

COMMONWEALTH UTILITIES CORPORATION
(A Component Unit of the Commonwealth
of the Northern Mariana Islands)

Report on the Audit of Financial Statements
in Accordance with the Uniform Guidance
September 30, 2021

COMMONWEALTH UTILITIES CORPORATION
(A Component Unit of the Commonwealth
of the Northern Mariana Islands)

Financial Statements and Supplementary Information
September 30, 2021
(With Independent Auditor's Report Thereon)

COMMONWEALTH UTILITIES CORPORATION
(A Component Unit of the Commonwealth of the Northern Marianas Islands)

Report on the Audit of Financial Statements in Accordance with the Uniform Guidance
Year ended September 30, 2021

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Commonwealth Utilities Corporation

Report on the Financial Statements

We have audited the accompanying financial statements of the Commonwealth Utilities Corporation (CUC), a component unit of the Commonwealth of the Northern Mariana Islands (CNMI), which comprise the statement of net position as of September 30, 2021, and the related statement of revenues, expenses and changes in net position and cash flows for the year then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

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Basis for Qualified Opinion

We were unable to determine the propriety of inventory quantities as we did not observe the inventory count as of September 30, 2021.

Qualified Opinion

In our opinion, except for the effects of the matter described in the “Basis for Qualified Opinion” paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Commonwealth Utilities Corporation as of September 30, 2021, and the changes in its net position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management’s Discussion and Analysis on pages 4 through 12 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management’s responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise CUC’s basic financial statements. The Schedule of Revenues, Expenses and Changes in Net Position on a Divisional Basis for the year ended September 30, 2021 (pages 39-40) is presented for purposes of additional analysis and is not a required part of the basic financial statements. The Schedule of Revenues, Expenses and Changes in Net Position on a Divisional Basis is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, except for the effects of the matters described in the “Basis for Qualified Opinion” paragraphs, the Schedule of Revenues, Expenses and Changes in Net Position on a Divisional Basis is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 21, 2023 on our consideration of CUC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of CUC's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering CUC's internal control over financial reporting and compliance.

Bryce Combs & Associates

Saipan, MP
September 21, 2023

COMMONWEALTH UTILITIES CORPORATION
(A Component Unit of the CNMI Government)

MANAGEMENT'S DISCUSSION & ANALYSIS
September 30, 2021

This discussion and analysis of the Commonwealth Utilities Corporation's (CUC) financial performance provides an overview of CUC's activities for the fiscal year ended September 30, 2021 with comparisons to the prior fiscal year ended September 30, 2020. We encourage readers to consider the information presented here in conjunction with the financial statements, related notes, and supplementary information (pages 13 through 40).

	<u>2021</u>	<u>2020</u>	<u>\$ Change</u>	<u>% Change</u>
Assets				
Current unrestricted assets	\$ 87,344,331	\$ 69,019,389	\$ 18,324,942	26.6%
Current restricted assets	12,742,111	12,131,154	610,957	5.0%
Noncurrent assets	120,942,103	118,665,292	2,276,811	1.9%
Deferred outflows of resources	<u>6,752,827</u>	<u>7,341,652</u>	<u>(588,825)</u>	-8.0%
	<u>\$ 227,781,372</u>	<u>\$ 207,157,487</u>	<u>\$ 20,623,885</u>	10.0%
Current liabilities	\$ 36,569,675	\$ 29,014,154	\$ 7,555,521	26.0%
Noncurrent liabilities	10,429,325	17,332,035	(6,902,710)	-39.8%
Deferred inflows of resources	66,102	71,606	(5,504)	-7.7%
Net investment in capital assets	120,942,103	118,665,292	2,276,811	1.9%
Restricted net position	45,000,000	45,000,000	-	0.0%
Unrestricted net position	<u>14,774,167</u>	<u>(2,925,600)</u>	<u>17,699,767</u>	-605.0%
	<u>\$ 227,781,372</u>	<u>\$ 207,157,487</u>	<u>\$ 20,623,885</u>	10.0%
Revenues, Expenses and Changes in Net Position				
	<u>2021</u>	<u>2020</u>	<u>\$ Change</u>	<u>% Change</u>
Net operating revenues	\$ 68,579,427	\$ 82,065,552	\$ (13,486,125)	-16.4%
Operating expenses	<u>83,267,800</u>	<u>81,639,092</u>	<u>1,628,708</u>	2.0%
Operating income (loss)	(14,688,373)	426,460	(15,114,833)	3544.3%
Non-operating revenues, net	<u>20,888,589</u>	<u>5,209,953</u>	<u>15,678,636</u>	300.9%
Income before capital contributions from primary government	6,200,216	5,636,413	563,803	10.0%
Capital contributions from primary government	<u>14,082,887</u>	<u>2,398,845</u>	<u>11,684,042</u>	487.1%
Change in net position	20,283,103	8,035,258	12,247,845	152.4%
Net position at beginning of year	160,739,692	152,704,434	8,035,258	5.3%
Adjustments to net position at beginning of year	<u>(306,525)</u>	<u>-</u>	<u>(306,525)</u>	0.0%
Net position at end of year	<u>\$ 180,716,270</u>	<u>\$ 160,739,692</u>	<u>\$ 19,976,578</u>	12.4%

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September 30, 2021

For the year ended September 30, 2021, CUC incurred a loss from operations of about \$14.7 million as compared to an income of \$426,460 for the year ended September 30, 2020.

OVERVIEW OF THE FINANCIAL STATEMENTS

The Financial Section of this report presents the CUC's financial statements as two components: basic financial statements, and notes to the financial statements. It also includes supplemental information.

Basic Financial Statements

The *Statement of Net Position* present information on assets and deferred outflows of resources, and liabilities and deferred inflows of resources with the difference between them presented as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of CUC is improving or deteriorating.

The *Statement of Revenues, Expenses and Changes in Net Position* reports how net position has changed during the year. It compares related operating revenues and operating expenses connected with CUC's principal business of providing power, water, and sewer services. Operating expenses include the cost of direct services to customers, administrative expenses, contracted services, and depreciation on capital assets. All other revenues and expenses are reported as non-operating.

The *Statement of Cash Flows* reports inflows and outflows of cash, classified into four major categories:

- Cash flows from operating activities include transactions and events reported as components of operating income in the Statement of Revenues, Expenses and Changes in Net Position.
- Cash flows from non-capital financing activities include operating grant proceeds.
- Cash flows from capital and related financing activities include the borrowing and repayment (principal and interest) of capital-related debt, the acquisition and construction of capital assets, and the proceeds of capital grants and contributions.
- Cash flows from investing activities include proceeds from sale of investments, receipt of interest and changes in the fair value of investments subject to reporting as cash equivalents. Outflows in this category include the purchase of investments.

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MANAGEMENT'S DISCUSSION & ANALYSIS

September 30, 2021

Notes to the Financial Statements

Various notes provide additional information that is essential to a full understanding of the data provided in the basic financial statements and are found immediately following the financial statements to which they refer.

Other Information

This report also presents certain supplementary information concerning CUC's Schedule of Revenues, Expenses and Changes in Net Position on a Divisional Basis (see pages 39 through 40).

ANALYSIS OF BASIC FINANCIAL STATEMENTS

Condensed Statements of Revenues, Expenses and Change in Net Position

	<u>2021</u>	<u>2020</u>
Operating revenues, net	\$ 68,579,427	\$ 82,065,552
Operating expenses	<u>83,267,800</u>	<u>81,639,092</u>
Earnings (loss) from operations	(14,688,373)	426,460
Nonoperating revenues (expenses), net	21,477,418	5,209,953
Change in recovery of fuel costs	<u>(588,829)</u>	<u>-</u>
Net earnings (loss) before capital contributions and federal grants	6,200,216	5,636,413
Capital contributions and federal grants	<u>14,082,887</u>	<u>2,398,845</u>
Change in net position	20,283,103	8,035,258
Adjustment to retained earnings	(306,525)	-
Net position, beginning	<u>160,739,692</u>	<u>152,704,434</u>
Net position, ending	<u>\$ 180,716,270</u>	<u>\$ 160,739,692</u>

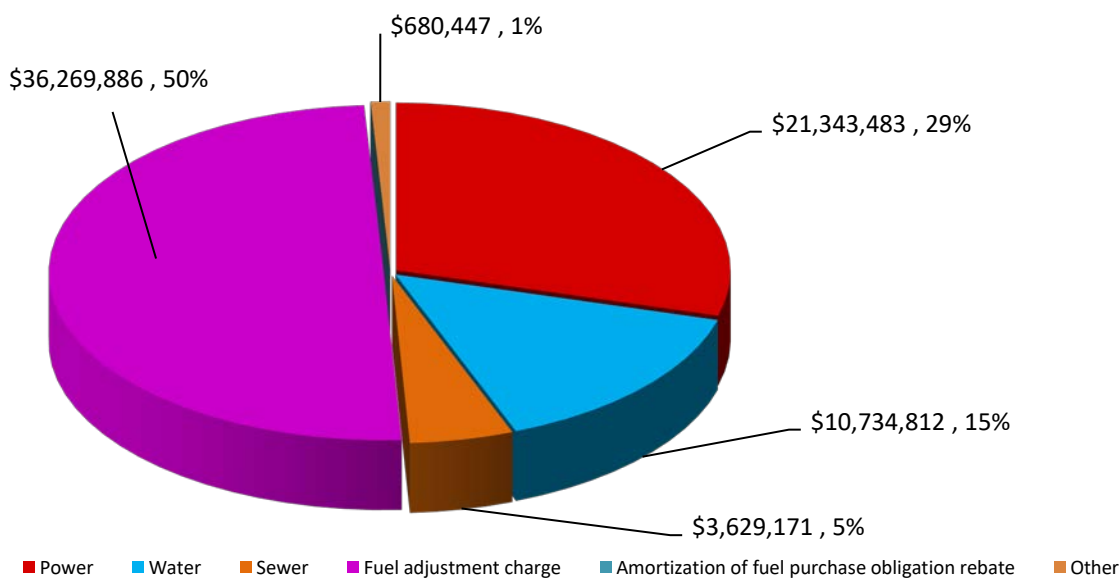
COMMONWEALTH UTILITIES CORPORATION
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MANAGEMENT'S DISCUSSION & ANALYSIS
September 30, 2021

Financial Highlights

Operating Revenues

	<u>2021</u>	<u>2020</u>	<u>\$ Change</u>	<u>% Change</u>
Power	\$ 21,343,483	\$ 29,225,612	\$ (7,882,129)	-27.0%
Water	\$ 10,734,812	\$ 14,389,738	\$ (3,654,926)	-25.4%
Sewer	\$ 3,629,171	\$ 4,744,216	\$ (1,115,045)	-23.5%
Fuel adjustment charge	\$ 36,269,886	\$ 34,707,000	\$ 1,562,886	4.5%
Amortization of fuel purchase obligation rebate	\$ -	\$ 631,316	\$ (631,316)	100.0%
Other	\$ 680,447	\$ 870,780	\$ (190,333)	-21.9%
Total	<u>\$ 72,657,799</u>	<u>\$ 84,568,662</u>	<u>\$ (11,910,863)</u>	-14.1%

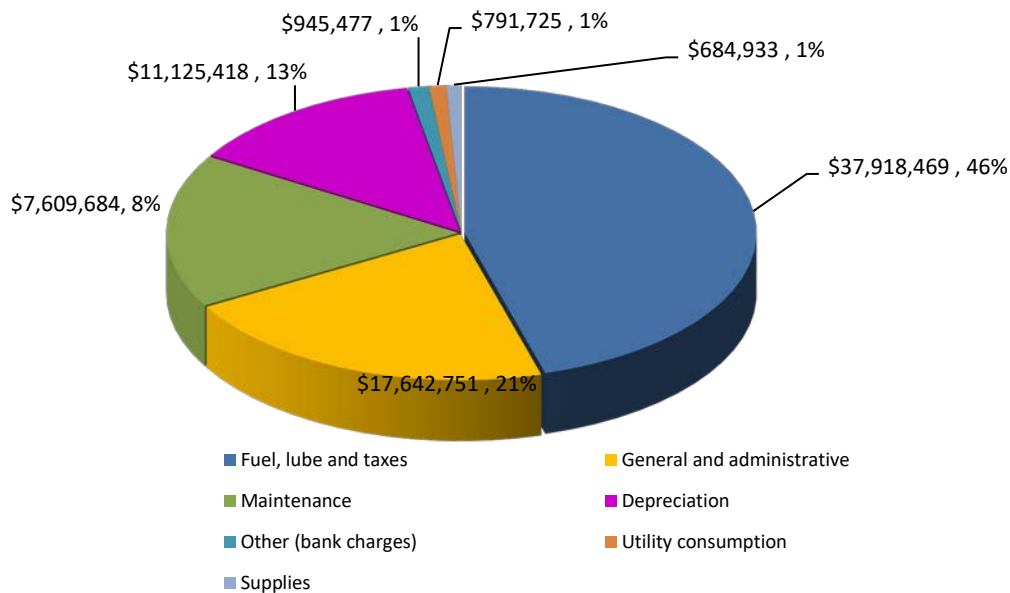


COMMONWEALTH UTILITIES CORPORATION
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MANAGEMENT'S DISCUSSION & ANALYSIS
September 30, 2021

Operating Expenses

	<u>2021</u>	<u>2020</u>	<u>\$ Change</u>	<u>% Change</u>
Fuel, lube, and taxes	\$ 37,918,469	\$ 37,875,495	\$ 42,974	0.1%
General and administrative	\$ 17,642,751	\$ 19,372,870	\$ (1,730,119)	-8.9%
Maintenance	\$ 14,159,027	\$ 11,731,862	\$ 2,427,165	20.7%
Depreciation	\$ 11,125,418	\$ 10,213,930	\$ 911,488	8.9%
Other (bank charges)	\$ 945,477	\$ 890,398	\$ 55,079	6.2%
Utility consumption	\$ 791,725	\$ 888,323	\$ (96,598)	-10.9%
Supplies	\$ 684,933	\$ 666,214	\$ 18,719	2.8%
Total	<u>\$ 83,267,800</u>	<u>\$ 81,639,092</u>	<u>\$ 1,628,708</u>	2.0%



CUC performed a physical count of all fixed assets and inventories and compared them to the accounting records of CUC for completeness and accuracy. Furthermore, CUC maintains and performs the full valuation of its fixed assets and inventories. CUC expanded its financial software capabilities to include the Fixed Asset Module of the GP system.

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Capital Assets

At September 30, 2021, CUC had \$121,252,254 invested in capital assets, net of depreciation where applicable, including electric plant, water plant, sewer plant, administrative equipment, and construction in progress.

	<u>2021</u>	<u>2020</u>
Utility plant in service		
Electric plant	\$ 181,115,573	\$ 181,681,008
Water plant	88,906,700	85,703,444
Sewer plant	56,459,596	55,835,152
Administrative equipment	<u>4,367,733</u>	<u>4,405,904</u>
	330,849,602	327,625,508
Accumulated depreciation	<u>(225,558,463)</u>	<u>(215,982,647)</u>
Depreciable assets, net	105,291,139	111,642,861
Construction work-in progress	<u>15,650,964</u>	<u>7,022,431</u>
Capital assets, net	<u>\$ 120,942,103</u>	<u>\$ 118,665,292</u>

For additional information regarding capital asset activity, refer to Note 7 in the accompanying notes to the financial statements.

Obligation under estimated environmental remediation costs

CUC has recorded a liability for estimated liability related to environmental remediation costs assessed by Federal government agencies at September 2021 and 2020 as follows:

	<u>2021</u>	<u>2020</u>
U.S. Environmental Protection Agency – long term	\$ 223,125	\$ -
U.S. Coast Guard – long term	839,375	-
Current portion	<u>375,000</u>	<u>-</u>
Total obligation recognized	<u>\$ 1,437,500</u>	<u>\$ -</u>

For additional information regarding this obligation, refer to Note 13 in the accompanying notes to the financial statements.

EXECUTIVE SUMMARY & OUTLOOK – FY2021

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(A Component Unit of the CNMI Government)

MANAGEMENT'S DISCUSSION & ANALYSIS

September 30, 2021

Overview

FY 2021 has been difficult both operationally and financially for the Commonwealth Utilities Corporation (CUC). Coming off a major typhoon, Yutu, needing to cleanup, repair and reestablish systems that were damaged and then sliding into the COVID-19 pandemic which severely damaged revenue generation throughout the CNMI due to the loss of Saipan's only industry, tourism, brought about a dramatic turn in events. CUC needed to remain the ultimate safety net for power, water, and sewer services despite the loss of revenue. CUC's cashflow each month went from \$9 million or more to \$5 million and less which required commitments from all divisions that there would be no overtime which would now be replaced with flex-time, all cell phones provided by the utility were turned in and shifted to personal responsibility, staffing was prioritized when vacancies occurred, vacations were cancelled, and maintenance was pulled back to critical repairs only with normal preventive maintenance being delayed pending available funds. The intent of management was to avoid austerity measures that other agencies and departments of the government were following which required losing 8 or 16 hours per week, with extensive personnel reductions through furloughs. Utilities are by nature 24 hour operations and cannot afford the luxury of waiting to respond to an emergency that affects the well-being and the quality of life of every resident on the islands of the CNMI.

Management's immediate effort was to hire two grant writers that could be used to identify funding that could be used to make prioritized repairs and react to funding opportunities as they arose during this period of the CARES Act and the American Rescue Plan Act. Both Acts and FEMA provided extensive financial resources as a result of Yutu and the Pandemic. With true fiscal discipline, CUC survived this financial downfall fairly well.

On top of the funding effort, is CUC's plan to review and modify the organization charts of the Water, Sewer, and Engineering sections. With the amount of funding coming our way, we have the chance to make some real change. The intent is to add new service areas for staffing, develop a middle management tier that has not been officially established, and to add several new field activities now that funding has made this equipment available. This includes the creation of a new fats, oils and grease program with the purchase of a new Vactor truck and CUES TV/Grouting system. This will go a long way to televise and grout failing lines, reduce infiltration and inflow from sewers, and put every inch of pipe on a GPS location for our GIS system. With a new survey group under Engineering but located in the field with Operations, new service requests can be better designed and laid out for installation, meter change outs can be better done with testing and more frequently, and shop drawings better done of work sites where key repairs are made.

Power Generation

Throughout these two events, CUC was in a major effort to perform extensive maintenance repairs to several of its critical engines in Power Plant #1. Funding became a matter of real concern since the age of the engines (45 plus years old) and the condition of the engines requires the procurement of new custom manufactured parts that put repairs into the several millions of dollars during a time when we are not earning excess income. Fuel costs are the largest percentage of spending we have

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MANAGEMENT'S DISCUSSION & ANALYSIS

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with salaries coming next and operations drawing the fewest dollars. CUC began working with MAN/BMW who are the original providers of the engines to assist with maintenance repairs after CUC lost thirteen (13) CW mechanics and who have never been replaced. At the point of startup on Engine #5, there was a problem with the controlled start and the newly maintained engine was damaged to the point we are now planning on replacing it. Parts were taken from the engine to shorten the timeline on the repairs to Engine #7 but the dilemma was now losing the power production and a solution to its replacement was required. The outcome of the failure pushed for mediation between CUC and MAN/BMW such that they have offered a considerable price reduction on a replacement engine. Repairs have been made to three foundations to assure they are capable of handling the weight and the vibration of a new replacement engine if CUC is able to arrange financing for them.

On Rota, power generation suffered a similar problem when their lead engine went down and CUC had to acquire a replacement engine on an emergency basis initiated by the Board. The engine was acquired from California and delivered within twelve weeks of purchase. In the meantime, the power plant relied on its backup generators to sustain power for the island.

On Tinian, Telesource has been working for most of the past two years to bring its power facility back up to good condition in anticipation of a new bid in October, 2021. The military is working with Power and Water on getting organized for the planned diversion project and airport expansion.

Power Transmission and Distribution

With two typhoons and a Pandemic affecting travel, FEMA plans other major investments in Tinian and Rota to repair down wooden poles with concrete. During the pandemic both islands have been event free of any significant repairs. Plans are still developing for further power pole replacements and potentially transformers as they are aging and consideration is being given to plan for their replacement.

Water Operations

Over the course of FY2021, Water Operations has been affected by a loss of staffing that they have not been able to efficiently replace and by the loss of overtime which reduces the number of effective hours of coverage even though every effort is made to cover a twenty-four hour period. Staff work long hours and they are tiring from the additional effort and the loss of the one incentive they have which is overtime work. The Division has been pursuing main breaks, meter change outs and new water line installations. But main breaks have been surging since the power supply has been regularly dropping service due to a variety of maintenance concerns which causes surging of water lines as they refill and numerous main breaks due to age and condition of the mains.

The issue of PFOS/PFOA developed over this period and a solution has been implemented and put in place. The ten (10) new duplex water treatment units that contain granular activated carbon (GAC) have been installed at the ten highest producing concentration of wells affected by this

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material in the water supply. The intent is to meet and/or be well below EPA's advisory level and the CNMI's MCL level of 70 ppt. This will be a long term initiative to keep control over. Funding for this project was from EPA.

At the same time, CUC has been looking to take advantage of American Rescue Plan Act (ARPA) funds to make major improvements in the water and wastewater system. There is a very good chance with funding targeted on replacing long runs of water mains CUC can reduce non-revenue water loss by a significant amount. CUC has \$138 million to spend in the next 3 to 4 years on all three islands to include funding for new Homesteads that require water and sewer systems.

Wastewater Operations

Just as Water is benefitting from the availability of ARPA funding, Wastewater systems will also benefit. By replacing and extending new sewers into septic areas of the community, we can eliminate failing collection mains and gain new sewer customers which we sorely need to make and sustain affordable rates. These repairs are now benefitting from the ARPA funding that is funding these repairs while the financial environment on the island waits for the tourist industry to return after mid-July 2021.

Funding has been made available for the feasibility studies for the Wastewater Treatment System for the Island of Tinian and Rota.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, customers, and creditors with a general overview of the CUC's finances and to demonstrate accountability for the funds it manages. Please direct any questions about this report or requests for additional information about CUC's finances to:

Commonwealth Utilities Corporation
Attn: Executive Director
PO Box 501220
Saipan, MP 96950
Or call (670) 664 4282

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)
Statement of Net Position
As of September 30, 2021

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES

Current assets:	
Cash and cash equivalents - unrestricted	\$ 45,983,449
Cash and cash equivalents - restricted	12,742,111
Total cash and cash equivalents	58,725,560
Accounts receivable - utility, net	7,784,567
Due from grantor agencies	7,680,916
Inventory	24,222,910
Notes receivable, net	161,285
Prepayments and other assets, net	1,511,204
Total current assets	100,086,442
Utility plant, at cost:	
Depreciable utility plant, net of accumulated depreciation	105,291,139
Non-depreciable utility plant	15,650,964
Total noncurrent assets	120,942,103
Total assets	221,028,545
Deferred outflows of resources:	
Unbilled fuel cost recovery	6,752,827
Total deferred outflows of resources	6,752,827
Total assets and deferred outflows of resources	<u>\$ 227,781,372</u>

LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION

Current liabilities:	
Accounts payable and accrued liabilities	12,934,951
Due to primary government	9,311,189
Compensated absences	1,604,922
Security deposits, including accrued interest	12,326,355
Obligations under estimated environmental remediation costs, current portion	375,000
Obligations under lease, current portion	17,258
Total current liabilities	36,569,675
Noncurrent liabilities:	
Retirement contributions payable	3,467,425
Unearned local grants	3,579,253
Unearned revenue	469,460
Obligations under estimated environmental remediation costs, non-current portion	1,062,500
Dividends payable	1,080,000
Obligations under lease, non-current portion	770,687
Total noncurrent liabilities	10,429,325
Total liabilities	46,999,000
Deferred inflows of resources:	
Rate stabilization (public law no. 16-7)	66,102
Total deferred inflows of resources	66,102
Net position:	
Net investment in capital assets	120,942,103
Restricted	45,000,000
Unrestricted	14,774,167
Total net position	180,716,270
Total liabilities, deferred inflows of resources and net position	<u>\$ 227,781,372</u>

See accompanying independent auditor's report and notes to financial statements.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)
Statement of Revenues, Expenses and Changes in Net Position
For the Year Ended September 30, 2021

Operating revenues:	
Power	\$ 21,343,483
Water	10,734,812
Sewer	3,629,171
Fuel adjustment charge	36,269,886
Amortization of fuel purchase obligation rebate	-
Other revenue	680,447
	72,657,799
Bad debts	(4,078,372)
Net operating revenues	68,579,427
Operating expenses:	
Fuel, lube and taxes	37,918,469
General and administrative	17,642,751
Maintenance	14,159,027
Depreciation	11,125,418
Miscellaneous expense	945,477
Utility consumption	791,725
Supplies	684,933
	83,267,800
Total operating expenses	83,267,800
Operating loss	(14,688,373)
Non-operating revenues (expenses):	
Recovery of bad debts	9,517,245
Settlement	8,428,812
Interest income and late charges	4,705,378
Miscellaneous income	127,437
Contributions to primary government	(401,454)
Change in deferred fuel cost	(588,829)
Dividends	(900,000)
	20,888,589
Total non-operating revenues	20,888,589
Income before capital contributions from primary government and other items	6,200,216
Capital contributions from primary government	14,082,887
Change in net position	20,283,103
Net position at the beginning of the year	160,739,692
Adjustments to net position at the beginning of the year	(306,525)
Net position at the end of the year	\$ 180,716,270

See accompanying independent auditor's report and notes to financial statements.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Statement of Cash Flows

For the Year Ended September 30, 2021

Cash flows from operating activities:	
Cash received from customers	\$ 88,612,214
Cash payments to suppliers for goods and services	(60,800,311)
Cash payments to employees for services	(12,092,122)
	<hr/>
Net cash provided by operating activities	15,719,781
Cash flows from non-capital financing activities:	
Dividend payments	(1,620,000)
Payment for environmental remediation liability	(74,922)
	<hr/>
Net cash used for non-capital financing activities	(1,694,922)
Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets	(12,915,057)
Capital contributions received, net	13,469,527
	<hr/>
Net cash used for capital and related financing activities	554,470
Net change in cash and cash equivalents	14,579,329
Cash and cash equivalents - unrestricted	32,015,077
Cash and cash equivalents - restricted	12,131,154
	<hr/>
Balances at the beginning of the year	44,146,231
Cash and cash equivalents - unrestricted	45,983,449
Cash and cash equivalents - restricted	12,742,111
	<hr/>
Balances at the end of the year	<u>\$ 58,725,560</u>
Reconciliation of operating loss to net cash provided by operating activities:	
Operating loss	\$ (14,688,373)
Adjustments to reconcile operating loss to net cash provided by operating activities:	
Bad debts	4,078,372
Recovery of bad debts	9,517,245
Depreciation	11,125,418
Interest income and late charges	4,705,378
Miscellaneous income	127,437
Contributions to the primary government	(401,454)
Change in deferred fuel cost	(588,829)
Decrease (increase) in operating assets:	
Accounts receivable - utility, net	(6,466,991)
Inventory	(1,357,632)
Notes receivable, net	35,100
Prepayments and other assets, net	(32,059)
Unbilled fuel cost recovery	588,825
Increase (decrease) in liabilities:	
Accounts payable and accrued liabilities	6,938,468
Due to primary government	401,454
Compensated absences	215,907
Security deposits, including accrued interest	(392,566)
Retirement contributions payable	(14,027)
Unearned local grants	1,947,548
Unearned revenue	(8,184)
Lease obligation	(5,752)
Rate stabilization (public law no. 16-7)	(5,504)
	<hr/>
Net cash provided by operating activities	<u>\$ 15,719,781</u>
Supplemental disclosure of noncash financing and investing activities:	
Reduction of partial settlement of environmental remediation obligations	\$ 8,428,812
Lease obligation recognized at the start of the year	<u>\$ 793,697</u>

See accompanying independent auditor's report and notes to financial statements.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(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 codified as Chapter 1 of Division 8 of Title 4 of the Commonwealth Code, and began operations on October 1, 1987. Chapter 1 of Division 8 of Title 4 of the Commonwealth Code was repealed and re-enacted by Section 10 of Public Law 16-17.

CUC was given responsibility for supervising the construction, maintenance, operations, and regulation of electric, water and sewage services, provided however, that whenever feasible, CUC shall contract with 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 for CUC to become financially independent of appropriations by the CNMI Legislature. CUC is governed by a five-member Board of Directors, appointed for terms of four years by the Governor of the CNMI with the advice and consent of the Senate.

(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. CUC utilizes the flow of economic resources measurement focus. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

Basis of Accounting

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

Budgets

In accordance with CNMI Public Law 3-68, the Planning and Budgeting Act of 1983, CUC is required to submit annual budgets to the CNMI Office of the Governor; however, CUC is financially independent of appropriations by the CNMI Legislature.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(2) Summary of Significant Accounting Policies, continued

Concentrations of Credit Risk

Financial instruments which potentially subject CUC to concentrations of credit risk consist principally of cash demand deposits, accounts receivable and receivables from related parties.

At September 30, 2021, CUC has cash deposits in bank accounts that exceed federal depository insurance limits. CUC has not experienced any losses on such accounts.

Cash and Cash Equivalents

Cash and cash equivalents are defined as cash on hand, demand deposits and savings, and short-term time certificates of deposit with a maturity date within three months of the date acquired.

Receivables

Accounts receivable are classified as current assets and are reported net of an allowance for uncollectible amounts.

CUC allows customers to settle their outstanding utilities through issuance of promissory notes with terms ranging from six months to ten years at an interest rate of 12% per annum. As of September 30, 2021, CUC recorded notes receivable of \$161,285 net of allowance of \$30,894.

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 represents will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. The allowance is established through a provision for bad debts charged to expense. CUC's policy (beginning in fiscal year 2013) is to provide an allowance of one hundred percent (100%) of account balances greater than sixty (60) days old.

Due from Grantor Agencies

Grant disbursements over receipts are recognized as due from grantor agencies until funds are received in accordance with grant terms and conditions. As of September 30, 2021, CUC recorded due from grantor agencies of \$7,680,916.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(2) Summary of Significant Accounting Policies, continued

Inventory Valuation

Fuel and lube inventory is valued at the weighted average cost valuation method. Materials and supplies inventories are valued at average cost.

Allowance for inventory obsolescence is provided for inventory items, parts and supplies for equipment no longer in use based on quadrennial reviews. Allowance for inventory obsolescence was \$742,943 as of September 30, 2021.

Prepayments and Other Assets

Payments made to vendors for services that will benefit future periods are recorded as prepayments. As of September 30, 2021, CUC recorded prepayments of \$1,293,942.

Other assets consist of employee advances and other receivables stated at the amount of unpaid balances, net of allowance. CUC recorded employee and travel advances of \$15,884 and other receivables of \$201,378, net of allowance of \$721,447 as of September 30, 2021.

Fuel Costs

CUC's fuel purchases are based on Means of Platts Singapore (MOPS) monthly pricing. Fuel cost increases or decreases billed to customers are based on price changes in fuel purchased by CUC. Under or over recovery of fuel cost is recorded as a deferred fuel cost asset or liability, respectively, in the accompanying Statement of Net Position, and is recovered in or deducted from future billings to customers based on the amendments to Part 24 of the Electric Service Regulations of the CUC adopted on July 20, 2006. The Fuel Adjustment Charge (FAC) rates are computed monthly based on MOPS.

Any difference between the actual fuel costs and the electric fuel rate is accumulated in a deferred account and is subject to annual reconciliation. No interest is charged or paid on any under or over recovery balance in the deferred account.

In its May 11, 2015 meeting, the Commonwealth Public Utilities Commission (CPUC) approved to change the Levelized Energy Adjustment Clause tariff to the FAC. It also authorized on an interim basis through the next regulatory session to adjust the FAC, in the event the MOPS monthly pricing to CUC equals or exceeds a 4.5% differential in the average per gallon cost of fuel used in the calculation of the then current FAC. In such event, CUC shall change the FAC rate to reflect the higher/lower MOPS price and shall promptly provide calculations and supporting work papers to CPUC. This change shall be calculated on the basis of the ratio of the then current monthly MOPS pricing to the average per gallon cost of fuel used in the calculation of the current FAC rate.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)

Notes to the Financial Statements
September 30, 2021

(2) Summary of Significant Accounting Policies, continued

Fuel Cost, continued

Approved FAC rates for the year ended September 30, 2021 are as follows:

<u>Effective Date</u>	<u>FAC Rates</u>
October 1, 2020	\$0.11165
January 1, 2021	\$0.13585
February 1, 2021	\$0.14704
March 1, 2021	\$0.16578
April 1, 2021	\$0.17341
July 1, 2021	\$0.19355

The unbilled fuel cost recovery at September 30, 2021 is as follows:

At the beginning of the year	\$	7,341,652
Change in recovery of fuel cost		(588,825)
At the end of the year	\$	6,752,827

Utility Plant

Utility plant is stated at original cost, where costs are available, less accumulated depreciation. Depreciation is provided on the straight-line method based on the estimated useful lives of the respective assets, which range from 3 to 25 years. The cost of additions and replacements are capitalized. Repairs and maintenance are charged to expense as incurred. Retirements, sales and disposals are recorded by removing the cost and accumulated depreciation from the asset and accumulated depreciation accounts with any resulting gain or loss reflected in non-operating revenues (expenses) in the Statements of Revenues, Expenses and Changes in Net Position. Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the fair value is less than the carrying amount of the asset, a loss is recognized for the difference.

CUC's current policy is to capitalize items in excess of \$5,000. The costs of acquisition and construction of equipment and facilities are recorded as construction-in-progress until such assets are completed and placed in service, at which time CUC commences recording depreciation expense. Interest costs incurred before the end of a construction period are recognized as an expense in the period incurred. There was no interest related to construction for the year ended September 30, 2021.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(2) Summary of Significant Accounting Policies, continued

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits. The accumulated vacation leave liability as of September 30, 2021 amounted to \$1,604,922.

Net Position

Net position represents the residual interest in CUC's assets and deferred outflows of resources after liabilities and deferred inflows of resources are deducted and is classified as follows:

- Net investment in capital assets - Capital assets, net of accumulated depreciation and reduced by outstanding debt attributable to the acquisition, construction or improvements of those assets.
- Restricted:
 - Nonexpendable - Net position subject to externally imposed stipulations that CUC maintain them permanently. For the year ended September 30, 2021, CUC's restricted nonexpendable net position pertains to the Commonwealth Development Authority's (CDA) preferred stock.
 - Expendable - Net position whose use by CUC is subject to externally imposed stipulations that can be fulfilled by actions of CUC pursuant to those stipulations or that expire by the passage of time. At September 30, 2021, CUC does not have restricted expendable net position.
- Unrestricted - Net position that is not subject to externally imposed stipulations. Unrestricted net position may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

Retirement Plan

CUC contributed to the Northern Mariana Islands Retirement Fund's (NMIRF) defined benefit plan (DB Plan), a cost-sharing, multiple-employer plan established and now administered by the CNMI. On September 30, 2013, the DB Plan was transferred to the Northern Mariana Islands Settlement Fund (NMISF). CUC also contributes to a defined contribution plan (DC Plan).

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(2) Summary of Significant Accounting Policies, continued

Retirement Plan, continued

On August 30, 2012, Public Law 17-79 was enacted to amend Title I of the Commonwealth Code to include the intent of the CNMI to participate in the retirement insurance system established by Title II of the U.S. Federal Insurance Contributions Act (FICA) and for participation to be extended to elected officials, employees, political subdivisions and instrumentalities of the CNMI. On September 11, 2012, Public Law 17-82 CNMI Pension Reform Recovery Act of 2012 was enacted. Unless specifically exempted or authorized by federal law, Public Law 17-82 provides for mandatory membership of CNMI Government employees and elected officials in the U.S. Social Security system and authorizes employees, who elect, to buy quarters of service in the U.S. Social Security system from contributions made to the DB Plan. In addition, Public Law 17-82 provides active and inactive DB Plan members the option to voluntarily terminate membership in the DB Plan, withdraw or roll over contributions to the DC Plan and to participate in the U.S. Social Security system without termination of employment or penalty. Further, Public Law 17-82 allows the CNMI Government to continue remitting its 4% employer contribution to the DC Plan unless the employee ceases to contribute the employee share.

On March 11, 2013, Public Law 18-02 was enacted to amend Public Law 17-82 to clarify those provisions necessary to expedite the refunds and to prevent any further frustration of the process. Included in the public law is the amendment of Section 203(a) of Title 1, Division 8, Part 3, which states that the government obligation to withhold and remit the employee's portion to the employee's defined account shall continue with respect to employees who do not terminate membership in the DB Plan. All but seven active CUC employees voluntarily terminated membership in the DB Plan and CUC contributed \$132,143, \$147,221 and \$257,067 to the DB Plan during the years ended September 30, 2021, 2020 and 2019, respectively.

Defined Contribution Plan (DC Plan)

On June 16, 2006, Public Law No. 15-13 was enacted which created the DC Plan, a multi-employer pension plan and is the single retirement program for all employees whose first time CNMI government employment commences on or after January 1, 2007. Each member of the DC Plan is required to contribute to the member's individual account an amount equal to 10% of the member's compensation. CUC is required to contribute to each member's individual account an amount equal to 4% of the member's compensation. CUC's recorded DC contributions for the years ended September 30, 2021, 2020 and 2019 was \$221,628, \$258,300 and \$598,743, respectively, equal to the required contributions for each year. Members of the DC Plan, who have completed five years of government service, have a vested balance of 100% of both member and employer contributions plus any earnings thereon.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(2) Summary of Significant Accounting Policies, continued

Operating and Non-Operating Revenues and Expenses

CUC defines operating revenues as revenue generated from power, water and sewer sales and services. Operating expenses are costs incidental to the generation of operating revenues. Revenues and expenses not meeting the above definitions are classified as non-operating revenues and expenses.

Nonoperating revenues and expenses result from investing and financing activities.

Revenue Recognition

Power, water and sewer sales 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 subsequent cycle billing. Unbilled revenues at September 30, 2021 included as receivables in the accompanying financial statements were \$1,862,996.

Amortization of fuel purchase obligation rebate represents \$1,100,000 annual amortization of unearned fuel purchase obligation rebate from CUC's fuel supplier of \$6,600,000. As of September 30, 2021, CUC recorded an unearned purchase obligation rebate of \$0.

Capital Contributions and Federal Grants

Capital contributions and Federal grant revenues are recognized when allowable expenses are incurred.

Unearned Revenues

Unearned revenues arise when cash is received prior to being earned and relates to grant money, fuel purchase obligations rebate and credit vouchers of \$3,579,253, \$0 and \$469,460, respectively, as of September 30, 2021, which refers to revenues of the subsequent year.

Deferred Outflows of Resources

Deferred outflows of resources represent unbilled fuel cost recovery, which is consumption of net position that is applicable to a future reporting period and will not be recognized as an outflow of resources (expense) until that future time.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)

Notes to the Financial Statements
September 30, 2021

(2) Summary of Significant Accounting Policies, continued

Deferred Inflows of Resources

Deferred inflows of resources represent an acquisition of net position that is applicable to a future reporting period and therefore will not be recognized as an inflow of resources (revenue) until that future time. CUC recorded deferred inflows of resources from rate stabilization per Public Law No. 16-7 of \$66,102 as of September 30, 2021.

GASB Statement No. 68

In June 2012, GASB issued Statement No. 68, Accounting and Financial Reporting for Pensions, which revised and established new financial reporting requirements for most governments that provide their employees with pension benefits through plans that are administered through trusts. Management has determined that the CNMI is legally responsible for making contributions to NMISF as a non-employer entity and that net pension obligations are allocated in total to the CNMI. Management acknowledges the requirement to recognize expense in an amount equal to the non-employer contributing entities' (CNMI) total proportionate share of the collective pension expense that is associated with CUC. CUC has not recorded related revenues and pension expenses for the years ended September 30, 2021 since amounts were not available.

New Accounting Standards

During the year ended September 30, 2020, GASB issued Statement No. 95, Postponement of the Effective Dates of Certain Authoritative Guidance, which postpones the effective dates of GASB Statement No.'s 84, 89, 90, 91, 92 and 93 by one year and GASB Statement No. 87 by 18 months; however, earlier application of the provisions addressed in GASB Statement No. 95 is encouraged and is permitted to the extent specified in each pronouncement as originally issued. In accordance with GASB Statement No. 95, management has elected to postpone implementation of these statements.

In January 2017, GASB issued Statement No. 84, Fiduciary Activities. This Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. The requirements of this Statement will enhance consistency and comparability by (1) establishing specific criteria for identifying activities that should be reported as fiduciary activities and (2) clarifying whether and how business-type activities should report their fiduciary activities. Management does not believe that this Statement had a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 84 is effective for the fiscal year ending September 30, 2021.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 31, 2021

(2) Summary of Significant Accounting Policies, continued

New Accounting Standards, continued

In June 2017, GASB issued Statement No. 87, Leases. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and as inflows of resources or outflows of resources recognized based on the payment provisions of the contract. In accordance with GASB Statement No. 95, GASB Statement No. 87 will be effective for the fiscal year ending September 30, 2022.

In June 2018, GASB issued Statement No. 89, Accounting for Interest Cost Incurred Before the End of a Construction Period. The objectives of this Statement are (1) to enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and (2) to simplify accounting for interest cost incurred before the end of a construction period. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 89 will be effective for fiscal year ending September 30, 2022.

In March 2018, GASB issued Statement No. 90, Majority Equity Interests - An Amendment of GASB Statements No. 14 and 61. The primary objectives of this Statement are to improve the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and to improve the relevance of financial statement information for certain component units. It defines a majority equity interest and specifies that a majority equity interest in a legally separate organization should be reported as an investment if a government's holding of the equity interest meets the definition of an investment. A majority equity interest that meets the definition of an investment should be measured using the equity method, unless it is held by a special-purpose government engaged only in fiduciary activities, a fiduciary fund, or an endowment (including permanent and term endowments) or permanent fund. Those governments and funds should measure the majority equity interest at fair value. Management does not believe that this Statement had a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 90 is effective for the fiscal year ended September 30, 2021.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)

Notes to the Financial Statements
September 30, 2021

(2) Summary of Significant Accounting Policies, continued

New Accounting Standards, continued

In May 2019, GASB issued Statement No. 91, Conduit Debt Obligations. The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 91 will be effective for the fiscal year ending September 30, 2023.

In January 2020, GASB issued Statement No. 92, Omnibus 2020. The objectives of this Statement are to enhance comparability in accounting and financial reporting and to improve the consistency of authoritative literature by addressing practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics and includes specific provisions about the effective date of Statement No. 87, Leases, and Implementation Guide No. 2019-3, Leases, for interim financial reports, the terminology used to refer to derivative instruments and the applicability of certain requirements of Statement No. 84, Fiduciary Activities, to postemployment benefits. The requirements related to the effective date of GASB Statement No. 87 and Implementation Guide 2019-3, reissuance recoveries and terminology used to refer to derivative instruments are effective upon issuance. The remaining requirements of GASB Statement No. 92 are effective for the fiscal year ending September 30, 2022.

In March 2020, GASB issued Statement No. 93, Replacement of Interbank Offered Rates. The primary objective of this Statement is to address those and other accounting and financial reporting implications of the replacement of an IBOR. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 93 will be effective for the fiscal year ending September 30, 2022.

In March 2020, GASB issued Statement No. 94, Public-Private and Public-Public Partnerships and Availability Payment Arrangements. The primary objective of this Statement is to improve financial reporting by addressing issues related to public-private and public-public partnership arrangements. This Statement also provides guidance for accounting and financial reporting for availability payment arrangements. Management

COMMONWEALTH UTILITIES CORPORATION

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Notes to the Financial Statements

September 30, 2021

(2) Summary of Significant Accounting Policies, continued

New Accounting Standards, continued

does not believe that this Statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 94 will be effective for the fiscal year ending September 30, 2023.

In May 2020, GASB issued Statement No. 96, Subscription-Based Information Technology Arrangements. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users (governments). This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-to-use subscription asset - an intangible asset - and a corresponding subscription liability; (3) provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and (4) requires note disclosures regarding a SBITA. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 96 will be effective for the fiscal year ending September 30, 2023.

In June 2020, GASB issued Statement No. 97, Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans - an amendment of GASB Statements No. 14 and No. 84, and a supersession of GASB Statement No. 32. The primary objectives of this Statement are to (1) increase consistency and comparability related to the reporting of fiduciary component units in circumstances in which a potential component unit does not have a governing board and the primary government performs the duties that a governing board typically would perform; (2) mitigate costs associated with the reporting of certain defined contribution pension plans, defined contribution other postemployment benefit (OPEB) plans, and employee benefit plans other than pension plans or OPEB plans (other employee benefit plans) as fiduciary component units in fiduciary fund financial statements; and (3) enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code (IRC) Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 97 will be effective for fiscal year ending September 30, 2022.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(2) Summary of Significant Accounting Policies, continued

Estimates

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

(3) Cash and Cash Equivalents

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk and concentration of credit risk. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

As of September 30, 2021, total unrestricted cash and cash equivalents were \$45,983,449 and the corresponding bank balances were \$42,998,490. Of the bank balance amounts, \$42,345,122 are maintained in financial institutions subject to FDIC insurance and \$653,368 represents amounts maintained in a non-FDIC insured bank as of September 30, 2021. CNMI law does not require component unit funds to be collateralized and thus CUC's funds, in excess of FDIC insurance, are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

Restricted cash and cash equivalents of \$12,742,111 at September 30, 2021, respectively, pertain to customer deposits.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(4) Accounts Receivable – Utility

Accounts receivable - utility as of September 30, 2021 are presented below:

By location:

Saipan:

Commercial	\$ 3,675,484
Residential	6,492,217
Government	<u>22,802,322</u>

32,970,023

Tinian:

Commercial	1,694,787
Residential	274,220
Government	<u>643,936</u>

2,612,943

Rota:

Commercial	184,118
Residential	272,516
Government	<u>1,686,756</u>

2,143,390

Total billed

37,726,356

Unbilled and disputed

11,503,212

Accounts receivable

\$ 49,229,568

By customer classification:

Billed:

Commercial	\$ 5,554,389
Residential	7,038,953
Government	25,133,014
Unbilled and disputed	<u>11,503,212</u>

Accounts receivable

49,229,568

Allowance for uncollectible accounts

(41,445,001)

Accounts receivable, net

\$ 7,784,567

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(4) Accounts Receivable – Utility, continued

Changes in allowance for uncollectible accounts for the year ended September 30, 2021 are as follows:

Total allowance, beginning of the year	\$ 46,883,873
Provision for uncollectible accounts	4,078,372
Recovery of bad debts	<u>(9,517,245)</u>
Total allowance, end of year	<u>\$ 41,445,000</u>

(5) Inventory

Inventory balances as of September 30, 2021 are as follows:

Fuel and lube	\$ 2,523,801
Materials and supplies	<u>22,442,052</u>
	24,965,853
Allowance for obsolescence	<u>(742,943)</u>
Inventory, net	<u>\$ 24,222,910</u>

(6) Capital Contributions and Federal Grants

CUC is a recipient of direct federal awards and is a subrecipient of federal grants received by the CNMI central government from various U.S. federal agencies. CUC records grants-in-aid for construction or acquisition of facilities and equipment as capital contributions. CUC recorded direct federal awards and subrecipient awards of federal grants of \$12,686,750 and \$465,278, respectively, for the year ended September 30, 2021.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)
Notes to the Financial Statements
September 30, 2021

(7) Capital Assets

A summary of the changes in capital assets for the year ended September 30, 2021 is as follows:

	<u>Useful Lives</u>	<u>October 1, 2020</u>	<u>Additions</u>	<u>Disposals</u>	<u>Adjustments or Transfers</u>	<u>September 30, 2021</u>
Non-depreciable capital assets:						
Construction in progress		\$ 7,022,431	\$ 11,658,858	\$ -	\$ (3,030,325)	\$ 15,650,964
Total non-depreciable capital assets		7,022,431	11,658,858	-	(3,030,325)	15,650,964
Depreciable capital assets:						
Utility plant in service:						
Electric plant	25 years	181,681,008	844,847	1,410,282	-	181,115,573
Water plant	25 years	85,703,444	3,264,708	91,550	30,098	88,906,700
Sewer plant	25 years	55,835,152	716,446	92,002	-	56,459,596
Administrative equipment	3-5 years	4,405,904	37,801	77,092	1,120	4,367,733
		327,625,508	4,863,802	1,670,926	31,218	330,849,602
Accumulated depreciation		(215,982,647)	(11,125,417)	(1,549,601)	-	(225,558,463)
Total depreciable capital assets		111,642,861	(6,261,615)	121,325	31,218	105,291,139
Total capital assets, net		\$ 118,665,292	\$ 5,397,243	\$ 121,325	\$ (2,999,107)	\$ 120,942,103

Included in utility plant in service adjustments/transfers for fiscal year ended September 30, 2021 are completed projects transferred from construction work-in-progress to utility plant in service of \$2,720,172.

CUC entered several construction contracts during the fiscal years 2021 for improvements, rehabilitation and replacement of facilities, and other capital projects. As of September 30, 2021, CUC had outstanding construction contracts totaling \$10,621,574 that will be financed from operating funds and federal awards.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(8) Security Deposits

Pursuant to 4 CMC § 8143, as amended by Public Law 16-17, CUC shall collect a one-month security deposit per residential customer account. Such deposits shall be placed in an interest-bearing trust fund and shall not be used for any other purpose. A summary of security deposits including accrued interest as of September 30, 2021 is as follows:

Electric	\$ 10,923,230
Water	566,118
Sewer	<u>235,666</u>
Total security deposits	11,725,014
Accrued interest on security deposits	<u>601,341</u>
Security deposits, including interest	<u>\$ 12,326,355</u>

(9) Related Party Transactions

Public Law 9-68, enacted on October 19, 1995, requires government agencies to pay the CNMI 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 CNMI Office of the Public Auditor (OPA) and the agency may agree, to fund the OPA. At September 30, 2021, CUC recognized outstanding payables to the CNMI Government of \$9,311,189, based on 1% of CUC's operations budget excluding fuel costs.

On September 26, 2011, the Appropriations and Budget Authority Act of 2012 (Public Law 17-55) was signed into law. Section 601 of Public Law 17-55 authorizes the CNMI Secretary of Finance to deduct the 1% due to the OPA from CUC from the monthly utility costs of the government. No application of payments was made as of September 30, 2021.

In fiscal year 2018, a settlement was reached on CUC's outstanding balance on employer contributions owed to NMISF. Under the agreement, CUC agreed to a payment total of \$3,469,797 to be paid in \$50,000 monthly installments on the first of each month until the balance is paid in full. As of September 30, 2021, CUC recorded retirement contributions payable of \$3,467,425. No payment has been made as of September 30, 2021 as CUC and NMISF have yet to execute a settlement agreement.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(9) Related Party Transactions, continued

On November 12, 2019, CUC entered into an omnibus agreement with the Commonwealth Ports Authority (CPA) which gave CUC a permanent easement over water wells, water lines, sand filtration, a 20-million-gallon tank, and power poles and transmission lines to power the water wells, located on CPA property. CUC is responsible for maintenance of the permanent easement and for maintaining a continuous water supply to CPA. CUC recorded a special item to the omnibus agreement for the year ended September 30, 2019 for the additional water well lease expense of \$3,559,840. In addition, CUC recorded land rights of \$3,642,991 and reversed receivables from CPA of \$7,202,831 as of September 30, 2019. Further, CUC waived penalties and interest related to outstanding billings to CPA estimated at \$878,241.

(10) Preferred Stock Issued to CDA

On October 2, 2008, Public Law No. 16-17 of the Commonwealth Utilities Corporation Act of 2008 authorized CUC to issue shares of cumulative, non-convertible, non-transferable preferred stock valued at \$45,000,000 to CDA.

CUC and CDA may provide by written agreement, subject to the terms and conditions of a Memorandum of Agreement (MOA), such terms and conditions being incorporated herein by reference, for the following:

- 1) Guaranteed annual dividends fixed and payable as agreed;
- 2) Buy-back provisions;
- 3) Default provisions;
- 4) Preferred shareholder rights; and
- 5) Consistent with Commonwealth law, such other rights and remedies as are typically found in shareholder and stock purchase agreements.

On May 7, 2009 the MOA was signed by officials of CUC and CDA. The MOA was subsequently approved by CPUC.

Pursuant to the terms of the MOA, the dividend payments for the first three years after issuance of the stock are to be amortized and interest free over a 15-year period. Although the preferred stock certificates have not been physically issued, CUC is of the opinion that CDA has constructive receipt of the preferred shares through the execution of the MOA.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(10) Preferred Stock Issued to CDA, continued

On August 17, 2016, CUC entered into an agreement with CDA for the total amount of unpaid dividend payments owed to CDA and agreed to a dividend of \$4,320,000 for the year ended September 30, 2016. The agreement states that CUC will make quarterly dividend payments of \$270,000 beginning October 1, 2016, as required by the preferred stock agreement, which represents the full amount of the quarterly dividend due. Dividends payable as of September 30, 2021 amounted to \$1,080,000.

(11) Risk Management

CUC is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. CUC does not maintain insurance coverage for a significant amount of fixed assets. In the event of a catastrophe, CUC may be self-insured to a material extent.

(12) Commitments and Contingencies

Commitments

Capital Commitments

At September 30, 2021, CUC had commitments of \$13.877 million for construction, purchases of inventory, and acquisition of property and equipment, all of which are expected to be incurred in 2022.

Fuel Purchase Contract

On May 8, 2020, CUC entered into a fuel supply contract with Mobil Oil Mariana Islands, Inc. The agreement is for four years with an option to extend for two years, renewable annually.

Operating Lease

CUC entered into a lease agreement for office space in Joeten Dandan Building for a term of five years commencing in December 2016 and expiring in December 2021. The annual lease payment is \$166,605.

CUC also entered into a lease agreement for lease of office/warehouse space for its Power Division in Saipan commencing in June 2018 and expiring in June 2020 with an option to extend for two years, renewable annually. On June 11, 2020 and April 07, 2021, the agreement was renewed to extend the contract expiration date to June 14, 2022. The annual lease payment is \$136,344 for the first two years and \$117,024 for the additional years.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)

Notes to the Financial Statements
September 30, 2021

(12) Commitments and Contingencies, continued

Commitments, continued

Operating Lease, continued

CUC also entered into a ground lease agreement for powerplant in Saipan for a term of forty years commencing in June 2021. The monthly lease payment is \$1,438 and will increase by 7.5% every 8 years.

CUC also entered into a lease agreement for office space in Rota for a term of six years commencing in December 2012 and expiring in December 2018. The Rota lease is currently on a month-to-month basis. The annual lease payment is \$16,900.

Future lease payments are as follows:

Year ending September 30,

2022	\$ 380,098
2023	350,953
2024	358,667
2025	384,122
2026	392,608
onwards	794,986
	<u>\$ 2,661,434</u>

Power Purchase Contract

In fiscal year 2020, CUC entered into a power purchase commitment with Telesource CNMI Inc., which is the power service provider in the island of Tinian. The agreement is for two years beginning April 1, 2020.

Omnibus Agreement

As discussed in note 9 to the financial statements, CUC entered into an omnibus agreement with CPA for permanent easement rights. In accordance with Section 2 of the agreement, CUC will not charge CPA for water up to \$600,000 annually on an indefinite basis beginning November 1, 2019. CPA shall pay to CUC any and all amounts in excess of the offset as billed.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)

Notes to the Financial Statements
September 30, 2021

(12) Commitments and Contingencies, continued

Contingencies

Certain conditions may exist as of the date the financial statements are issued, which may result in a loss to CUC but which will only be resolved when one or more future events occur or fail to occur. CUC's management and its legal counsel assess such contingent liabilities, and such assessment inherently involves an exercise of judgment.

In assessing loss contingencies related to legal proceedings that are pending against CUC or unasserted claims that may result in such proceedings, CUC's legal counsel evaluates the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought therein.

If the assessment of a contingency indicates that it is probable that a material loss has been incurred and the amount of the liability can be estimated, then the estimated liability would be accrued in CUC's financial statements. If the assessment indicates that a potentially material loss contingency is not probable, but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material, would be disclosed.

Loss contingencies considered remote are generally not disclosed unless they involve guarantees, in which case the nature of the guarantee would be disclosed.

Litigation and Potential Claims

CUC is subject to various claims and legal proceedings covering a wide range of matters that arise in the ordinary course of its operations, including customer disputes.

No provision for any liability that may result upon resolution of these matters has been made in the accompanying financial statements; however, there are pending cases under litigation.

Stipulated Orders

The U.S. Environmental Protection Agency (EPA) brought suit against CUC and the CNMI Government alleging a failure to comply with various regulations and requirements related to the Safe Drinking Water Act ("SDWA") and the Federal Water Pollution Control Act ("FWPCA"). To date there have been two primary stipulated orders entered as a result of this action.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(12) Commitments and Contingencies, continued

Contingencies, continued

Stipulated Orders, continued

Stipulated Order One (SO1) is intended to ensure that CUC's wastewater and drinking water systems achieve compliance with the SDWA and the FWPCA. The major components of SO1 are:

1. The reformation of CUC's management, finances and operations; and
2. The construction of wastewater infrastructure.

CUC is also required to take steps to comply with National Pollution Discharge Elimination System permits and compliance orders, comply with drinking water standards, and to eliminate spills from the wastewater system.

Stipulated Order Two (SO2) is intended to ensure that CUC's power plant facilities achieve compliance with the Clean Water Act (CWA). These requirements include requiring CUC to eliminate oil spills, implement appropriate spill prevention measures, implement effective inspection procedures for its oil storage facilities, provide containment for oil storage facilities and prepare appropriate operating plans.

The SO2 projects continue under the direction of the Court's appointed Engineering and Environmental Management Company (EEMC) - Gilbane Federal - pursuant to the provisions of the Stipulated Order entered on September 26, 2014. Progress on outstanding issues under Court order are projected to be completed in 2020 with consideration by the Court to terminate SO2 provisions along with a continuing obligation to fund the TMO fund for an additional five years as a maintenance reserve for SO2 funded improvements.

Cumulative Questioned Costs

CUC participates in several federally assisted grant programs funded by the United States Government. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. Cumulative questioned costs of \$490,364 have been set forth in CUC's Single Audit Report for the year ended September 30, 2020 and is comprised of questioned costs of \$157,647 for fiscal year 2020 and \$332,717 for fiscal year 2019. The ultimate disposition of these questioned costs can be determined only by final action of the respective grantor agencies. As of September 30, 2021, the questioned costs have been addressed and resolved.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)

Notes to the Financial Statements
September 30, 2021

(13) Obligations Under the Estimated Environmental Remediation Costs

U.S. Environmental Protection Agency

On March 10, 2011, CUC received an order from the U.S. EPA, which requires CUC to perform cleanup activities of Power Plants 1 and 2, pursuant to the National Oil and Hazardous Substances Pollution Contingency Plan, which appears at Title 40, CFR Part 300 and paragraphs 12 and 14 of SO2 for Preliminary Injunctive Relief.

On October 27, 2011, EPA contacted CUC regarding release or threatened release of hazardous substance connected with the Rota Power Plant located in Songsong Village, Rota (the Site). As a current owner and operator of the Rota Power Plant, EPA believes that CUC may be liable pursuant to Section 107(a) of the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), as amended, 42 U.S.C. 9607(a), for response costs incurred to address environmental contamination at the Site. By letter dated November 3, 2011, CUC indicated that it lacked the financial ability to perform an immediate cleanup of hazardous substances and requested EPA's assistance in performing such a cleanup. EPA has incurred at least \$2,131,697 in costs related to the Site as of January 31, 2016.

A settlement agreement was also entered between CUC and the U.S. EPA pursuant to CERCLA section 122(h)(1) for recovery of past response costs of \$315,000 plus 3% interest. CUC will pay in 48 installments starting August 15, 2021.

U.S. Coast Guard

On April 26, 2017, CUC received an assessment to reimburse the United States Coast Guard (USCG) for the costs incurred for oil discharge pollution removal at CUC Power Plants 1 and 2 totaling \$7,809,537. In fiscal year 2020, CUC and USCG agreed to enter into a settlement agreement pursuant to Section 1015 of the Oil Pollution Act of 1990. CUC agreed to pay USCG the principal sum of \$1,185,000 in forty-eight monthly installments of \$24,688 plus 3% annual interest.

Future principal payments are as follows:

Year ending September 30,

2022	\$ 375,000
2023	375,000
2024	375,000
2025	312,500
	<u>\$ 1,437,500</u>

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 30, 2021

(14) Economic Dependency

CUC is dependent on various equipment manufacturers, distributors, and dealers for the supply of parts for the utility plants and suppliers of fuel and lube. CUC is dependent on the ability of its suppliers to provide products on a timely basis and on favorable pricing terms. The loss of certain principal suppliers or a significant reduction in product availability from principal suppliers could have a material adverse effect on CUC. CUC believes that its relationships with its suppliers are satisfactory and has not experienced any significant delays due to its major suppliers.

(15) COVID-19 Pandemic

Economic uncertainties have arisen because of the COVID-19 coronavirus pandemic. The CNMI government suspended commercial air travel to the Commonwealth to prevent the spread of the COVID-19. Although this suspension has been lifted, it has negatively impacted business in the CNMI and resulted in permanent closure of some businesses and employee furloughs both in private and public sectors. CUC expects this matter to negatively impact its future financial results; however, the related financial impact cannot be reasonably estimated at this time.

(16) Date of Management's Review

Management has evaluated subsequent events and transactions occurring after the balance sheet date through the date of availability of the financial statements to be issued, September 21, 2023. The Company has determined that none of the events occurring after the date of the balance sheet substantially affects the amounts, presentation, and disclosure of the accompanying financial statements.

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Schedule of Revenues, Expenses and Changes in Net Position on a Divisional Basis

For the Year Ended September 30, 2021

	Power	Water	Sewer	Administrative and General	Elimination	Total
Operating revenues:						
Government	\$ 4,626,078	2,839,261	1,970,318	-	(1,927,084)	7,508,573
Commercial	12,008,903	2,540,547	1,015,333	-	-	15,564,783
Residential	6,331,445	5,625,169	677,496	-	-	12,634,110
	<u>22,966,426</u>	<u>11,004,977</u>	<u>3,663,147</u>	<u>-</u>	<u>(1,927,084)</u>	<u>35,707,466</u>
Fuel adjustment charge	38,507,298	-	-	-	(2,237,412)	36,269,886
Other revenue	574,400	85,296	20,751	-	-	680,447
	<u>62,048,124</u>	<u>11,090,273</u>	<u>3,683,898</u>	<u>-</u>	<u>(4,164,496)</u>	<u>72,657,799</u>
Bad debts	(2,044,443)	(1,485,414)	(548,515)	-	-	(4,078,372)
Net operating revenues	60,003,681	9,604,859	3,135,383	-	(4,164,496)	68,579,427
Operating expenses:						
Fuel, lube and taxes	37,918,469	-	-	-	-	37,918,469
General and administrative	3,037,894	2,778,453	331,757	11,494,647	-	17,642,751
Maintenance	12,492,062	1,063,595	256,744	346,626	-	14,159,027
Depreciation	6,478,169	2,275,578	2,096,928	274,743	-	11,125,418
Utility consumption	1,120,796	3,068,151	760,460	6,814	(4,164,496)	791,725
Miscellaneous expense	-	-	-	945,477	-	945,477
Supplies	122,582	276,440	56,548	229,363	-	684,933
Total operating expenses	<u>61,169,972</u>	<u>9,462,217</u>	<u>3,502,437</u>	<u>13,297,670</u>	<u>(4,164,496)</u>	<u>83,267,800</u>
allocation of common costs	(1,166,291)	142,642	(367,054)	(13,297,670)	-	(14,688,373)
Allocation of common costs	<u>(10,653,679)</u>	<u>(1,981,075)</u>	<u>(668,271)</u>	<u>13,303,025</u>	<u>-</u>	<u>-</u>
Operating income (loss), rolled forward	(11,819,970)	(1,838,433)	(1,035,325)	5,355	-	(14,688,373)

See accompanying independent auditor's report and notes to financial statements.

(A Component of the CNMI Government)
Schedule of Revenues, Expenses and Changes in Net Position on a Divisional Basis
For the Year Ended September 30, 2021

	Power	Water	Sewer	Administrative and General	Elimination	Total
Operating income (loss), carried forward	(11,819,970)	(1,838,433)	(1,035,325)	5,355	-	(14,688,373)
Non-operating revenues (expenses):						
Recovery of bad debts	5,807,693	2,997,024	712,528	-	-	9,517,245
Settlement	8,433,812	(5,000)	-	-	-	8,428,812
Interest income and late charges	2,641,456	1,176,126	877,179	10,617	-	4,705,378
Miscellaneous income	7,619	16,942	32,030	70,846	-	127,437
Contributions to primary government	(297,682)	(72,345)	(31,427)	-	-	(401,454)
Change in deferred fuel cost	(588,829)	-	-	-	-	(588,829)
Dividends	(900,000)	-	-	-	-	(900,000)
Total non-operating revenues	15,104,069	4,112,747	1,590,310	81,463	-	20,888,589
Income before capital contributions from primary government and other items	3,284,099	2,274,314	554,985	86,818	-	6,200,216
Capital contributions from primary government	1,282,938	7,366,423	5,433,526	-	-	14,082,887
Change in net position	<u>\$ 4,567,037</u>	<u>9,640,737</u>	<u>5,988,511</u>	<u>86,818</u>	<u>-</u>	<u>20,283,103</u>

See accompanying independent auditor's report and notes to financial statements.

COMMONWEALTH UTILITIES CORPORATION
(A Component Unit of the Commonwealth
of the Northern Mariana Islands)

Independent Auditor's Reports on
Internal Control and on Compliance
September 30, 2021
(With Independent Auditor's Report Thereon)



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

To the Board of Directors
Commonwealth Utilities Corporation

We have audited, 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, the financial statements of Commonwealth Utilities Corporation (CUC), a component unit of the Commonwealth of the Northern Mariana Islands, which comprise the statement of net position as of September 30, 2021, and the related statements of revenues, expenses and changes in net position, and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated September 21, 2023.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered CUC's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of CUC's internal control. Accordingly, we do not express an opinion on the effectiveness of CUC's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Questioned Costs as item 2021-001 that we consider to be a significant deficiency.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether CUC's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

CUC's Response to Findings

CUC's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. CUC's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Bryce Combs & Associates

Saipan, MP
September 21, 2023



**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR
FEDERAL PROGRAM; REPORT ON INTERNAL CONTROL OVER COMPLIANCE;
AND REPORT ON SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
REQUIRED BY THE UNIFORM GUIDANCE**

To the Board of Directors
Commonwealth Utilities Corporation

Report on Compliance for Each Major Federal Program

We have audited Commonwealth Utilities Corporation's (CUC's) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of CUC's major federal programs for the year ended September 30, 2021. CUC's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of CUC's major federal programs based on our audit of the types of compliance requirements referred to above. 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 the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Those standards and the Uniform Guidance 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 qualified and unmodified opinions on compliance for major federal programs. However, our audit does not provide a legal determination of CUC's compliance.

Basis for Qualified Opinion on CFDA Program

As described in Finding 2021-001 in the accompanying Schedule of Findings and Questioned Costs, CUC did not comply with the reporting requirements of one of its major programs. Compliance with such requirements is necessary, in our opinion, for CUC to comply with the requirements applicable to those programs.

Qualified Opinion on CFDA Program 66.600

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, CUC complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on CFDA Program 66.600 Drinking Water and Wastewater Infrastructure: Consolidated Environmental Programs for the year ended September 30, 2021.

Unmodified Opinion on Each of the Other Major Federal Programs

In our opinion, CUC complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its other major federal programs identified in the summary of auditors' result section of the accompanying Schedule of Findings and Questioned Costs for the year ended September 30, 2021.

Other Matters

The results of our auditing procedures disclosed other instances of noncompliance which are required to be reported in accordance with the Uniform Guidance and which are described in the accompanying Schedule of Findings and Questioned Costs as item 2021-001. Our opinion on each major federal program is not modified with respect to these matters.

CUC's response to the noncompliance findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. CUC's response was not subject to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

CUC is responsible for preparing a correction action plan to address each audit finding included in our auditor's report. CUC's corrective action plan was not subjected to the audit procedures applied in the audit of compliance and, accordingly, we express no opinion on it.

Report on Internal Control over Compliance

The management of CUC is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered CUC's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of CUC's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we did identify certain deficiencies in internal control over compliance, described in the accompanying Schedule of Findings and Questioned Costs as item 2021-001 that we consider to be a significant deficiency.

CUC's response to the internal control over compliance findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. CUC's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

CUC is responsible for preparing a correction action plan to address each audit finding included in our auditor's report. CUC's corrective action plan was not subjected to the audit procedures applied in the audit of compliance and, accordingly, we express no opinion on it.

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the financial statements of CUC as of and for the year ended September 30, 2021, and have issued our report thereon dated September 21, 2023, which contained a qualified opinion on those financial statements due to our inability to determine the propriety of inventory as of September 30, 2021, and which included an explanatory paragraph concerning the impact of COVID-19. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated in all material respects in relation to the financial statements as a whole.

Bryce Combs & Associates

Saipan, MP
September 21, 2023

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)
Schedule of Expenditures of Federal Awards
For the Year Ended September 30, 2021

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Nubmer	Pass-Through Entity Identifying Number	Federal Expenditure
<u>U.S. Environmental Protection Agency</u>			
Direct Program:			
Drinking Water and Wastewater Infrastructure: Consolidated Environmental Programs	66.600		\$ 11,441,591
Total U.S. Environmental Protection Agency			11,441,591
<u>U.S. Department of Homeland Security</u>			
Pass-Through Program from CNMI Government:			
Disaster Grants - Public Assistance (Presidentially Declared Disasters):	97.036		
Typhoon Yutu		DR-4235-MP	332,717
Typhoon Soudelor		DR-4404-MP	5,635
Total U.S. Department of Homeland Security			338,352
<u>U.S. Department of Commerce</u>			
Direct Program:			
Economic Development Cluster:			
Public Works and Economic Development Facilities Program: Sewer System Improvements for Saipan's Lower Base Industrial Park	11.300		659,332
Total U.S. Department of Commerce			659,332
<u>U.S. Department of Interior</u>			
Direct Program:			
Economic, Social and Political Development of the Territories	15.875		585,827
Total U.S. Department of Interior			585,827
<u>U. S. Department of Defense</u>			
Office of Economic Adjustment			
Pass-Through From Government of CNMI:			
Relocation of Utilities on Tinian	12.600	CNMI-CIP-1287- 20-01	113,651
Total U.S. Department of Defense			113,651
<u>U. S. Department of Treasury</u>			
American Rescue Plan Act (ARPA)			
Coronavirus State and Local Fiscal Recovery Funds			
Pass-Through From Government of CNMI:			
Investments in Water and Sewer (06-21-050 Water Projects)	21.027	CNMI22002	13,275
Total U.S. Department of Treasury			13,275
Total Expenditures of Federal Awards			\$ 13,152,028

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

COMMONWEALTH UTILITIES CORPORATION

(A Component of the CNMI Government)

Notes to the Financial Statements

September 31, 2021

(1) Scope of Audit

The Commonwealth Utilities Corporation (CUC) is a component unit of the Commonwealth of the Northern Mariana Islands (CNMI) Government and was established as a public corporation by CNMI Public Law 4-47, as amended and has the powers of a body corporate, as defined in the act and local statutes. Only the transactions of CUC are included within the scope of the Single Audit.

(2) Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes the federal award activity of CUC under programs of the federal government for the year ended September 30, 2021. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of CUC, it is not intended to and does not present the financial position, changes in net position or cash flows of CUC.

(3) Summary of Significant Accounting Policies

Basis of Accounting

Expenditures reported on the Schedule are reported on the accrual basis of accounting, consistent with the manner in which CUC maintains its accounting records. All expenses and capital outlays are reported as expenditures. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Pass-through entity identifying numbers are presented where available. CUC recognizes contributions from the federal government when qualifying expenditures are incurred.

Indirect Costs

CUC does not have an indirect cost negotiation agreement and does not elect to use the de-minimis indirect cost rate allowed under the Uniform Guidance.

Matching Costs

The 10 percent non-federal share of CFDA 97.036 is not included in the accompanying Schedule of Expenditures of Federal Awards.

The 25 percent non-federal share of CFDA 11.300 is not included in the accompanying Schedule of Expenditures of Federal Awards.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)
 Schedule of Findings and Questioned Cost
 September 31, 2021

SECTION I – SUMMARY OF AUDITOR’S RESULTS

Financial Statements

Type of auditor’s report issued:	Qualified	
Internal Control over Financial Reporting:		
• Were material weakness(es) identified?	___ Yes	_x_ No
• Were significant deficiency(ies) identified that are not considered to be material weaknesses?	___ Yes	_x_ None Reported
Non-compliance material to financial statements noted?	___ Yes	_x_ No

Federal Awards

Internal Control over Major Federal Programs:		
• Material weakness(es) identified?	___ Yes	_x_ No
• Were significant deficiency(ies) identified that are not considered to be material weaknesses?	_x_ Yes	___ None Reported
Type of auditors’ report issued on compliance for Major Federal Program:		
• 11.300 Public Works and Economic Development Facilities Program: Sewer System Improvements for Saipan's Lower Base Industrial Park	Unmodified	
• 66.600 Drinking Water and Wastewater Infrastructure: Consolidated Environmental Programs	Qualified	
Are there any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	_x_ Yes	___ No

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)
Schedule of Findings and Questioned Cost
September 31, 2021

SECTION I – SUMMARY OF AUDITOR’S RESULT, continued

Federal Awards

Identification of Major Programs

<u>CFDA No.</u>	<u>Description</u>	<u>Federal Expenditures</u>
11.300	Public Works and Economic Development Facilities Program: Sewer System Improvements for Saipan's Lower Base Industrial Park	\$ 659,332
66.600	Drinking Water and Wastewater Infrastructure: Consolidated Environmental Programs	<u>11,441,591</u>
	Total Major Program Expenditures	<u>\$ 12,100,932</u>
Total Federal Expenditures		<u>\$ 13,152,028</u>
Percentage of Federal Expenditures tested as Major Programs		<u>92%</u>
Dollar threshold used to distinguish between Type A and Type B Programs:		\$750,000
Did the auditee qualify as low-risk?		_____ Yes <u> x </u> No

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)
Schedule of Findings and Questioned Cost
September 31, 2021

SECTION II – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Finding No. 2021-001

Federal Agency:	U.S. Environmental Protection Agency
CFDA No.:	66.600
Program Title:	Drinking Water and Wastewater Infrastructure: Consolidated Environmental Programs
Area:	Special Tests and Provisions – Administrative Conditions
Repeat Finding from Prior Audit?	No
Questioned Cost:	\$0.00

Criteria:

According to the Administrative Conditions of the grant agreement, the Commonwealth Utilities Corporation must prepare an SF 425 annually and submit it on or before December 31 of the same year.

Condition:

Of the five projects under CFDA No. 66.600, the SF 425 for all five projects was submitted late. M00T33715 was submitted on February 23, 2022. M-00T33717, M-00T33719, M-00T33721, and M-98T07701 were submitted on March 1, 2023.

Cause:

The Grant Administrator did not submit the report on time but requested an extension. No proof was provided that the extension was filed or approved by the grantor.

Effect:

There is a risk that the grantor may not approve future grants due to CUC's noncompliance with the grant requirements.

Recommendation:

The Commonwealth Utilities Corporation should properly maintain their accounting, financial, and project records in a manner that will facilitate timely preparation and submission of required reports.

Views of the Officials:

CUC's response is documented in the corrective action plan.

COMMONWEALTH UTILITIES CORPORATION
(A Component of the CNMI Government)
Schedule of Findings and Questioned Cost
September 31, 2021

SECTION III – SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS

No.	Subject Matter	Status	Current Year No.	Questioned Costs
2020-001	Schedule of Expenditure of Federal Awards	Resolved	-	\$0.00
2020-002	Capital Assets	Unresolved	-	\$0.00
2020-003	Procurement	Unresolved	-	\$157,647
2020-004	Payroll	Resolved	-	\$0.00
2020-005	11.300 Allowable Cost/Cost Principles	Resolved	-	\$0.00
2020-006	11.300 Matching, Level of Effort, Earmarking	Resolved	-	\$0.00
2020-007	11.300 Reporting	Resolved	-	\$0.00
2020-008	11.300 Special Tests and Provisions – Wage Rate Requirements	Resolved	-	\$0.00
2020-009	66.600 Equipment and Real Property Management	Resolved	-	\$0.00
2020-010	66.600 Reporting	Resolved	-	\$0.00
2020-011	66.600 Special Tests and Provisions	Resolved	-	\$0.00
2019-001	Schedule of Expenditure of Federal Awards	Resolved	-	\$0.00
2019-002	Inventory	Unresolved	-	\$0.00
2019-003	Capital Assets	Unresolved	-	\$0.00
2019-004	66.600 Procurement and Suspension and Debarment	Resolved	-	\$0.00
2019-005	Non-Payroll Expenditure	Resolved	-	\$0.00
2019-006	97.036 Allowable Cost/Cost Principles	Resolved	-	\$332,717
2019-007	97.036 Matching, Level of Effort, Earmarking	Resolved	-	\$0.00



Commonwealth Utilities Corporation



October 2, 2023

Mr. David Burger, Partner
Burger Comer Magliari
P.O. Box 504053
Saipan, MP 96950

Subject: Schedule of Findings and Questioned Costs for the year ended September 30, 2018

Dear Mr. Burger:

Please see below CUC's responses to the findings regarding the CUC FY 2018 Audit:

Finding No. 2021-001

Federal Agency:	U.S. Environmental Protection Agency
CFDA No.:	66.600
Program Title:	Drinking Water and Wastewater Infrastructure: Consolidated Environmental Programs
Area:	Special Tests and Provisions – Administrative Conditions
Repeat Finding from Prior Audit?	No
Questioned Cost	\$0.00

Criteria:

According to the Administrative Conditions of the grant agreement, the Commonwealth Utilities Corporation must prepare an SF 425 annually and submit it on or before December 31 of the same year.

Condition:

Of the five projects under CFDA No. 66.600, the SF 425 for all five projects was submitted late. M00T33715 was submitted on February 23, 2022. M-00T33717, M-00T33719, M-00T33721, and M-98T07701 were submitted on March 1, 2023.

Cause:

The Grant Administrator did not submit the report on time but requested an extension. No proof was provided that the extension was filed.

Effect:

There is no assurance that the Commonwealth Utilities Corporation was not in default since no proof was provided.

Recommendation:

The Commonwealth Utilities Corporation should keep an orderly record of documents so the documents are readily available.

CUC Response:

CUC agrees with the finding.

Management's Corrective Action Plan:

CUC has assigned personnel to monitor various projects and work with Grants Administrator to ensure that reports are prepared and submitted in a timely manner.

Proposed Completion Date: Completed

Sincerely,


Rodolfo Urbano
Acting Chief Financial Officer