4-47, as amended by Public Law 5-47, effective October 1, 1985, and began operations on October 1, 1987. CUC was given responsibility for supervising the construction, maintenance, operations, and regulation of all utility services, including power, sewage, refuse collection, telephone, cable television, and water, provided however, that whenever feasible, CUC shall contract for private businesses to assume its duties with respect to one or more of these divisions. CUC was also designated the responsibility to establish rates, meter, bill and collect fees in a fair and rational manner from all customers of utility services in order for CUC to become financially independent of appropriations by the CNMI Legislature. CUC is governed by a nine-member Board of Directors, appointed for terms of four years by the Governor of the CNMI.

Public Law 4-47 effected transfer to CUC of identifiable assets, liabilities, operations, and unexpended capital improvement funding allocations formerly administered directly by the CNMI Department of Public Works.

(2) Summary of Significant Accounting Policies

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

Estimates

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

Basis of Accounting

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 the fund are included on the balance sheets. Proprietary fund operating statements present increases and decreases in net total assets.

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(2) Summary of Significant Accounting Policies, Continued

Basis of Accounting, Continued

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. Revenues are recorded as billed to customers on a monthly cycle billing basis. At the end of each month, unbilled revenues are accrued for each cycle based on the most recent cycle billing.

Budgets

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

Cash and Cash Equivalents

For purposes of the balance sheets and the statements of cash flows, cash and cash equivalents and restricted cash and cash equivalents are defined as cash on hand, cash in checking and savings accounts, and short-term time certificates of deposit with a maturity date within three months of the date acquired. At September 30, 2000 and 1999, CUC's cash and cash equivalents are substantially with federally insured banks. CNMI law does not require government agency funds to be collateralized in excess of Federal Depository Insurance Corporation (FDIC) limits; therefore, any amounts in excess of these limits are uncollateralized. FDIC insurance aggregated \$184,423 and \$200,000 at September 30, 2000 and 1999, respectively.

Short-term time certificates of deposit amounting to \$6,184,244 and \$5,174,782 as of September 30, 2000 and 1999, respectively, represent customer deposits, which must be segregated pursuant to CUC policy, and accordingly, are classified as restricted in the accompanying financial statements.

Receivables and Allowance for Doubtful Accounts

CUC provides utility services to customers within the CNMI and bills for these services on a monthly basis. The accumulated provision for uncollectible accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectibility of these accounts and prior collection experience. The allowance is established through a provision for bad debts charged to expense.

Inventory

Inventories of fuel are valued at the lower of cost (first-in, first-out) or market (net realizable value). Inventories of supplies and materials are valued at average cost.

Utility Plant and Depreciation

Utility plant are stated at cost, where available. Cost of certain utility plant transferred from the CNMI Department of Public Works, is based on contract amounts to construct certain utility plant. Depreciation is calculated on the straight-line method based on the estimated useful lives of the respective assets. Current policy is to capitalize items in excess of \$300.

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(2) Summary of Significant Accounting Policies, Continued

Utility Plant and Depreciation, Continued

Capitalization of Interest

CUC capitalizes interest in order to recognize all costs associated with non-contributed construction projects based on CUC's weighted average borrowing rate. During the years ended September 30, 2000 and 1999, eligible interest expense was not considered significant and consequently no interest has been capitalized.

Retirement Plan

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

Plan members are required to contribute 6.5% and 9.0% of their annual covered salary for Class I and Class II members, respectively, and CUC is required to contribute at an actuarially determined rate. The current rate is 26.4% of annual covered payroll. The contribution requirements of plan members and CUC are established and may be amended by the Fund's Board of Trustees. CUC's contributions to the Fund for the years ended September 30, 2000, 1999 and 1998 were \$2,687,910, \$2,619,860, and \$2,622,676, respectively, equal to the required contributions for each year.

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. The liability at September 30, 2000 and 1999 amounted to \$904,996 and \$997,009, respectively. No liability is recorded for nonvesting accumulating rights to receive sick pay benefits. The sick pay benefit liability as of September 30, 2000 and 1999, was approximately \$2,000,000.

Franchise Income

Franchise income is received from a local telecommunications company for the right to provide telecommunication services within the CNMI.

Reclassification

Certain 1999 balances in the accompanying financial statements have been reclassified to conform to the 2000 presentation.

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

GASB has issued Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*. The provisions of this statement require capital grants and contributions to be recognized as non-operating revenue on the Statements of (Loss) Earnings and Retained Earnings. In prior periods, capital grants and contributions had been recorded as a direct increase to contributions in aid in the equity section of the statement of net assets. As a result, contributed capital and retained earnings as of October 1, 1999 have been restated from the amounts previously reported.

For fiscal year 2002, CUC will be implementing GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by Statement No. 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, and modified by Statement No. 38, *Certain Financial Statement Disclosures*. These statements establish financial reporting standards for governmental entities which require that management's discussion and analysis of the financial activities be included with the basic financial statements and notes and modifies certain other financial statement disclosure requirements. CUC is required to adopt GASB Statement No. 34, as amended by GASB Statement No. 37, and certain provisions of GASB Statement No. 38 in fiscal year 2002. For fiscal year 2005, CUC will be implementing GASB Statement No. 40, *Deposit and Investment Risk Disclosures (an amendment of GASB Statement No. 3)* and GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. As of September 30, 2000, CUC has not evaluated the financial statement impact of GASB Statement Nos. 34, 37, 38, 40 and 42.

(3) Due From Grantor Agencies

CUC is a subrecipient of federal grants received by the CNMI from various U.S. federal agencies. CUC follows the accounting principle generally accepted in the United States of America of recording grants-in-aid for construction or acquisition of facilities and equipment as contributions. Excess grant disbursements over receipts are recognized as due from grantor agencies until funds are received in accordance with grant terms and conditions.

Changes in the due from grantor agencies accounts for the years ended September 30, 2000 and 1999, are as follows:

	<u>2000</u>	<u>1999</u>
Balance at beginning of year	\$ 790,824	\$ 471,135
Adjustments	(718,304)	-
Deductions - cash receipts from grantor agencies	(5,174,318)	(4,231,570)
Additions - program outlays	<u>5,636,507</u>	<u>4,551,261</u>
Balance at end of year	\$ <u>534,709</u>	\$ <u>790,826</u>

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(4) Utility Plant

Utility plant at September 30, 2000 and 1999, consists of the following:

	Estimated Useful Lives	Balance at October 1, 1999 (As Restated)	Additions	Deletions	Balance at September 30, 2000
Utility plant:					
Electric plant	20 years	\$ 99,999,933	\$ 5,998,620	\$ -	\$ 105,998,553
Water plant	20 years	45,821,455	4,476,175	-	50,297,630
Sewer plant	20 years	16,763,605	19,884	-	16,783,489
Administrative equipment	3 - 5 years	3,801,897	230,438	-	4,032,335
		166,386,890	10,725,117	-	177,112,007
Less accumulated provision for depreciation		(73,358,249)	(8,094,748)	-	(81,452,997)
		93,028,641	2,630,369	-	95,659,010
Construction work in progress		19,640,384	-	(1,152,743)	18,487,641
		\$ 112,669,025	\$ 2,630,369	\$ (1,152,743)	\$ 114,146,651

	Estimated Useful Lives	Balance at October 1, 1998	Additions	Deletions	Adjustments	Balance at September 30, 1999
Utility plant:						
Electric plant	20 years	\$ 90,289,795	\$ 11,167,692	\$ -	\$ (1,457,554)	\$ 99,999,933
Water plant	20 years	43,366,054	1,346,508	-	1,108,893	45,821,455
Sewer plant	20 years	16,531,191	96,654	-	135,760	16,763,605
Administrative equipment	3 - 5 years	3,436,380	273,014	-	92,503	3,801,897
		153,623,420	12,883,868	-	(120,398)	166,386,890
Less accumulated provision for depreciation		(65,391,603)	(6,763,144)	-	(1,203,502)	(73,358,249)
		88,231,817	6,120,724	-	(1,323,900)	93,028,641
Construction work in progress		18,400,833	4,522,921	-	(3,283,370)	19,640,384
		\$ 106,632,650	\$ 10,643,645	\$ -	\$ (4,607,270)	\$ 112,669,025

(5) Notes Payable

A schedule of CUC's long-term debt as of September 30, 2000 and 1999, is as follows:

	2000	1999
Promissory note payable to the Commonwealth Development Authority (CDA), a component unit of the CNMI. Principal amount available to \$30,000,000, interest at 7% per annum, with a maturity date of February 17, 2013. Principal and interest payments are due in quarterly payments of \$658,469.	\$ 30,000,000	\$ 30,000,000
Promissory note payable to CDA. Principal amount available to \$16,135,650, interest at 5% per annum, with a maturity date of January 12, 2014. Principal and interest payments are due in quarterly payments of \$359,514.	16,068,750	16,068,750

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(5) Notes Payable, Continued

	<u>2000</u>	<u>1999</u>
Promissory note payable to CDA. Principal amount available to \$5,500,000, interest at 7% per annum, with a maturity date of January 30, 2000. Principal and interest payments are due in quarterly payments of \$276,471.	5,500,000	5,500,000
Promissory note payable to CDA. Principal amount available to \$10,000,000 and interest at 7% per annum. Principal and interest payments are due in monthly payments of \$58,509. No promissory agreement related to this note has been signed.	<u>10,000,000</u>	<u>10,000,000</u>
	<u>\$ 61,568,750</u>	<u>\$ 61,568,750</u>

At September 30, 2000 and 1999, and subsequent to that date, CUC was in default of repayment terms of all notes payable to CDA. In accordance with the associated loan agreements, in the event of default, CDA may accelerate all remaining amounts due. Thus, \$61,568,750 at September 30, 2000 and 1999, associated with the notes payable to CDA along with interest payable on these notes of \$53,195,842 and \$46,291,453 as at September 30, 2000 and 1999, respectively, has been classified as current liabilities within the accompanying financial statements.

(6) Loan Payable

On June 29, 1988, the CNMI executed a loan contract with the United States Department of Agriculture, Farmers Home Administration in the amount of \$1,033,400. The loan contract bears interest at 6-1/8% per annum with repayments due on January 1 beginning in 1989 and continuing through 2008. Proceeds of the loan are to be used for the acquisition and construction of improvements and replacements to the Saipan Water System, which is administered by CUC. CUC is required to deposit all water system revenue and funds it receives through the "Covenant to Establish a CNMI in Political Union With the United States of America (the Covenant)" into a water system revenue fund to provide for repayment of the loan. As of September 30, 2000 and 1999, CUC had not established the required water system revenue fund but has established separate general ledger accounts to summarize water system revenues and Covenant funds. It is CUC's intention to repay the loan from these sources and management is of the opinion that its process of accounting for water system revenues and Covenant funds is in compliance with the intent of the loan agreement.

The following summarizes this loan payable as of September 30, 2000 and 1999:

	<u>2000</u>	<u>1999</u>
Loan payable to the U.S. Department of Agriculture with repayments due on January 1, beginning in 1989 through 2008, bearing interest at 6-1/8% per annum.	\$ 363,203	\$ 397,633
Less current portion	<u>36,539</u>	<u>34,430</u>
Long-term loan payable	<u>\$ 326,664</u>	<u>\$ 363,203</u>

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(6) Loan Payable, Continued

Future repayment commitments of principal and interest are as follows:

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>
2001	\$ 36,539	\$ 22,246
2002	38,777	20,008
2003	41,152	17,633
2004	43,672	15,112
2005	46,347	12,438
Subsequent years	<u>156,716</u>	<u>19,574</u>
	<u>\$ 363,203</u>	<u>\$ 107,011</u>

(7) CNMI Office of the Public Auditor Funding

Public Law 9-66, enacted October 19, 1995, requires government agencies to pay the Commonwealth Treasurer an amount not less than the greater of 1% of its total operations budget from sources other than legislative appropriations or pursuant to any other formula, which the Public Auditor and the agency may agree, to fund the Office of the Public Auditor (OPA). At September 30, 2000 and 1999, CUC had an outstanding payable to OPA in the amount of \$2,777,222 and \$2,158,854, respectively.

(8) Capital Lease

On June 10, 1997, CUC entered into an agreement with a contractor for the construction, maintenance and operation, and transfer of ownership of a 10 Megawatt Power Plant on the island of Tinian. The agreement is for a guaranteed price of \$9,959,000 plus interest and fees of \$11,641,000 payable over ten years in equal monthly installments of \$180,000. During this period, the contractor will maintain and operate the power plant and be paid operation, production and maintenance fees of \$50,000 per month in addition to the guaranteed price. Additionally, CUC will pay a production fee of two cents (\$0.02) per plant-produced kilowatt hour for as long as the operations and maintenance portion of the contract is in effect. The power plant will be turned over to CUC at the end of the ten year period from the date of substantial completion. On December 13, 1998, CUC executed a change order to expand the 10 Megawatt Power Plant to 30 Megawatts. Such expansion is to be fulfilled within the ten year period as stated in the original agreement.

CUC implemented accounting guidance of Emerging Issues Task Force (EITF) Issue No. 01-8, which provides guidance in determining when purchase agreements may be subject to lease accounting. CUC has determined that the agreement to purchase electricity is in fact a capital lease to acquire the plant and that the capacity payments made under the agreement are lease payments. The operation, production and maintenance payments and production fees under the agreement are reflected as energy conversion costs under other production expense.

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(8) Capital Lease, Continued

The effects of adopting EITF No. 01-8 were to increase plant and obligations under capital lease by \$9,959,000. CUC has not obtained the actual cost of the power plant and has not obtained an appraisal to determine the fair value of the leased property, which is required by accounting principles generally accepted in the United States of America. As a result, management has not been able to assess its compliance with the EITF requirements and the impact of this matter on the accompanying financial statements is uncertain. The lease has an effective interest rate of 18%.

CUC may, without penalty, discharge the entire outstanding balance of the guaranteed price by paying a discounted amount equal to the adjusted guaranteed price as follows:

<u>Period</u>	<u>Amount</u>
End of year 3	\$ 9,783,000
End of year 4	\$ 8,821,000
End of year 5	\$ 7,750,000
End of year 6	\$ 6,540,000
End of year 7	\$ 5,200,000
End of year 8	\$ 3,900,000

Future repayment commitments of principal and interest are as follows:

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>
2001	\$ 518,306	\$ 1,641,692
2002	620,225	1,539,774
2003	742,183	1,417,817
2004	888,122	1,271,878
2005	1,062,758	1,097,241
Subsequent years	<u>5,475,269</u>	<u>1,904,733</u>
	<u>\$ 9,306,863</u>	<u>\$ 8,873,135</u>

(9) Commitments and Contingencies

Commitments

CUC has entered into a commitment to borrow \$89,000,000 from the Commonwealth Development Authority for proposed capital improvement projects. As of September 30, 2000 and 1999, CUC had entered into promissory note agreements for \$30,000,000, \$16,135,650, and \$5,500,000 against the \$89 million as described in note 5. Although CUC retains the ability to borrow, management does not believe that future borrowing will occur.

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(9) Commitments and Contingencies, Continued

Commitments, Continued

On September 23, 1996, CUC entered into an agreement with a third party for the purchase of electric power and associated services. The agreement provides for a monthly minimum purchase of 7,300,000 kilowatt-hours (KWH) at \$0.033 per KWH after January 1, 1998. Additionally, the agreement provides for periodic adjustment of the prices agreed upon but not to exceed 10% of the price then in effect. The agreement will expire on July 31, 2006 and renewable for an additional ten year period to expire on July 31, 2016. Future minimum commitments related to the purchase of electric power are as follows:

<u>Year ending September 30,</u>	<u>Minimum Payment</u>
2001	\$ 2,740,700
2002	2,890,800
2003	2,960,880
2004	3,101,040
2005	3,101,040
2006	<u>2,584,200</u>
	\$ <u>17,378,660</u>

Contingencies

CUC entered into certain memorandums of understanding (MOUs) with developers who paid CUC sewer connection fees in excess of that required by CUC's regulations. To the extent that CUC has not complied with obligations imposed on it by the MOUs (i.e., depositing the contributions in a special fund, making accountings, and spending the contributions for specified capital improvement projects), developers could consider CUC to have breached the terms of the MOUs. The maximum amount that CUC could be required to expend pursuant to the MOUs is \$3,027,951. No provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

CUC currently does not maintain insurance coverage with respect to its inventory and utility plant. In the event of a loss, CUC will be self insured for the entire amount. No provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

(10) Restatements

Effective fiscal year 2000, CUC implemented GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*. The provisions of this statement require capital grants and contributions to be recognized as non-operating revenue on the Statements of (Loss) Earnings and Retained Earnings. In prior periods, capital grants and contributions had been recorded as a direct increase to contributions in aid in the equity section of the Balance Sheet. As a result, contributed capital and retained earnings have been restated from the amounts previously reported.

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(10) Restatements, Continued

As discussed in note 8, CUC implemented accounting guidance of EITF No. 01-8 and determined that an agreement previously recorded as a note payable is in fact, a capital lease.

Subsequent to the issuance of CUC's 1999 financial statements, CUC's management determined that utility plant was overstated as of September 30, 1999. As a result, utility plant and accumulated depreciation have been restated from the amounts previously reported.

A summary of the above restatements is as follows:

	<u>As Previously Reported</u>	<u>Restated</u>
Electric plant	\$ <u>101,457,487</u>	\$ <u>99,999,933</u>
Water plant	\$ <u>44,712,562</u>	\$ <u>45,821,455</u>
Sewer plant	\$ <u>16,627,845</u>	\$ <u>16,763,605</u>
Administrative equipment	\$ <u>3,709,394</u>	\$ <u>3,801,897</u>
Construction work in progress	\$ <u>22,923,754</u>	\$ <u>19,640,384</u>
Accumulated depreciation	\$ <u>(72,154,747)</u>	\$ <u>(73,358,249)</u>
Notes payable	\$ <u>71,308,751</u>	\$ <u>61,568,750</u>
Obligations under capital lease	\$ <u>-</u>	\$ <u>9,740,001</u>
Deficit	\$ <u>(35,165,160)</u>	\$ <u>12,380,563</u>
Contributed capital	\$ <u>52,152,993</u>	\$ <u>-</u>

(11) Subsequent Events

On November 21, 2002, a Memorandum of Agreement (MOA) was established between CDA and CUC to waive a portion of the notes payable to CDA and the conversion into equity ownership of the balance. Public Law 13-35 effectuated terms of the MOA allowing CDA to waive \$16,068,750 and waive certain specified interest payments and for other purposes. Public Law 13-36 effectuated terms of the MOA by authorizing CUC to issue shares to CDA of cumulative nonconvertible non-transferable preferred stock valued at \$45,500,000. At September 30, 2000, terms of the MOA are being negotiated between CDA and CUC and thus debt has not been waived and preferred stock has not been issued.

In January 2004, the Memorandum of Agreement (MOA), entered into on November 21, 2002 between CUC and CDA was amended to exclude a certain provision requiring CUC to obtain legislative approval for rate increases. As terms of the MOA are in the process of negotiations, no adjustments have been made to the accompanying financial statements.

COMMONWEALTH UTILITIES CORPORATION

Notes to Financial Statements
September 30, 2000 and 1999

(11) Subsequent Events, Continued

On October 26, 2004, CUC published proposed amendments to the Electrical Service Regulations (ESR) for a fuel surcharge. The regulation limited the fuel surcharge to a maximum of 3.5 cents per kilowatt hour (kwh) for the first calendar year after adoption of the regulation, but allowed for full cost recovery in subsequent calendar years. The regulation includes an exception, required by statute, limiting the annual increase for low volume users. After notices and hearings, the fuel surcharge was adopted in January 2005. The final regulation was published on February 17, 2005 and became effective by operation of law on February 28, 2005. As a result of the regulation being finalized in 2005, the 3.5 per kwh cents cap on the surcharge will remain in effect until the end of calendar year 2005. For calendar year 2006, the formula included in the fuel surcharge regulation will be applied to establish a new ceiling and the fuel surcharge may be increased to that ceiling over the course of the year.

During the year ended September 30, 2003, CUC and the CNMI Government, with the concurrence of OPA, offset a portion of the liability related to CNMI OPA funding against utility receivables of the CNMI Government. The offset was performed through an exchange of checks for \$3,997,847.

Related to the agreement described in note 8, on May 10, 2001, CUC executed another change order (Expanded Agreement) to extend the term of the original agreement to be effective upon the execution of the expanded agreement until the later of March 31, 2020 or the completion of the term as mutually agreed upon. The expanded agreement provides for CUC to pay a base loan rate of \$0.03 plus applicable price adjustments per kilowatt-hour CUC uses each month effective March 1, 2009 until March 31, 2020. Additionally, the contractor will operate and maintain the existing distribution system of CUC for the duration of the expanded agreement at no cost to CUC. During the term of the expanded agreement, CUC is not allowed to purchase electric energy from any other producer other than the contractor for the island of Tinian.

COMMONWEALTH UTILITIES CORPORATION

Statement of Revenues and Expenses on a Divisional Basis
Year Ended September 30, 2000

	Power	Water	Sewer	Administrative and General	Internal Revenues and Expenses (1)	Total
Operating revenues:						
Governmental:						
CNMI Government	\$ 4,863,623	\$ 2,128,858	\$ 877,369	\$ -	\$ -	\$ 7,869,850
CNMI agencies	<u>3,957,100</u>	<u>1,100,611</u>	<u>737,547</u>	<u>-</u>	<u>(2,281,614)</u>	<u>3,513,644</u>
Total governmental	8,820,723	3,229,469	1,614,916	-	(2,281,614)	11,383,494
Commercial	33,344,804	3,094,049	788,519	-	-	37,227,372
Residential	15,232,834	3,005,953	109,799	-	-	18,348,586
Grants and contributions	436,485	1,013	165	-	-	437,663
Miscellaneous	(1,149,876)	(981,968)	(357,980)	559,093	-	(1,930,731)
Other	-	-	-	883,088	-	883,088
Total operating revenues	<u>56,684,970</u>	<u>8,348,516</u>	<u>2,155,419</u>	<u>1,442,181</u>	<u>(2,281,614)</u>	<u>66,349,472</u>
Operating expenses:						
Production fuel	27,956,569	-	-	-	-	27,956,569
General and administrative	6,973,106	2,467,962	1,388,762	7,193,551	-	18,023,381
Bad debts	-	-	-	10,870,454	-	10,870,454
Depreciation	6,156,652	1,230,985	445,855	272,922	-	8,106,414
Maintenance	5,249,070	1,080,523	710,584	503,348	-	7,543,525
Other production	5,111,672	83,886	128,390	-	(2,281,614)	3,042,334
Supplies	211,280	255,128	100,558	137,114	-	704,080
Other	-	-	-	196,207	-	196,207
Total operating expenses	<u>51,658,349</u>	<u>5,118,484</u>	<u>2,774,149</u>	<u>19,173,596</u>	<u>(2,281,614)</u>	<u>76,442,964</u>
Earnings (loss) from operations	<u>5,026,621</u>	<u>3,230,032</u>	<u>(618,730)</u>	<u>(17,731,415)</u>	<u>-</u>	<u>(10,093,492)</u>
Nonoperating revenues (expenses):						
Interest income	-	-	-	813,257	-	813,257
Federal grant income	-	-	-	-	-	-
Foreign exchange gain	-	-	-	-	-	-
Interest expense	(7,806,157)	(818,567)	-	-	-	(8,624,724)
CNMI Office of the Public Auditor funding	-	-	-	(683,368)	-	(683,368)
Total nonoperating revenues (expenses), net	<u>(7,806,157)</u>	<u>(818,567)</u>	<u>-</u>	<u>129,889</u>	<u>-</u>	<u>(8,494,835)</u>
Net earnings (loss) before capital contributions	(2,779,536)	2,411,465	(618,730)	(17,601,526)	-	(18,588,327)
Capital contributions	<u>6,357,034</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,357,034</u>
Net earnings (loss) by division	<u>\$ 3,577,498</u>	<u>\$ 2,411,465</u>	<u>\$ (618,730)</u>	<u>\$ (17,601,526)</u>	<u>\$ -</u>	<u>\$ (12,231,293)</u>

(1) The Water and Sewer Divisions recognize an expense for power supplied by the Power Division to operate their facilities. The Power division recognizes internal revenue for the corresponding amount.

See accompanying independent auditors' report.

COMMONWEALTH UTILITIES CORPORATION

INDEPENDENT AUDITORS' REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2000

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

Board of Directors
Commonwealth Utilities Corporation:

We have audited the financial statements of the Commonwealth Utilities Corporation (CUC), as of and for the year ended September 30, 2000, and have issued our report thereon dated March 21, 2005, which was qualified due to our inability to determine the propriety of utility receivables, inventory, due from grantor agencies, utility plant and obligations under capital lease. Except as described in the preceding sentence, 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.

Compliance

As part of obtaining reasonable assurance about whether CUC's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered CUC's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect CUC's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs (pages 10 through 28) as Findings 2000-1 through 2000-18.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider Findings 2000-1, 2000-2, 2000-4, 2000-8, 2000-9, 2000-10, 2000-12, 2000-13, 2000-14, 2000-15, 2000-16, 2000-17 and 2000-18 to be material weaknesses.

This report is intended for the information of the management of CUC, the Board of Directors, the cognizant audit and other federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche

March 21, 2005

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

Board of Directors
Commonwealth Utilities Corporation:

Compliance

We have audited the compliance of the Commonwealth Utilities Corporation (CUC) with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its one major federal program for the year ended September 30, 2000. CUC's major federal program is identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs (pages 10 through 28). Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of CUC's management. Our responsibility is to express an opinion on CUC's compliance based on our audit.

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

In our opinion, CUC complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended September 30, 2000.

Internal Control Over Compliance

The management of CUC is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered CUC's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of CUC as of and for the year ended September 30, 2000, and have issued our report thereon dated March 21, 2005, which was qualified due to our inability to determine the propriety of utility receivables, inventory, due from grantor agencies, utility plant and obligations under capital lease. Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards (pages 6 and 7) is presented for the purpose of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. This schedule is the responsibility of the management of CUC. Such information has been subjected to the auditing procedures applied in our audit of the financial statements and, in our opinion, except as described in the aforementioned report, is fairly stated, in all material respects, when considered in relation to the financial statements taken as a whole.

This report is intended for the information of the management of CUC, the Board of Directors, the cognizant audit and other federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche

March 21, 2005

COMMONWEALTH UTILITIES CORPORATION

Schedule of Programs Selected for Audit in
 Accordance with OMB Circular A-133
 Year Ended September 30, 2000

The following list specifies grants selected for detailed compliance testing in accordance with applicable A-133 requirements.

<u>Original Grantor</u>	<u>CFDA #</u>	<u>Description</u>	<u>Amount of Expenditures</u>
U.S. Federal Emergency Management Agency	83.544	Waterline Projects	\$ 1,021,847
U.S. Department of the Interior	15.875	OTIA Fiscal Year 1993, 1994 and 1995 Capital Development Projects	<u>3,530,364</u>
		Total program expenditures tested (1)	\$ <u>4,552,211</u>
		Total federal program expenditures	\$ <u>5,636,507</u>
		% of total federal program expenditures tested	<u>81%</u>

- (1) In addition, proceeds of the loan funds described in notes 3A and 3B to the Schedule of Expenditures of Federal Awards, totaling \$61,998,826, were tested for detailed compliance in accordance with A-133 requirements.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2000

Federal Grantor/ Pass Through Grantor/ Program Title	Federal CFDA Number/ Grantor ID No./ Pass Through Grantor's Number	CNMI Cost Center	Program or Award Amount	Receivable (Deferred) Revenue) from Grantor at October 1, 1999	Adjustments FY00	Cash Receipt FY00	Expen- ditures FY00	Receivable (Deferred) Revenue) from Grantor at September 30, 2000
U.S. Environmental Protection Agency								
Direct Program:								
San Roque/Tanapag Sewer Collection	66.418/C690001-050/-	-	\$ 1,273,300	\$ 256,374	\$ (256,374)	\$ -	\$ -	\$ -
Beach Road Sewer System	66.418/-/-	-	2,886,120	211,325	-	987,820	1,020,131	243,636
Lower Navy Hill Sewerline			-	-	-	-	64,165	64,165
Passed through the CNMI								
Dept. of Public Works:								
Construction	66.418/-/-	3307	39,350	807	(807)	-	-	-
Waste Water, Agingan Waste Water Treatment Plant and Saipan Pump Station Renovation	66.418/C690001-030/-	3346	1,228,881	93,445	(93,445)	-	-	-
Rota Water Cave TL	66.418/07-01-02901/-	3347	743,250	50,094	(50,094)	-	-	-
Rota Wast Water TS	66.418/C690002-010/-	3348	1,120,115	222,336	(222,336)	-	-	-
Sadog Tasi Sewage Treatment Plant	66.418/C690001-04-0/-	3352	1,252,732	193,229	(193,229)	-	-	-
CK, Sus, Kag SV Water	66.418/-/-	3363	-	219	(219)	-	-	-
Subtotal CFDA #66.418			8,543,748	1,027,829	(816,504)	987,820	1,084,296	307,801
U.S. Department of the Interior								
Partnership Agreement to Strengthen CUC	OMIP 95-1		1,011,251	19,335	-	50,893	31,558	-
	OMIP 99-2		149,000	1,785	-	20,420	29,523	10,888
Passed through the Government of the CNMI:								
Federal Portion								
Water and Power Projects	15.875/-/-	-	-	(398,111)	-	-	233,789	(164,322)
Upgrade Feeder 4	15.875/-/-	5804	1,407,543	-	-	-	-	-
Kagman III Homestead Waterline	15.875/-/-	4910	1,722,550	-	-	47,649	47,649	-
Oleai Waterline	15.875/-/-	4912	439,800	-	-	-	-	-
Isley/San Vicente Waterline	15.875/-/-	4932	741,393	-	-	31,433	31,433	-
Tatachog/Songsong Waterline	15.875/-/-	4938	513,100	-	(12,123)	-	-	(12,123)
Electric Power Transmission Substations	15.875/-/-	4901	4,005,637	-	-	866,804	866,804	-
Sinapalu-Dugai Waterline	15.875/-/-	4909	366,548	138,812	(138,812)	-	-	-
Tinian 1.5MW Generator	15.875/-/-	4987	376,078	177,576	(177,576)	-	-	-
Precinct II Distribution Upgrade	15.875/-/-	5804	1,200,000	-	-	123,231	123,231	-
Design & Construction San Jose Waterline Replacement	15.875/-/-	4936	1,158,509	-	-	446,038	446,038	-
Sinapalu-Chugai Waterline	15.875/-/-	4939	479,008	-	-	77,448	77,448	-
Precinct I Waterline	15.875/-/-		316,259	-	-	137,832	137,832	-
Y2K Remediation	15.875/-/-	19875Y	126,800	126,800	-	126,800	-	-
Marpo Well	15.875/-/-		607,862	-	-	380,444	380,444	-
Chalan Pale Arnold Sewerline	15.875/-/-		640,883	-	-	48,302	48,302	-
Beach Road Sewerline	15.875/-/-		450,000	-	-	161,698	161,698	-
Subtotal Federal Portion			15,712,221	66,197	(328,511)	2,518,992	2,615,749	(165,557)
Local Matching Portion								
Upgrade Feeder 4	15.875/-/-	5804	512,707	-	-	-	-	-
Kagman III Homestead Waterline	15.875/-/-	4910	627,450	-	-	17,355	17,355	-
Oleai Waterline	15.875/-/-	4912	160,200	-	-	-	-	-
Isley/San Vicente Waterline	15.875/-/-	4932	270,057	-	-	11,450	11,450	-
Tatachog/Songsong Waterline	15.875/-/-	4938	186,900	-	(2,358)	2,058	-	(4,416)
Design & Construction Beach Road Sewer	15.875/-/-	4980	1,375,050	-	-	58,900	58,900	-
Carolina Heights Waterline	15.875/-/-	4712	107,328	-	-	-	-	-
Electric Power Transmission Substations	15.875/-/-	4901	1,458,363	-	-	326,464	326,464	-
Sinapalu-Dugai Waterline	15.875/-/-	4909	133,452	50,563	(50,563)	-	-	-
Tinian 1.5MW Generator	15.875/-/-	4987	136,922	63,924	(63,924)	-	-	-
Precinct II Distribution Upgrade	15.875/-/-	5804	800,000	-	-	103,401	103,401	-
Design & Construction San Jose Waterline Replacement	15.875/-/-	4936	422,515	-	-	162,472	162,472	-
Sinapalu-Chugai Waterline	15.875/-/-	4939	174,482	-	-	28,200	28,200	-
Precinct I Waterline	15.875/-/-		115,200	-	-	50,206	50,206	-
Marpo Well	15.875/-/-		405,242	-	-	138,579	138,579	-
Chalan Pale Arnold Sewerline	15.875/-/-		233,446	-	-	17,588	17,588	-
Subtotal Local Matching Portion			7,119,314	114,487	(116,845)	916,673	914,615	(4,416)
Subtotal CFDA #15.875			22,831,535	180,684	(445,356)	3,435,665	3,530,364	(169,973)

See accompanying notes to schedule of expenditures of federal awards.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Expenditures of Federal Awards, Continued
Year Ended September 30, 2000

Federal Grantor/ Pass Through Grantor/ Program Title	Federal CFDA Number/ Grantor ID No./ Pass Through Grantor's Number	CNMI Cost Center	Program or Award Amount	Receivable (Deferred) Revenue from Grantor at October 1, 1999	Adjustments FY00	Cash Receipt FY00	Expen- ditures FY00	Receivable (Deferred) Revenue) from Grantor at September 30, 2000
<u>U.S. Federal Emergency Management Agency</u>								
Passed through the Government of the CNMI:								
Public Assistance	83.544/-/-	-	898,000	(9,534)	-	91,699	101,233	-
Rota Water Well Drilling			-	123,687	-	326,962	203,275	-
Water Augmentation Program	83.544/-/-	-	1,279,500	11,714	-	332,172	717,339	396,881
Subtotal CFDA #83.544			2,177,500	125,867	-	750,833	1,021,847	396,881
<u>U.S. Department of Agriculture</u>								
Passed through the Government of the CNMI:								
Loan project Saipan Water	10.423/-/-	3344	-	(34,359)	34,359	-	-	-
CK/Sasupe Waterline PhIII	10.423/-/-	4512	3,100,200	778,528	(778,528)	-	-	-
Kagman San Vicente Water	10.423/-/-	4511	-	1,437,585	(1,437,585)	-	-	-
Water Dist. Coll.	10.423/-/-	4513	-	(2,788,204)	2,788,204	-	-	-
Subtotal CFDA #10.423			3,100,200	(606,450)	606,450	-	-	-
<u>U.S. Department of Commerce - Economic Development Administration</u>								
Direct Program:								
Tasa Marpi Waterline	11.300/-/-	-	1,200,000	(320,130)	320,130	-	-	-
Rota Sinapalo-Tatachog Waterline	11.300/-/-	-	-	655,448	(655,448)	-	-	-
Rota Tatachog-SongSong-Teneto Ponia Waterlin	11.300/-/-	-	456,998	557	(557)	-	-	-
Passed through the Government of the CNMI:								
Rota Water Cave	11.300/-/-	3362	1,200,000	(264,281)	264,281	-	-	-
Unlocated difference			-	(8,700)	8,700	-	-	-
Subtotal CFDA #11.300			2,856,998	62,894	(62,894)	-	-	-
			\$ 39,509,981	\$ 790,824	\$ (718,304)	\$ 5,174,318	\$ 5,636,507	\$ 534,709

See accompanying notes to schedule of expenditures of federal awards.

COMMONWEALTH UTILITIES CORPORATION

Notes to Schedule of Expenditures of Federal Awards Year Ended September 30, 2000

(1) Scope of Review

The Commonwealth Utilities Corporation (CUC) was established as a Public Corporation by the Commonwealth of the Northern Mariana Islands (CNMI) Public Law 4-47, effective October 1, 1985. CUC was given responsibility for supervising the construction, maintenance operations, and regulation of all utility services, including power, sewage, refuse collections, telephone, cable television, and water, provided however, that, whenever feasible, CUC shall contract for private businesses to assume its duties with respect to one or more of its divisions. CUC was also designated with the responsibility to establish rates, meter, bill and collect fees in a fair and rational manner from all customers of utility services in order for CUC to become financially independent of appropriations by the Commonwealth Legislature. All projects of CUC funded either directly by U.S. federal agencies through the CNMI or indirectly as loans from the Commonwealth Development Authority (CDA) and the U.S. Department of Agriculture are included in the scope of the OMB Circular A-133 audit (the "Single Audit"). The U.S. Department of the Interior has been designated as CUC's cognizant agency for the Single Audit.

A. Programs Subject to Single Audit

All of the programs presented in the Schedule of Expenditures of Federal Awards are subject to the Single Audit. U.S. Federal Covenant funds received as loans from CDA and funds received from the U.S. Department of Agriculture as loans are also subject to the Single Audit.

(2) Summary of Significant Accounting Policies

A. Basis of Accounting

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

B. Indirect Cost Allocation

For fiscal year 2000, CUC had no indirect cost agreement with grantor agencies.

COMMONWEALTH UTILITIES CORPORATION

Notes to Schedule of Expenditures of Federal Awards, Continued
Year Ended September 30, 2000

(3) Loan Funds

A. United States Department of the Interior (Commonwealth Development Authority)

Through the *Agreement of the Special Representatives on Future United States Financial Assistance for the Northern Mariana Islands* (the Agreement), the United States Department of the Interior (DOI) granted to the Commonwealth of the Northern Mariana Islands (CNMI) government funds to be used for capital improvement projects. The CNMI government subgranted these funds to the Commonwealth Development Authority (CDA). These funds are to be disbursed in accordance with a seven-year strategic plan for capital improvement projects. Additionally, CDA is required to establish a revolving fund, into which repayments of principal and interest from revenue producing projects shall be deposited for financing of additional revenue producing capital development projects. As such, CDA has entered into a \$40,000,000 and a \$5,500,000 loan agreement with CUC to be used for power related projects and a \$16,135,650 loan agreement to be used for water related projects. At September 30, 2000, \$40,000,000, \$5,500,000 and \$16,068,750 of the loans had been disbursed, respectively. As these funds are not grants but loans of CUC, they are not included in the accompanying Schedule of Expenditures of Federal Awards. However, these funds were reviewed for compliance with federal requirements.

B. U.S. Department of Agriculture, Farmers Home Administration

On June 29, 1988 the CNMI executed a promissory note with the United States Department of Agriculture, Farmers Home Administration for \$1,033,400. The note bears interest at 6-1/8% per annum with repayments due on January 1 beginning in 1989 and through 2008. Proceeds of the loan are to be used for the acquisition and construction of improvements and replacements to the Saipan Water System, which is administered by CUC. As such, CUC is required to deposit all water system revenue and Covenant funds it receives into a water system revenue fund to provide for repayment of the loan. As of September 30, 2000, CUC had not established the required water system revenue fund.

Although CUC administers the use of the proceeds of the loan agreement, the CNMI Department of Finance provides accounting services for all related receipts and disbursements. As of September 30, 2000, the CNMI Department of Finance had disbursed the entire \$1,033,400 relating to the loan agreement. CUC has recognized the related loan payable. CUC has made repayments on the loan in accordance with the agreed-upon repayment schedule. As of September 30, 2000, the remaining balance of the loan payable is \$363,203, of which \$36,539 is classified as the current portion.

As the \$1,033,400 drawdown represents loans not grants, they are not included in the Schedule of Expenditures of Federal Awards. However, the funds have been reviewed for compliance with federal requirements.

(4) Adjustments

During the year ended September 30, 2000, CUC determined that certain receivables (deferred revenues) from grantors at October 1, 1999 were recorded in error. CUC has made adjustments for these errors in the accompanying schedule of expenditures of federal awards.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs
Year Ended September 30, 2000

Section I - Summary of Auditor's Results

1. The Independent Auditors' Report on the financial statements expressed a qualified opinion.
2. Reportable conditions in internal control over financial reporting were identified, some of which are considered to be material weaknesses.
3. One instance of noncompliance considered material to the financial statements was disclosed by the audit.
4. No reportable conditions in internal control over compliance with requirements applicable to major federal awards programs were identified.
5. The Independent Auditors' Report on compliance with requirements applicable to major federal award programs expressed an unqualified opinion.
6. The audit disclosed findings required to be reported by OMB Circular A-133.
7. CUC's major programs were as follows:

<u>Name of Federal Program or Cluster</u>	<u>CFDA Number</u>
U.S. Department of Commerce	11.300
U.S. Department of the Interior	15.875

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

Section II - Financial Statements Findings

<u>Reference Number</u>	<u>Findings</u>	<u>Refer Page #</u>	<u>Questioned Costs</u>
2000-1 - 4	Revenue/Receipts	12 - 15	\$ -
2000-5	Payroll	16	\$ -
2000-6	External Financial Reporting	17	\$ -
2000-7 - 10	Receivables	18 - 21	\$ -
2000-11	Inventory	22	\$ -
2000-12 - 15	Utility Plant	23 - 26	\$ -
2000-16	Other Assets	27	\$ -
2000-17	Payables	28	\$ -
2000-18	Capital Lease	29	\$ -

Section III - Federal Award Findings and Questioned Costs

No findings are reported.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Section II - Financial Statement Findings

Revenue/Receipts

Finding No. 2000-1

Criteria: All recorded revenues and receivables should reflect collectible balances.

Condition: Investigation of long outstanding and undisconnected accounts revealed a listing prepared by the credit and collections division of accounts that were not to be disconnected. The explanation given for the lack of disconnection of these accounts was that these customers had CUC wells, poles, pumps, etc., on their property, and were therefore not billed for utility usage.

Cause: The cause of the above condition is the lack of formal agreements with landowners.

Effect: The effect of the above condition is the misstatement of accounts receivable, bad debt expense and rental expense. Additionally, there could be inequalities in the consideration paid for certain parcels depending on the value of utilities used.

Recommendation: We recommend that CUC execute formal agreements with all landowners for the use of land.

Prior Year Status: Lack of formal agreements with landowners for the use of land was reported as a finding in the audits of CUC for fiscal year 1996 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Revenue/Receipts

Finding No. 2000-2

Criteria: Outstanding receivables should be reviewed on a regular basis to ensure that delinquent accounts are followed up and collected in a timely manner.

Condition: Specific review of long outstanding individual receivables revealed a total of \$1,173,851 in forty-five accounts, which were not disconnected despite more than \$10,000 in each account being over seventy-five days outstanding. Various explanations were given to explain some of the large, long-outstanding balances, however, the majority were not supported by sufficient documentation to evidence the reasons for non-application of CUC's disconnection policy.

Additionally, of the forty-five items tested, two accounts revealed errors in meter readings that resulted in an overstatement of receivables of \$27,222.

Cause: The cause of the above condition appears to be inadequate procedures to ensure timely follow-up and collection of balances due, disconnection of delinquent customers and the accuracy of meter readings.

Effect: The effect of the above condition is an increased potential for bad debts, resulting in significant losses to CUC and the misstatement of revenues and receivables.

Recommendation: We recommend that CUC implement policies and procedures to ensure timely follow-up and collection of balances due. We also recommend that billings be accurately processed.

Prior Year Status: The inadequacy of filing and procedures to ensure timely follow-up and collection of balances due was reported as a finding in the audits of CUC for fiscal years 1994 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Revenue/Receipts

Finding No. 2000-3

Criteria: Proper internal control requires that cashier reports be signed by the preparer and reviewer.

Condition: Of twenty-five cash receipts tested, we noted three instances (receipt date 04/20/2000, CR # 240, cust. # 35271-6; receipt date 04/03/2000, CR # 50, cust. # 29382-9; receipt date 12/20/1999, CR #310, cust. # 35985-1) where the verifier did not sign the daily cash report.

Cause: The cause of the above condition is that the verifier did not sign the daily cash report.

Effect: The effect of the above condition is lack of adherence to established internal control.

Recommendation: We recommend that CUC ensure that established internal control procedures are strictly adhered to.

Prior Year Status: Lack of adherence to established internal controls was reported as a finding in the audit of CUC for fiscal year 1999.

COMMONWEALTH UTILITIES CORPORATION
Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Revenue/Receipts

Finding No. 2000-4

Criteria: Billing reports should be properly filed.

Condition: Of twenty-five billing reports tested, the following could not be provided:

<u>Month</u>	<u>Cycle</u>	<u>Location</u>
12	3	Saipan
11	5	Rota
11	1	Saipan
10	4	Tinian
11	4	Tinian
10	3	Saipan

Cause: The cause of the above condition is improperly filed billing reports.

Effect: The effect of the above condition is lack of billing support.

Recommendation: We recommend that all billing reports be properly filed.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Payroll

Finding No. 2000-5

Criteria: Non-emergency overtime is required to be pre-approved by a supervisor seventy-two hours in advance.

Condition: Of sixty-two payroll disbursements tested, ten employees (check #s 91646, 92294, 94093, 94447, 94949, 95058, 96047, 96304 and 97804 and direct deposit, pay period 19/00, employee # 182) were paid overtime with approval made subsequent to the date the overtime was worked.

Cause: The cause of the above condition is the lack of adherence to prescribed policies and procedures.

Effect: The effect of the above condition is the potential for payment of unnecessary overtime.

Recommendation: We recommend that all non-emergency overtime be pre-approved and appropriately documented.

Prior Year Status: Lack of adherence to prescribed policies and procedures regarding overtime was reported as a finding in the audits of CUC for fiscal years 1996 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

External Financial Reporting

Finding No. 2000-6

Criteria: Without an adequate system to record receivable or payable balances from or to the grantor agency, an entity cannot accurately report on the use of funding.

Condition: CUC is not reconciling receivable or payable balances from or to the grantor agency on a timely basis. CUC's Schedule of Expenditures of Federal Awards (SFA) contains numerous projects which have had no current activity but maintain material receivable or payable balances from or to the grantor agency. Additionally, CUC is not reconciling expenditures of its Schedule of Expenditures of Federal Awards to increases in contributed capital.

Cause: The cause of the above condition is that management has not introduced an adequate system of reconciling receivable or payable balances or contributed capital accounts.

Effect: The effect of the above condition is that amounts due from or to the grantor agency and contributed capital accounts are misstated throughout the year.

Recommendation: We recommend that CUC implement a system whereby a receivable/payable account records all cash received from the grantor agency and records all related expenditures. The account should be reconciled on a monthly basis to the SFA. Additionally, we recommend that expenditures of the Schedule of Expenditures of Federal Awards be reconciled to contributed capital accounts on a timely basis.

Prior Year Status: The non-reconciliation of receivable or payable balances from or to grantor agencies and contributed capital accounts was reported as a finding in the audits of CUC for fiscal years 1990 through 1999.

Auditor Response: CUC is reconciling its SFA to its general ledger due from grantor agencies account through adjustments made directly to the SFA and not through the general ledger.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Receivables

Finding No. 2000-7

Criteria: Disputed customer receivables should be reconciled and resolved in a timely manner.

Condition: CUC's account receivable balance from the CNMI government at September 30, 2000 was \$12,116,804. The CNMI confirmation of balance due at this date indicated an amount materially different from this balance.

Cause: The cause of the above condition is that the balance due from the CNMI has not been reconciled for several years.

Effect: The effect of the above condition is that accounts receivable may be misstated.

Recommendation: We recommend that CUC reconcile the balance due from the CNMI with appropriate CNMI officials and record any necessary adjustments.

Prior Year Status: Lack of reconciliation of the balance due from the CNMI was reported as a finding in the audits of CUC for fiscal years 1995 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Receivables

Finding No. 2000-8

Criteria: Disputed receivable balances should be resolved in a timely manner.

Condition: For ten receivable accounts tested, we noted the following:

- Account # 29619-4 was backbilled for water and sewer charges incurred from 1997 through 1999 for \$138,063. The customer is not making payments on the backbilling.
- Account # 15058-1 was closed in 1993 and written off in 1995 but charges were made to the account in 1996 and 1997 totaling \$100,083. This account was a master account of an apartment building for which individual accounts were established. The account appears to be a duplication of individual accounts charged.
- Account # 21110-2 for \$74,358 has made no payment since 1994. The customer has not been disconnect due to an easement claim.
- Account # 35108-0 for \$70,401 was misstated in total due to meter malfunctions and improper late fees charged.
- Account # 2798-7 reflects a disputed water billing of approximately \$45,000 prior to October 1998. No payments have been made and there has been no action taken.

Cause: The cause of the above condition is a lack of reconciliation of receivable accounts.

Effect: The effect of the above condition is a misstatement of receivable accounts.

Recommendation: We recommend that CUC perform a detailed reconciliation of its receivable accounts.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Receivables

Finding No. 2000-9

Criteria: All advances should be periodically reviewed to determine if the actual expense has been incurred.

Condition: Detailed summaries of other receivables and travel advances outstanding as of September 30, 2000 were found to contain many individual items outstanding for in excess of one year.

Cause: The cause of the above condition is the lack of periodic review of the accounts.

Effect: The effect of the above condition is an overstatement of CUC's assets and an understatement of expenses at September 30, 2000. Additionally, the lack of timely follow-up on travel advances reduces the chance of recovery.

Recommendation: We recommend that long outstanding balances included in the accounts as of September 30, 2000 be reviewed and expensed as necessary. We also recommend that these accounts be reviewed on a monthly basis.

Prior Year Status: The lack of timely follow-up of advances and prepayments was reported as a finding in the audits of CUC for fiscal years 1993 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Receivables

Finding No. 2000-10

Criteria: Prepayments should be properly adjusted for goods/services subsequently received.

Condition: Our review of prepayment schedules indicates that adjustments were not made during the year for goods/services subsequently received. An adjustment at September 30, 2000 was proposed to reflect current year activity.

Cause: The cause of the above condition is the lack of monitoring and timely reconciliation of the account.

Effect: The effect of the above condition is the possible overstatement/understatement of other receivables and expenses.

Recommendation: We recommend that CUC establish policies and procedures to ensure other receivables are adequately monitored and reconciled on a timely basis.

Prior Year Status: Lack of monitoring and timely reconciliation of the prepayments account was reported as a finding in the audit of CUC for fiscal year 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Inventory

Finding No. 2000-11

Criteria: Final inventory summaries should reflect the number of items counted during inventory procedures.

Condition: Our verification of items on hand as of September 30, 2000 revealed thirty-four instances of fifty items tested where the number of items counted varied from the final inventory listing. In addition, the Rota Power Plant physical count adjustments were not recorded at September 30, 2000.

Cause: The cause of the above condition is the application of inadequate inventory procedures.

Effect: The effect of the above condition is a possible misstatement of inventory balances as of September 30, 2000.

Recommendation: We recommend that final inventory listings reflect quantities of items counted.

Prior Year Status: Inaccuracies in inventory items counted as of balance sheet date versus the final inventory listing was reported as a finding in the audits of CUC for fiscal years 1994 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Utility Plant

Finding No. 2000-12

Criteria: Proper accounting for internal construction projects requires that all applicable material and labor costs be assigned to appropriate projects for capitalization and depreciation over the estimated useful life of the resulting asset.

Condition: A detailed listing of construction projects in progress as of September 30, 2000, was not available for our review. Our review of the movement analysis could not be specifically attributed to individual projects. In addition, similar balances carried over from previous years are still maintained within construction work-in-progress, but cannot be attributed to specific projects.

Cause: The cause of the above condition is the lack of proper record maintenance.

Effect: The effect of the above condition is a possible misstatement of the value of construction-in-progress.

Recommendation: We recommend that proper construction work-in-progress records be maintained.

Prior Year Status: The lack of transfer of construction-in-progress projects to fixed assets and the related nonrecording of depreciation was reported as a finding in the audits of CUC for fiscal years 1988 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Utility Plant

Finding No. 2000-13

Criteria: Adequate presentation and control of fixed assets is essential in preparing accurate financial statements. Additionally, unless all fixed assets are recorded, depreciation used in rate settings could be misstated.

Condition: CUC has not taken a physical inventory of fixed assets. Additionally, CUC has no registration system in place to ensure safekeeping of fixed assets.

Cause: The cause of the above condition is that no inventory of fixed assets has been taken.

Effect: The effect of the above condition is that fixed assets and depreciation expense could be misstated. Additionally, a serious weakness in control exists over the safeguarding of fixed assets.

Recommendation: We recommend that CUC perform a physical inventory of all fixed assets on hand, agree the count with its records and make necessary adjustments. Additionally, we recommend that CUC implement a system of tagging fixed assets and perform periodic counts to ensure existence.

Prior Year Status: The lack of control over fixed assets was reported as a finding in the audits of CUC for fiscal years 1988 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Utility Plant

Finding No. 2000-14

Criteria: Utility plant general ledger balances should be supported by a detailed fixed asset register.

Condition: As at September 30, 2000, the fixed asset general ledger accounts were \$778,878 less than the fixed asset register. Additionally, our determination of expected depreciation expense for the year ended September 30, 2000 differed from general ledger depreciation expense by \$1,252,000. CUC could not explain this differential.

Cause: The cause of the above condition is the lack of reconciliation procedures between the general ledger and the fixed asset register and between general ledger depreciation expense and fixed asset register depreciation.

Effect: The effect of the above condition is the misstatement of utility plant and depreciation expense as of September 30, 2000.

Recommendation: We recommend that the fixed asset register be reconciled to the general ledger on a monthly basis.

Prior Year Status: Lack of reconciliation procedures between the general ledger and the fixed asset register was reported as a finding in the audits of CUC for fiscal years 1997 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Utility Plant

Finding No. 2000-15

Criteria: Insurance coverage protects an organization from potential material losses.

Condition: CUC has not obtained insurance for its fixed assets.

Cause: The cause of the above condition is the lack of an adequate policy to ensure insurance coverage.

Effect: The effect of the above condition is the possibility of material losses.

Recommendation: We recommend that CUC implement a policy with respect to required insurance coverage levels.

Prior Year Status: The lack of insurance coverage was reported as a finding in the audits of CUC for fiscal years 1989 through 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Prepayments

Finding No. 2000-16

Criteria: Prepayments should be properly adjusted for goods/services subsequently received.

Condition: Our review of the prepayment schedule indicates that adjustments were not made during the year for goods/services subsequently received. An adjustment at September 30, 2000 was proposed to reflect current year activity.

Cause: The cause of the above condition is the lack of monitoring and timely reconciliation of the account.

Effect: The effect of the above condition is the possible overstatement/understatement of prepayments.

Recommendation: We recommend that CUC establish policies and procedures to ensure prepayments are adequately monitored and reconciled on a timely basis.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Payables

Finding No. 2000-17

Criteria: An effective system of internal control includes policies and procedures to ensure that liabilities are recorded in the appropriate fiscal year.

Condition: Tests of subsequent disbursements determined that material amounts of liabilities relating to the year ended September 30, 2000 were not recorded.

Cause: The cause of the above condition is the lack of appropriate cut-off.

Effect: The effect of the above condition is the misstatement of accounts payable, expenses and construction work-in progress at September 30, 2000.

Recommendation: We recommend implementation of appropriate policies and procedures to ensure recording of all liabilities in the appropriate fiscal year.

Prior Year Status: The lack of appropriate cut-off was reported as a finding in the audits of CUC for fiscal years 1998 and 1999.

COMMONWEALTH UTILITIES CORPORATION

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2000

Capital Lease

Finding No. 2000-18

Criteria: Financial Accounting Standards Board (FASB) Statement No. 13, *Accounting for Leases*, requires that the lessee record a capital lease as an asset and an obligation at an amount equal to the present value of minimum lease payments during the lease term. However, if the amount so determined exceeds the fair value of the leased property at the inception of the lease, the amount recorded as the asset and liability shall be fair value.

Emerging Issues Task Force (EITF) Issue No. 01-8 states that in certain circumstances energy-related contracts may represent lease transactions, and the evaluation of whether an arrangement contains a lease within the scope of FASB No. 13 should be based on the substance of the arrangement and whether the use of specific property, plant and equipment is necessary in the fulfillment of the arrangement.

Condition: CUC entered into an agreement with a contractor for the construction, maintenance and operation, and transfer of ownership of a 10 Megawatt Power Plant on the island of Tinian. The agreement is for a guaranteed price of \$9,959,000 plus interest and fees of \$11,641,000 payable over ten years. During this period, the contractor will maintain and operate the power plant and be paid operation, production and maintenance fees in addition to the guaranteed price. The power plant will be turned over to CUC at the end of the ten year period.

CUC has determined that this agreement is in fact a capital lease and that the payments made under the agreement are lease payments. As such, CUC recorded \$9,959,000 as plant and obligations under capital lease.

CUC has been unable to determine whether the guaranteed price of \$9,959,000, in fact, constitutes the fair value of the leased property.

Cause: The cause of the above condition is that CUC has not determined the actual cost of the power plant or obtained an appraisal.

Effect: The effect of the above condition is the inability to determine whether the recording of the plant and obligation under capital lease is in accordance with FASB No. 13 and EITF No. 01-8.

Recommendation: We recommend that CUC determine the actual cost of the plant, or obtain an appraisal of the plant for purposes of compliance with the EITF.

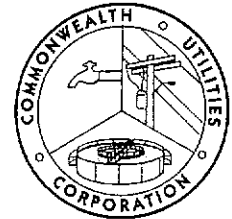
COMMONWEALTH UTILITIES CORPORATION

Unresolved Prior Year Findings and Questioned Costs
Year Ended September 30, 2000

The status of unresolved prior year findings is discussed within the Schedule of Findings and Questioned Costs section of this report (pages 10 through 28).



Commonwealth Utilities Corporation



Corrective Action Plans to Questioned Costs and Findings included in the Independent Auditors' Reports on Internal Control and Compliance for the Year Ended September 30, 2000

Financial Statements Findings Section

Revenue/Receipts

Finding No. 2000-1

CUC agrees with the finding. CUC has forwarded all easement disputes on file to outside counsel for immediate resolution. All but two disputes (involving eight accounts) forwarded to counsel have either been resolved or is pending resolution. The unresolved dispute account holders are requesting administrative hearing to resolve their dispute. CUC has advertised for an administrative hearing officer and will adhere to the customers' rights to an administrative hearing.

To prevent the occurrence of future easement claims, CUC requires all new connections to be accompanied with dedication of easement by the applicant or owners of the land. For its own in house projects, CUC has hired an easement specialist to ensure that CUC projects do not encroach private property. For those projects requiring the use of private property, CUC shall formally seek an agreement with the affected parties prior to using such properties.

Revenue/Receipts

Finding No. 2000-2

CUC partially agrees to the finding. While there are a few accounts that CUC is unable to explain the lack of adherence to the disconnection policy, most of the accounts are in fact accounts with long standing disputes or accounts that were in the process for adjustment.

CUC currently requires monthly reviews of accounts with disputes. A monthly status report of unresolved disputes is provided to the Director and Comptroller to ensure timely resolution. The Comptroller has been tasked to monitor and ensure that disputes are resolved in a timely manner and that accounts requiring collection action is initiated.

To ensure adherence to the disconnection and reconnection policies, Credit & Collection (C&C) is tasked to properly document the reasons for noncompliance (i.e. billing, easement disputes). Documentation will require that C&C implement filing procedures to record such disputes. Customer service shall be required to properly document customer disputes and forward copies of disputes to C&C.

Revenue/Receipts

Finding No. 2000-3

CUC agrees with the finding. A memorandum prepared by the Treasurer dated June 30, 2000 was sent to all cashiers and supervisors reminding them that daily cashier reports should be signed. Cashiers and their supervisors have duly acknowledged the receipt of the memorandum. To ensure compliance with the memorandum, CUC's Treasurer has been instructed to review cashier reports daily to ensure strict compliance to internal control procedures. Cashiers and supervisors not adhering to procedures will be duly warned and reprimanded (if necessary).

Revenue/Receipts

Finding No. 2000-4

CUC partially agrees with the finding. The Billing Supervisor transferred all the FY 2000 billing reports to the container at Power Plant 4 for safekeeping. CUC agrees that the billing reports were not properly filed because six (6) reports mentioned could not be located during the audit. However, these reports are saved in the system and the EDP staff can retrieve and generate a query report about the account history of the customers sampled for testing.

We need more information on this finding. We need to know the specific reports needed for testing. For example, edit sheets are computer-generated. They are generated after uploading the meter reading handheld device. However, these reports cannot be recreated if EDP staff fails to save in back-up files.

The Billing Section and the EDP staff were advised to ensure that billing data such as meter readings are electronically saved and backed-up.

Payroll

Finding No. 2000-5

CUC agrees with this finding. Pre-approved overtime is required to be approved by the Director or his designee not supervisors.

All managers have been reminded to comply with the overtime policy and procedures. The memorandum states that the Director will strictly enforce this policy and will not hesitate to take necessary administrative actions to ensure compliance (i.e. reprimands and demotions).

External Financial Reporting

Finding No. 2000-6

CUC agrees with this finding. CUC has prepared the procedures below to address the finding.

Recording of Grants

Objectives:

1. To implement a system to record receivable/payable balances from/to grantor agencies.
2. To monitor all contributed assets from Federal and CNMI governments.

External Financial Reporting, Continued

Finding No. 2000-6, Continued

Procedures:

New Grants

1. Grants Section forwards to Accounting copies of all the documents supporting approval of the grant.

Direct Grants:

- Grantor Agency's letter of approval to award
- Contract (including change orders, if any)

CNMI 702 CIP:

- Public Law/Appropriations/Resolutions
- DOI/OIA's Approval Letter
- Allotment Advice
- Contract (including change orders, if any)

2. Accounting opens a folder and a subsidiary ledger for each direct grant/CIP project for reference and monitoring purposes.

Payment Processing

A. Direct grants (CUC advances payment and requests for reimbursement from grantor)

1. Division Manager certifies the invoice(s) or completion of work and submits payment request to Grants Section (invoice is supported by an approved purchase order and completion of work is approved by Executive Director).
2. Grants Section processes the payment request and forwards to Accounts Payable for check preparation.
3. Grants Section keeps a ledger of payment requests/drawdowns for each project.
4. Upon receipt of payment request from Grants, Accounts Payable cuts the check and forwards to Grants Section a copy of the check for reimbursement purposes.
5. Grants Section prepares necessary documents for reimbursement processing and distributes copies of the request for reimbursement to the following:
 - Executive Director
 - Accounting
 - Treasury
 - Division Manager

B. 702 CIP (DOF processes payment)

1. Division Manager certifies the invoice(s) or completion of work and submits payment request to Grants Section.

External Financial Reporting, Continued

Finding No. 2000-6, Continued

2. Grants Section processes the payment request and forwards a copy to Accounting.
3. Grants Section keeps a ledger of payment requests/drawdowns for each project.

Accounting for Grants

1. Upon receipt of the copy of payment request from Grants, Accounting performs the following procedures:
 - Prepare journal entries
 - Update of subsidiary ledgers (SL) to monitor available balance of grant by subtracting from the approved grant amount/contract amount all the drawdowns or payment requests. SL details are:
 1. PR No.
 2. Billing date
 3. Amount
 4. Reference JV No.
 5. CNMI share
 6. Federal share
 - File documents in their individual folders for easy reference.
2. Treasurer/Cashier informs Accounting of any reimbursement/payment received from grantor agency.
3. Cashier prepares charge voucher and forwards to Accounting the yellow copy with attached supporting documents (e.g. check stub, transmittal letters, etc.).
4. Upon receipt of copy of charge voucher and attachments, Accounting updates the subsidiary ledger and files documents to their individual folders.

Monthly Reconciliation Procedures

Grants Section:

1. Prepares the following reports:
 - Monthly Fund Status Report for on-going CIP's (separate columns for local matching share and federal share)
 - Grant/Project Ledger showing available balance/project drawdowns
2. Forwards monthly report to the following:
 - Accounting
 - Division Managers concerned

External Financial Reporting, Continued

Finding No. 2000-6, Continued

Accounting Section:

1. Prints subsidiary ledgers for each grant/project
2. Prepares the following reports:
 - Schedule of Due from Grantor Agency as of end of the month
 - Schedule of 702 CIP's (CWIP/CNMI and Federal share)
3. Reconciles with monthly reports obtained from Grants Section
4. Reconciles general ledger figures to subsidiary ledgers

Completed Projects Funded by Grants

1. Division Managers certifies completion of the project and approved by the Executive Director. The following documents are required by Accounting to close out a CWIP account and transfer to its proper fixed asset account:
 - Certificate of Completion
 - Final Acceptance
 - Turn-Over Certificate
2. Accounting processes closing of the CWIP and enters to the Fixed Asset system.

Receivables

Finding No. 2000-7

CUC agrees with the finding. CUC will initiate discussion with CNMI Department of Finance to reconcile the outstanding receivable. When completed, the general ledger and chief accountant will prepare the appropriate adjustment. The adjustment will be subject to review and approval by the Assistant Comptroller or Comptroller.

Receivables

Finding No. 2000-8

CUC agrees that disputed balances should be resolved timely.

Of the five accounts mention, CUC made adjusting entries for Account # 35108-0 in March 2001 and the account balance now reflects the correct amount due.

However, CUC has not yet adjusted the four remaining accounts. Account # 21110-2 has an easement claim. For comments regarding easement claims, see CUC response to Finding No. 2000-1. The other three accounts have billing disputes. For comments regarding billing disputes, see CUC response to Finding 2000-2, middle paragraph.

Receivables, Continued

Finding No. 2000-8, Continued

Further, the Comptroller is planning to reorganize Accounting and give one manager overall responsibility for three sections: Accounts Receivable, Billing and Credit and Collections. The manager will be tasked to ensure that all billing disputes are resolved and billing errors are corrected promptly, that all uncollectible accounts are written-off as bad debts, and that amounts due are paid or acceptable payment arrangements are made. In addition, the manager will forward all other unpaid accounts to the CUC Legal Counsel to pursue collection.

Receivables

Finding No. 2000-9

On a monthly basis, CUC will review the status of employee travel and other advances and will initiate collection action on advances that are not timely liquidated or travels that have outstanding balances. To ensure that expenses are timely recorded, CUC will enforce its payroll deduction policies for travel authorizations that are not liquidated. In addition, accounting will require the Human Resources section to obtain clearance from the accounting section prior to the processing of their resignation action and immediately inform accounting of personnel who are resigning so as to allow accounting to require immediate payroll deduction for all outstanding balances.

Receivables

Finding No. 2000-10

CUC agrees with the finding. To correct this finding, CUC is requiring that Accounts Payable section record and reclassify the purchases as the original invoices and the receiving report are received. In addition to this procedure, CUC will review monthly its prepayment purchases to monitor and ensure that the purchases are timely received and recorded.

Inventory

Finding No. 2000-11

CUC agrees with the finding. CUC has recently hired a fixed asset/inventory accountant to implement procedures to ensure that physical counts match the final inventory listing and the withdrawal of inventory is properly recorded. In addition to the procedures to be implemented, semi-annually and annually CUC will reconcile counts against the final inventory listing to ensure proper recording of the physical counts.

Utility Plant

Finding No. 2000-12

CUC agrees with the finding. CUC has been properly capitalizing labor and material charges to its internal construction projects but has been unable to timely close completed projects. Again, CUC has hired a fixed asset accountant who has been tasked to address its timeliness issue. CUC anticipates to address the backlog files issue either by seeking professional service assistant or internally or combination thereof.

Utility Plant

Finding No. 2000-13

CUC partially agrees with the finding. Although we have not taken a physical inventory of fixed assets, we have a registration system in place to keep track of all our fixed assets purchases.

Acquired fixed assets are processed through our accounts payable system and are initially lodged to a fixed asset clearing account for review by our chief accountant. The clearing account is analyzed weekly and the corresponding item is assigned a property tag number and its applicable useful life. The property is then recorded in the proper account code in the fixed assets register. Monthly, the fixed asset register total is reconciled with the corresponding general ledger balance. Completed CIPs are likewise recorded in the fixed assets register monthly.

CUC is currently backlogged in closing work orders of system improvements and new customer installations. However, work order costs are initially recorded as Construction Work in Progress (CWIP). The delayed closing has caused the understatement of fixed assets and thereby affecting our financial statement.

To address CUC's lack of inventory of fixed assets and timeliness of closing work orders, CUC has announced and selected a fixed assets/inventory accountant to conduct a complete count of fixed assets and to close complete work orders. CUC plans to seek proposals from qualified firms to assist in the inventory and valuation of its fixed assets. CUC expects to complete both the inventory and close all work orders by Fiscal Year 2002.

Utility Plant

Finding No. 2000-14

CUC partially agrees with the finding. Since February 2000, the Comptroller's office, accounting section, reconciled the utility plant general ledger balances to the detailed fixed asset register. The reported condition was due primarily to the auditors' adjustment, which has subsequently been recorded.

Utility Plant

Finding No. 2000-15

CUC agrees with the finding. CUC currently has a fixed asset schedule that requires review and confirmation. CUC is in the process of hiring a fixed asset/inventory accountant to review and confirm this listing. Upon completion of the review, CUC will solicit insurance coverage for its fixed assets. The recommendation to insure CUC construction projects has been forwarded to the Procurement manager to prepare to incorporate into its procurement requirements. This change of policy will be presented to the board for adoption.

Other Assets

Finding No. 2000-16

CUC agrees with the finding. To correct this finding, CUC is requiring that Accounts Payable section record and reclassify the purchases as the original invoices and the receiving report are received. In addition to this procedure, CUC will review monthly its prepayment purchases to monitor and ensure that the purchases are timely received and recorded.

Payables

Finding No. 2000-17

CUC agrees with the finding. The policies and procedures to record payable are in place. However, without a proper procurement system, these procedures are prone to untimely recognition of expenses. Most of the findings relate to CUC's untimely recording of CWIP projects that have not been closed. CUC is revisiting its procedures in closing CWIP projects to ensure that it records its expenses (i.e. depreciation) in the proper fiscal period.

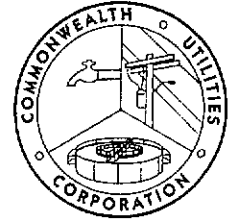
Capital Lease

Finding No. 2000-18

CUC agrees with the finding and will attempt to determine the fair market value of the Tinian Power Plant.



Commonwealth Utilities Corporation



Summary of Schedule of Prior Audit Findings

Status of audit findings included in the schedule of findings and questioned costs for the year ended September 30, 1999:

Financial Statement Findings

- Finding No. 99-1 - Not corrected. See corrective action plan to Finding 2000-1.
- Finding No. 99-2 - Not corrected. See corrective action plan to Finding 2000-2.
- Finding No. 99-3 - Not corrected. See corrective action plan to Finding 2000-3.
- Finding No. 99-4 - Corrective action was taken.
- Finding No. 99-5 - Not corrected. See corrective action plan to Finding 2000-5.
- Finding No. 99-6 - Not corrected. See corrective action plan to Finding 2000-6.
- Finding No. 99-7 - Corrective action was taken.
- Finding No. 99-8 - Not corrected. See corrective action plan to Finding 2000-7.
- Finding No. 99-9 - Not corrected. See corrective action plan to Finding 2000-9.
- Finding No. 99-10 - Not corrected. See corrective action plan to Finding 2000-10.
- Finding No. 99-11 - Not corrected. See corrective action plan to Finding 2000-11.
- Finding No. 99-12 - Not corrected. See corrective action plan to Finding 2000-12.
- Finding No. 99-13 - Not corrected. See corrective action plan to Finding 2000-13.
- Finding No. 99-14 - Not corrected. See corrective action plan to Finding 2000-14.
- Finding No. 99-15 - Not corrected. See corrective action plan to Finding 2000-15.
- Finding No. 99-16 - Corrective action was taken.
- Finding No. 99-17 - Not corrected. See corrective action plan to Finding 2000-17.
- Finding No. 99-18 - Corrective action was taken.