



COMMONWEALTH PORTS AUTHORITY

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The Honorable Benigno R. Fitial
Governor
Hon. Juan A. Sablan Administration Building
Capital Hill
Saipan, MP 96950

The Honorable Pete P. Reyes
Senate President
Sixteenth Northern Marianas
Commonwealth Legislature
Saipan, MP 96950

July 13, 2008

The Honorable Arnold I. Palacios
Speaker, House of Representatives
Sixteenth Northern Marianas
Commonwealth Legislature
Saipan, MP 96950

Subject: Third Interim Bond Indenture Compliance Report by the Commonwealth Ports Authority as to its obligations under its 1998 Bond Indenture Agreement for the \$20 Million Airport Revenue Bonds (Emergency Declaration Executive Order No. 08-04).

Dear Governor Fitial, President Reyes and Mr. Speaker:

Pursuant to your Executive Order and Implementing Instructions, the Commonwealth Ports Authority hereby files its Third Interim Bond Indenture Compliance Report to the Executive Branch and the Legislature. This constitutes the report at 60 days into the Emergency Declaration after Governor Fitial extended the declaration period (of May 13th) for another 30 days.

Since our initial report and the extension of the Declaration of Emergency, I report as follows:

RATE UPDATE BY RICONDO & ASSOCIATES: As I mentioned in my second interim report, CPA's Bond Consultant representative Ms. Bonnie Deger of Ricondo &

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Associates undertook the field work compilation to update the 2006 Rate Report. The work included reviewing all CPA revenue sources and expense items; management; and operational costs. In addition to meeting with CPA Management and counsel, Ricondo met with the airlines and tenants; Deloitte & Touche; the Bond Trustee; MVA and the Administration.

Ricondo has submitted its Draft Report to CPA and we have provided comments. Ricondo will be finalizing that report and the recommendations shall be implemented once we receive that final report. Material information at this point is that Ricondo will make recommendations to operations; management; and rates. Once we receive that final report, which is expected by July 15th, CPA may make it available for everyone's information as it implements those recommendations as required under the Bond Indenture Agreement.

FY 2007 AUDIT REPORT: CPA's auditing firm, Deloitte and Touche, has completed the draft audit and efforts are well underway toward finalizing. Per the Acting Comptroller Frances Mafnas, several issues on the audit are the following: (1) Interest (25%) charged by NMIRF on outstanding amounts due to NMIRF payments for 2006 ER contributions. The amount of interest is approximately \$240,000¹. (2) The auditors are also awaiting final form of CUC/CPA MOA on Superseding Agreement on the Sewer Line and Wharfage Fees offset agreement. CUC finally agreed to the superseding agreement and the auditors and Ricondo are aware of this fact. The executed copy is being amended to reflect a lesser amount (about \$100,000 less) on the Sewer Line amount. This adjustment will be reflected in the final audit report.

The FY 2007 Final Audit Report, you can be sure, will reveal the continued financial problems which beset CPA as a result of decreased revenues flowing from the Airline Incentive Program. CPA will continue to work toward increasing revenues such as the ongoing effort to resolve the food/beverage concession issue with LSG and to develop the East and West Concourses for better sales in food concessions.

But the challenges will remain for a period of time before we will see the opportunity for full financial integrity at CPA. We do hope that we continue the strides forward toward that goal with the Administration and Legislature's support.

¹ For background reference, CPA incurred a substantial loss resulting from the check-kiting scheme by Information Data Services ("IDS") back on October, 2006. IDS prepared the payroll for CPA as it did with other companies like Mobil, PIC and World Resort. The FBI raided IDS and froze all accounts. Checks which IDS had written back to CPA as a result of the suspension of the retirement contributions, were insufficient and rejected by the Bank. As a result CPA did not remit Employer and Employee contributions for several months. NMIRF issued demand letters and CPA has been paying back this amount in installments of approximately \$40,000 per month. The entire back amount of delinquent contributions will be paid in full by September 2009 (on a 24 month payment plan). NMIRF, despite CPA's request to waive the penalty as a result of the criminal conduct by IDS, imposed a 25% penalty upon CPA (the \$240,000 amount).

SEAPORT BOND INDENTURE RATE STUDY/ BOND CONSULTANT: CPA has previously informed the Administration and the Legislature that with the 60% reduction in revenue at the Port of Saipan, CPA also expects that the debt service ratio will also become an issue for the Seaport Revenue Bond.

Indeed, previously at the briefing on May 1st with the Legislature, CPA has requested that the Legislature and CDA consider waiving or deeming satisfied the balance of the CIP project bond of approximately \$6 million which CPA is paying at approximately \$68,000 per month.

The contemplated or requested legislation, sent to House Floor Leader Joseph Camacho, has not materialized and it is unknown whether the Legislature or CDA support CPA's request and/or whether the Legislature or CDA Board will agree to the proposal. As a result, the debt service coverage will become deficient given this drop in revenue prompted by the closure of garment factories and the decrease in seaport revenues.

To comply with the separate Seaport Bond Indenture Agreement, CPA has solicited the services of BST Associates out of Kenmore, WA which specializes in seaport rate reviews as required by the Bond Indenture Agreement. CPA intends to proceed on this on a Sole Source procurement given the exigency of the bond indenture requirement and the specialized requirement.

The preliminary information on the debt service coverage is that it may be at .84, well below the requirement of 1.25. As you may all know very well by now, the rate study will propose rate increases which will be passed on to the shipping industry in the form of tariffs and will further affect all involved in our local economy. Unfortunately, CPA is faced with having to undertake this reality as a result of the Bond Indenture Agreement for the seaport bond.

EMERGENCY PROCUREMENT OF CPA AIRPORT BACK-UP GENERATOR:

Recently it has been accurately reported that CPA's back-up generator at the Saipan International Airport has started to fail. This is a serious and disturbing development.

The load-shedding at CUC has affected CPA's ability to deliver service and calling upon the increased load on the generator which is intended for back-up and limited service. This back-up generator is an item of great urgency. Today's paper reported on the complete black-out at CPA with the failure of the back-up generator, affecting travelers and compromising safety. CPA's vendor has provided a quotation for the repair of the existing generator and CPA is conferring with FAA regarding the procurement of a second back-up generator.

CPA PERSONNEL NEEDS: Since the last Interim Bond Report, there have been several staff resignations at CPA. These include the Staff Engineer whose separation

date with CPA will be effective July 19. Replacements hiring is currently being considered with a view on the financial impacts of such hiring.

CPA has advised the Administration, the Bond Consultant and the Bond Trustee regarding these personnel needs. Some of the needs have arisen because of the military deployment of CPA personnel. CPA has provided a justification and the financial impact costing to the foregoing parties.

Current CPA staffs confirmed for military deployment in mid July are as follows: ARFF (4) and Ports Police (1). Both ARFF and Ports Police have requested for replacement hiring and are included in the above. CPA is assessing personnel needs due to resignations and military deployment of current staff. Personnel are needed with CPA Ports Police and AARF to ensure compliance with the homeland security and FAA safety requirements. However, funding remains a significant challenge. CPA must raise the revenue to pay for these critical staff. As a result, CPA will continue to consult with the Bond Trustee and the Administration for their concurrence before any hiring.

CPA BOARD AND MANAGEMENT STATUS: As you may be aware, I am also separating from CPA effective July 31st. The Legislature, in House Joint Resolution 16-5, rejected the Governor's Executive Order relating to the 120-day period placing CPA under the Executive Branch.

As CPA understands it, the status is that CPA remains under the Administration's supervision and control based on the Emergency Declaration. Under its Bylaws, CPA requires at least four (4) Board Members to constitute a quorum and to conduct its business.

Of course, the Administration may terminate the Emergency Declaration given the corrective measures which have been fully implemented. In fact, Governor Fitial has issued additional directives correcting CPA's Travel Per Diem to be consistent with the central government. CPA has also instituted the corrective measures regarding salary caps.

For its part CPA Management can and has operated CPA pending the nomination and confirmation of a full board or the minimum number required for a quorum. In transition from the prior Administration, this occurred and CPA was able to function without limitation pending the confirmation of a full board to handle major policy issues. This matter of CPA's governance and future, however, is left to the discretion of the Administration and the advice/consent of the Senate.

In my humble view as the Acting Executive Director, however, the CPA management and staff believe that it is more prudent to restore CPA's Board as soon as possible. I understand that on June 27th Acting Governor Villagomez nominated Thomas P. Villagomez of Saipan and Manuel Villagomez on Tinian to the CPA Board. I am not aware of the status of those nominations. I also understand that Acting

Governor Villagomez has requested Board Director Jose R. Lifoifo to rescind his resignation letter dated May 16th.

If these persons become part of the CPA Board then at least one more person is needed to muster a quorum and the CPA Board can conduct its business. Perhaps the question remains whether the circumstances which prompted the Emergency Declaration exist today. In my view the Governor's Directives have fully addressed those serious and major concerns. The directives have been fully implemented to comply with the Bond Indenture Agreement requirements. What remains now is the administrative and operational governance of CPA. Given the turnover in key staff and management, it appears appropriate that the CPA Board of Directors be restored as soon as possible to ensure that the changes which have taken place are carried through to completion.

It is clear to CPA Management that the Bond Trustee continues to closely monitor CPA's status to ensure its independence and autonomy as required under the Bond Indenture Agreement. Restoring CPA's autonomy with its Board of Directors and continuing to work with the Administration, Legislature and the Bond Trustee ensure the continued progress toward resolution of CPA's challenges.

Sincerely,

A handwritten signature in black ink, appearing to be 'Lee Cabrera', written in a cursive style.

LEE CABRERA
ACTING EXECUTIVE DIRECTOR

cc: LT. GOVERNOR
ATTORNEY GENERAL
CPA BOARD OF DIRECTORS
CPA ACTING COMPTROLLER