

Navajo Agricultural Products Industry  
An Enterprise of the Navajo Nation

Single Audit Reporting Package  
May 31, 2009 and 2008

Navajo Agricultural Products Industry  
 Single Audit Reporting Package  
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## Independent Auditor's Report

Honorable Chairman and Members of the Board of Directors  
Navajo Agricultural Products Industry  
Farmington, New Mexico

We have audited the accompanying financial statements of the Navajo Agricultural Products Industry, an enterprise of the Navajo Nation, as of and for the years ended May 31, 2009 and 2008, as listed in the table of contents. These financial statements are the responsibility of the Navajo Agricultural Product's Industry's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 2, the financial statements present only the Navajo Agricultural Products Industry and do not purport to, and do not, present fairly the financial position of the Navajo Nation as of May 31, 2009 and 2008 and the changes in its financial position, or, where applicable, its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Navajo Agricultural Products Industry as of May 31, 2009 and 2008, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 21, 2009, on our consideration of the Navajo Agricultural Products Industry'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 to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 3 through 14 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the Navajo Agricultural Products Industry's financial statements. The accompanying schedule of expenditures of federal awards listed in the table of contents is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

*Muller, Allen & Co PC*

August 21, 2009





P.O. DRAWER 1318 · FARMINGTON, NM 87499 · PHONE (505) 566-2600

August 21, 2009

### **Management's Discussion and Analysis**

This discussion and analysis introduces the basic financial statements and provides an overview of Navajo Agricultural Products Industry's (NAPI) financial activities for the years ended May 31, 2009 and 2008. Please read it in conjunction with the financial statements, which immediately follow.

### **Primary Missions:**

The Navajo Agricultural Products Industry's primary missions are as follows:

- To operate a profitable commercial farm,
- To plan, develop, and promote the use of agricultural and related resources, including water in compliance with the Navajo Nation Water Code,
- Promote agribusiness development, the multiplier effect, and related businesses and industries in the Navajo Nation.

### **Financial Highlights:**

- The NAPI's overall financial position improved in fiscal year 2009. The assets of NAPI exceeded its liabilities at the close of the fiscal year by \$73,875,863. Included in this amount is \$38,120,013, which may be used to meet NAPI's ongoing mission of operating a profitable commercial farm.
- NAPI's total net assets increased by \$9,479,497.
- At May 31, 2009, total NAPI assets were \$92,854,980, compared to \$79,661,065 at May 31, 2008. NAPI's most significant current asset is crops in progress of \$16,965,725 at May 31, 2009, compared to \$15,859,569 at May 31, 2008.
- At May 31, 2009, NAPI's current assets of \$32,652,345 were sufficient to cover current liabilities of \$10,178,747 (current ratio of 3.21). At May 31, 2008, NAPI's current assets of \$31,548,194 exceeded current liabilities of \$10,909,069 (current ratio of 2.89).
- NAPI's liabilities totaled \$18,979,117 at May 31, 2009 compared to \$15,264,699 at May 31, 2008. A \$6,458,702 long-term note payable to Wells Fargo Bank represents the largest liability as of May 31, 2009.
- The Navajo Agricultural Products Industry total debt increased by \$4,765,969 (76%) between fiscal years 2009 and 2008.

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- NAPI's gross crop revenues were \$43,374,476 and \$35,574,862 for the years ended May 31, 2009 and 2008, respectively. This represented an increase in crop revenue of \$7,799,614 from the previous fiscal year. Crop revenues increased significantly as a result of the increase in the price of potatoes and pinto beans. Potatoes prices experienced an increase of three times than the budgeted price for FY2009.
- Funding for the Navajo Indian Irrigation Project and other related grants was \$7,670,383 and \$6,318,052 for the years ended May 31, 2009 and 2008, respectively. This represented an increase in intergovernmental revenue of \$1,352,331 or 21% from the previous fiscal year. This increase is a result of additional funding provided by the governmental entities to support the NIIP and related projects under the 638 contract.
- Income from agricultural-related leases was \$2,286,250 and \$1,781,521 for the years ended May 31, 2009 and 2008, respectively. This represented an increase of \$ 504,729 or 28% from the previous fiscal year. This increase was a result of the increase acreage being allotted to those leases along with an increase in the rental cost per acre.
- Selling and administrative expenses were \$4,594,626 and \$3,892,127 for the years ended May 31, 2009 and 2008, respectively. This represented an increase of \$702,499 or 18% from the previous fiscal year. The increase represents a significant change with NAPI's organizational chart in December 2008 with the addition of a Chief Operations Officer along with disbursement of the NAPI Employee Profit Sharing as approved by the NAPI Board of Directors.
- Interest and fiscal charges were \$425,061 and \$383,822 for the years ended May 31, 2009 and 2008, respectively. This represented an increase of \$41,239 or 11% from the previous fiscal year due to the renewal and use of the line of credit agreement and the Center Pivot Rehabilitation loan.

**Overview of the Basic Financial Statements:**

The NAPI's annual financial statements are presented in accordance with the Governmental Accounting Standards Board (GASB) Statement No. 34, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments". This format is similar to the type of financial statements typical of a business enterprise. The basic financial statements consist of the following:

The Statement of Net Assets reflects the financial position of NAPI at May 31, 2009 and 2008. It shows the various assets owned or controlled, related liabilities and other obligations, and the various categories of net assets. Net assets is an accounting concept defined as total assets less total liabilities, and as such, represents equity or ownership in the total assets of NAPI. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of NAPI is improving or deteriorating when considered with nonfinancial facts such as crop statistics (yields, acres in production, etc.) and the condition of facilities.

The Statement of Revenues, Expenses, and Changes in Net Assets reflects the results of operations and other changes for the year ended May 31, 2009 and 2008. It shows the various revenues and expenses, both operating and nonoperating, reconciling the beginning net assets amount to the ending net assets amount – which is shown on The Statement of Net Assets described above.

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The Statement of Cash Flows presents the inflows and outflows of cash and cash equivalents for the years ended May 31, 2009 and 2008. It shows the various cash activities by type, reconciling the beginning cash and cash equivalents amount to the ending cash and cash equivalents amount, which is shown on the Statement of Net Assets described above. In addition, this statement reconciles cash flows from operating activities to operating income/loss on the Statement of Revenues, Expenses and Changes in Net Assets described above.

The condensed financial information below highlights the main categories of The Statement of Net Assets. Assets and liabilities are distinguished as to their current or noncurrent nature. Current liabilities are typically those obligations intended for liquidation or payment within the next fiscal year while current assets are those resources that are available for use in meeting the operating needs of NAPI, including current liabilities. Net assets are divided into two categories reflecting the equity in assets by broad characteristics.

**Condensed Financial Information**

**Condensed Statements of Net Assets  
As of May 31, 2009 and 2008**

	May 31, 2009	May 31, 2008
<b>Assets:</b>		
Current assets	\$32,652,345	\$31,548,194
Noncurrent assets, other than capital assets	13,379,653	9,517,760
Capital assets, net	46,822,982	38,595,111
Total assets	\$92,854,980	\$79,661,065
<b>Liabilities:</b>		
Current liabilities	\$10,178,747	\$10,909,069
Noncurrent liabilities	8,800,370	4,355,630
Total liabilities	\$18,979,117	\$15,264,699
<b>Net assets:</b>		
Invested in capital assets, net of related debt	\$35,755,850	\$32,293,948
Unrestricted net assets	38,120,013	32,102,418
Total net assets	\$73,875,863	\$64,396,366

At May 31, 2009, total NAPI assets were \$92,854,980, compared to \$79,661,065 at May 31, 2008. NAPI's most significant current asset is crops in progress of \$16,965,725 at May 31, 2009, compared to \$15,859,569 at May 31, 2008.

At May 31, 2009, NAPI's current assets of \$32,652,345 were sufficient to cover current liabilities of \$10,178,747 (current ratio of 3.21). At May 31, 2008, NAPI's current assets of \$31,548,194 exceeded current liabilities of \$10,909,069 (current ratio of 2.89).

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NAPI's liabilities totaled \$18,979,117 at May 31, 2009 compared to \$15,264,699 at May 31, 2008. A \$6,458,702 long-term note payable to Wells Fargo Bank represents the largest liability as of May 31, 2009.

The Navajo Agricultural Products Industry total debt increased by \$4,765,969 (76%) between fiscal years 2009 and 2008.

As noted earlier, net assets may serve over time as a useful indicator of NAPI's financial position. In the case of the Navajo Agricultural Products Industry, assets exceeded liabilities by \$73,875,863 at the close of the most recent fiscal year.

By far the largest portion of the Navajo Agricultural Products Industry's net assets (48%) reflects its investment in capital assets (e.g. land improvements, buildings, irrigation and sprinkler equipment, automotive equipment, office and communication equipment, construction in progress, software, and farm, feedlot, shop and other equipment) less any related debt used to acquire those assets that is still outstanding. The Navajo Agricultural Products Industry uses these capital assets to operate its agricultural activities; consequently, these assets are not available for future spending. Although the Navajo Agricultural Products Industry's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The condensed financial information below highlights the main categories of the Statement of Revenues, Expenses, and Changes in Net Assets. The major sources of gross operating revenues for NAPI are agricultural products: alfalfa, barley, corn, tablestock potatoes, wheat, oats, beans, feed yard, intergovernmental revenue and agricultural-related leases. Depreciation expense is recorded in accordance with the adoption of the economic resources measurement focus. For a description of the difference between operating and nonoperating, please refer to the Summary of Significant Accounting Policies, Note 2 to the basic financial statements.

**Condensed Statements of Revenues, Expenses, and Changes in Net Assets**  
**For the Years Ended May 31, 2009 and 2008**

	May 31, 2009	May 31, 2008
<b>Revenues:</b>		
Operating:		
Crops	\$43,374,476	\$35,574,862
Agricultural-related leases	2,286,250	1,781,521
Sale of electric power rights	714,206	955,762
Indirect cost recovery	938,109	249,253
Nonoperating:		
Intergovernmental	7,670,383	6,318,052
Investment income	56,781	479,658
Other	(32,058)	279,141
Gain (loss) on sale of capital assets	(15,410)	38,667

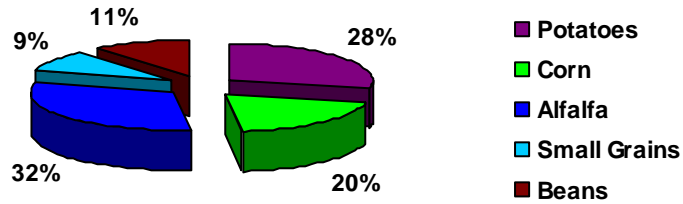
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**Condensed Statements of Revenues, Expenses, and Changes in Net Assets  
For the Years Ended May 31, 2009 and 2008**

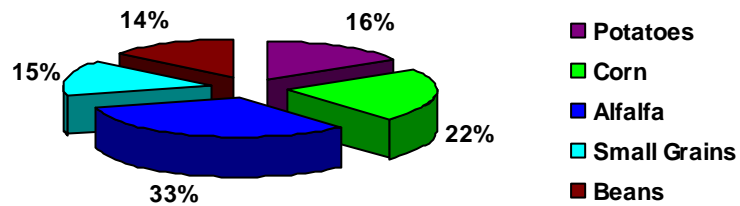
	<b>May 31, 2009</b>	<b>May 31, 2008</b>
Total revenues	<u>54,992,737</u>	<u>45,676,916</u>
<b>Expenses:</b>		
Operating:		
Cost of crops and goods sold:		
Crops	32,823,170	28,868,265
Selling and administrative	4,594,626	3,892,127
Nonoperating:		
Costs associated with the Navajo Indian Irrigation Project and other related grants	7,670,383	6,318,052
Interest and fiscal charges	<u>425,061</u>	<u>383,822</u>
Total expenses	<u>45,513,240</u>	<u>39,462,266</u>
Income before contributions and transfers	9,479,497	6,214,650
Transfers to the Navajo Nation – Scholarship Fund	<u>-</u>	<u>(500,000)</u>
Change in net assets	9,479,497	5,714,650
Net assets, beginning	<u>64,396,366</u>	<u>58,681,716</u>
Net assets, ending	<u>\$73,875,863</u>	<u>\$64,396,366</u>

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**2009 Significant Crop Revenue -  
by Crop**

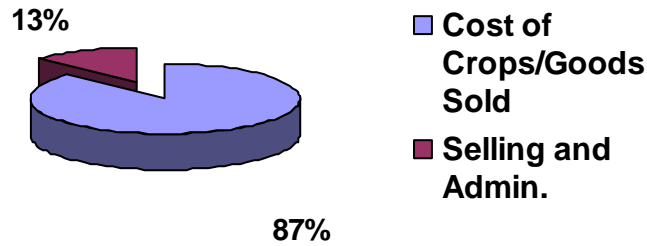


**2008 Significant Crop Revenue -  
by Crop**

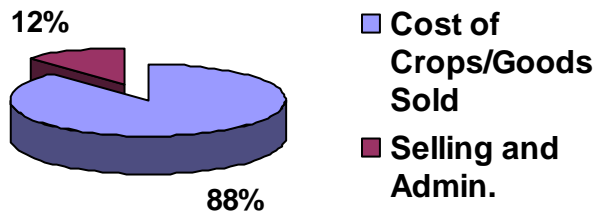


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**2009 Operating Expenses - by Type**



**2008 Operating Expenses - by Type**



NAPI's gross crop revenues were \$43,374,476 and \$35,574,862 for the years ended May 31, 2009 and 2008, respectively. This represented an increase in crop revenue of \$7,799,614 from the previous fiscal year. Crop revenues increased significantly as a result of the increase in the price of potatoes and pinto beans. Potatoes prices experienced an increase of three times than the budgeted price for FY2009.

Funding for the Navajo Indian Irrigation Project and other related grants was \$7,670,383 and \$6,318,052 for the years ended May 31, 2009 and 2008, respectively. This represented an increase in intergovernmental revenue of \$1,352,331 or 21% from the previous fiscal year. This increase is a result of additional funding provided by the governmental entities to support the NIIP and related projects under the 638 contract.

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Income from agricultural-related leases was \$2,286,250 and \$1,781,521 for the years ended May 31, 2009 and 2008, respectively. This represented an increase of \$504,729 or 28% from the previous fiscal year. This increase was a result of the increase acreage being allotted to those leases along with an increase in the rental cost per acre.

Selling and administrative expenses were \$4,594,626 and \$3,892,127 for the years ended May 31, 2009 and 2008, respectively. This represented an increase of \$702,499 or 18% from the previous fiscal year. The increase represents a significant change with NAPI's organizational chart in December 2008 with the addition of a Chief Operations Officer along with disbursement of the NAPI Employee Profit Sharing as approved by the NAPI Board of Directors.

Interest and fiscal charges were \$425,061 and \$383,822 for the years ended May 31, 2009 and 2008, respectively. This represented an increase of \$41,239 or 11% from the previous fiscal year due to the renewal and use of the line of credit agreement and the Center Pivot Rehabilitation loan.

**Capital Assets and Debt Administration:**

**Capital assets** – The Navajo Agricultural Products Industry's investment in capital assets (net of accumulated depreciation) as of May 31, 2009 and 2008 amounts to \$46,822,982 and \$38,595,111, respectively. This investment in capital assets includes land improvements, buildings, irrigation and sprinkler equipment, automotive equipment, office and communications equipment, construction in progress, software, and farm, feedlot, shop, and other equipment. The total increase in the Navajo Agricultural Products Industry's investment in capital assets for the current fiscal year was 21%.

Major capital asset events during the current fiscal year included the following:

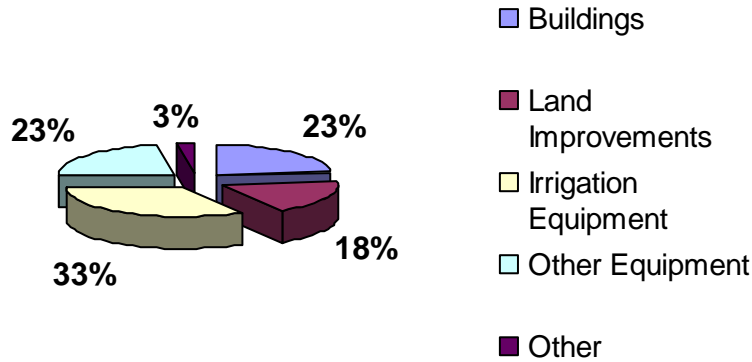
- Center Pivot Rehabilitation Project of Block 2, \$6,458,702;
- Farm Equipment, \$1,362,566.



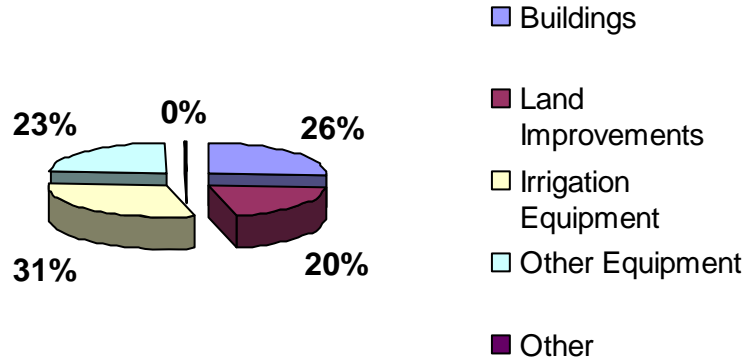
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The following chart depicts the distribution of NAPI's capital assets – by type at May 31, 2009 and 2008, respectively.

**2009 Capital Assets - by Type**



**2008 Capital Assets - by Type**



Additional information on the Navajo Agricultural Products Industry's capital assets can be found in Note 6 to the financial statements on page 28.

**Long-term debt** – As of May 31, 2009 and 2008, NAPI had total long-term debt of \$11,067,132 and \$6,301,163, respectively. As of May 31, 2009, this long-term debt comprised of 3 bank note payables and equipment purchase agreements. As of May 31, 2008, this long-term debt comprised of 4 bank note payables and equipment purchase agreements. In fiscal year 2009, to

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finance the purchase of pivot irrigation equipment, NAPI secured a new bank note payable in the amount of \$6,458,702. To finance the purchase of farm equipment, NAPI secured new capital lease debt of \$1,362,566 for the year ended May 31, 2008. During the years ended May 31, 2009 and 2008, NAPI repaid long-term debt in the amounts of \$1,984,333 and \$2,455,310, respectively.

<b>Navajo Agricultural Products Industry's Outstanding Debt</b>		
	2009	2008
Capital leases	\$1,682,038	\$2,428,291
Notes payable	9,093,494	3,872,872
Credit agreement	291,600	-
Total	\$11,067,132	\$6,301,163

**Navajo Indian Irrigation Project (NIIP):**

In 1962 the United States Congress authorized the construction of the Navajo Indian Irrigation Project (NIIP) for the sole purpose of providing a water delivery system from the Navajo Dam reservoir to the Navajo Nation. This project is a partial satisfaction of The Treaty of 1868 to the Navajo Nation. Revenues and expenditures from the above Public Law 93-638 Programs (Operations and Maintenance, On-Farm Development, and Soil Labs) comprised the most significant portion of NAPI's federal financial assistance. Operation and Maintenance maintains the 71-mile canal system and pipeline that transports irrigated water throughout NAPI, On-Farm Development is responsible for the installation of new irrigation systems; the Soil Labs tests the soil to ensure adequate moisture and fertilizer application.

Intergovernmental revenues from these programs totaled approximately \$7,670,383 for the year ended May 31, 2009 and \$6,318,052 for the year ended May 31, 2008. Recognized expenditures of such funds were \$7,670,383 and \$6,318,052 for the year ended May 31, 2009 and for the year ended May 31, 2008, respectively.

**Economic Outlook and Agricultural Outlook:**

**Economic Outlook –**

- GDP (Gross Domestic Product) was projected to decrease by 2.9 percent after inflation in 2008 and by 2.8 percent in 2009; however, with the substantial slowing of the economy in both 2008 and 2009 and recessionary status both the US and global economies, GDP growth is currently projected to fall by 3.9 percent or lower for 2009.
- Unemployment rate has increased to current 9.1 percent through May 2009; however, with the certain indicators predicting continued uncertainty of the US economy, this could change significantly.
- CPI (Consumer Price Index) is projected to decline from 2.3 percent for 2008 to 0.3 percent for 2009.
- Real GDP growth among the United States' major trading partners is forecast to decline by 6.1 percent which is significantly lower than growth in the United States. Average growth during the 2008-2009 is expected to be negative 1.3 percent for the Asian Pacific

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countries, about 1.1 percent for Latin America, and negative 2.8 percent for Western Europe and Canada.

- The expectation exists for the federal funds rate to decrease by 100 basis points by the fall of 2008 and the rate to be below 1% by the spring of 2009.
- The interest rate on 3-month Treasury bills is expected to decrease significantly below 1% through the 2009 fiscal year.
- The interest rate on 10-year Treasury notes is projected to decline by 7 percent in 2009.
- Crude oil prices in 2009 are expected to decline approximately 50 percent from 2008.
- Gasoline and diesel prices will be down by approximately 40 percent.

**Agricultural Outlook –**

- Exports:
  - Compared to an earlier forecast in May 2009, the economic environment is now perceived to be in a recession. As a result, US farm exports as the rest of the world's growth is weaker and the strength of the US dollar has also devalued by approximately 2.6 to 3 percent in several major markets. This could affect dry bean exports to Mexico along with countries in South America and Africa.
  - The forecast for fiscal 2009 agricultural exports is \$96 billion which is a result of an increase demand for soybeans and a decline demand for wheat; however, this is a decline of \$19.5 billion from \$115.5 billion for 2008.
  - Grains which were forecasted at a record \$23 billion in fiscal 2008 is expected to decline significantly in 2009 as a result of the projected decline of US wheat exports of \$1 billion, an expected \$300 million rise of corn exports and a decline of \$500 million for feed exports as a result of the declining demand of meat, leather and dairy products in US and global markets.
  - US corn crop production has increased marginally with the expectations of the 2008 corn prices as it relates to the domestic ethanol production. However, according to the latest USDA reports, it is projected that the demand for corn exports will be lower based on the current status of the global economy.
  - The fiscal 2009 wheat exports are expected to decline from the 2008 increase of an approximate \$1.3 billion from the 2007. This is due to downward revisions in wheat volume and value along with stronger competition from key suppliers such as Australia and Russia.
  - Total US potato exports are expected to increase by 5 percent despite the current economic situation. The projected price of potatoes is expected to increase 19 percent from 2008 to 2009.
- Imports:
  - The revised import forecast for 2009 is \$81 billion, 2 percent (\$2 billion) more than 2008.
  - The result of the current domestic economic conditions and the fluctuation of the US dollar's exchange rate could slow the import growth in 2009 with a weaker domestic and global economic activity.

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- Initial import projections for 2009 shows a marginal increase for grains and feed which are predicted to increase only by \$100 million over 2008 \$600 million increase. Again, this is a result of lower cattle imports and a weaker domestic and global economy.
- US imports of bulk grains remain relatively flat from 2008's predicted increases of nearly 40 percent. All other grains, feeds, and grain product groups are predicted to increase marginally but will not experience the double-digit rates based on value in 2006-2008 fiscal periods. These imports are predicted by lower domestic prices and reduced domestic supply as a result of the current economy. The import prices of feed and wheat are predicted to decrease where as corn price are expected to remain relatively stable and might increase slightly.

### **Other Matters with Potential Impact on Future Operations**

Agricultural products experience periodic changes due to uncontrollable market conditions and future commodity pricing cannot be predicted. Adequate supplies of water are also a significant consideration for farming enterprises in the Southwest. NAPI's supply of water has historically been sufficient. NAPI management views this as a competitive advantage until such time that the current drought conditions improve in the region.

Navajo Indian Irrigation Project funding has increased over previous levels for 2009 and 2008. Future funding levels cannot be determined at this time. Additional planned expansion of irrigated cropland may be slowed unless appropriations are returned to previous levels of funding.

### **Request for Information**

This financial report is designed to provide a general overview of the Navajo Agricultural Products Industry's finances for all those with an interest in NAPI's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Mr. Russell Litke, Chief Financial Officer, PO Drawer 1318, Farmington, New Mexico, 87499.

## Basic Financial Statements

**Navajo Agricultural Products Industry**  
**Statements of Net Assets**  
**May 31, 2009 and 2008**

<b>Assets</b>	2009	2008
<b>Current assets:</b>		
Cash and cash equivalents	\$ 9,549,505	\$ 2,653,626
Investments	2,140,611	2,551,339
Accounts receivable - trade (net of allowance for uncollectibles)	1,128,089	1,095,292
Accounts receivable - Navajo Agricultural Marketing, Inc.	2,000,000	8,600,000
Inventories	17,669,068	16,533,795
Prepaid items	165,072	114,142
Total current assets	32,652,345	31,548,194
<b>Noncurrent assets:</b>		
Accounts receivable - Navajo Agricultural Marketing, Inc.	4,374,579	2,476,437
Temporarily restricted:		
Cash and cash equivalents	73,128	-
Investments	4,470,440	4,418,424
Deferred alfalfa stand costs	4,361,533	2,404,247
Deferred conservation program costs	40,139	200,991
Other assets	59,834	17,661
Capital assets, net	46,822,982	38,595,111
Total noncurrent assets	60,202,635	48,112,871
Total assets	\$ 92,854,980	\$ 79,661,065
<b>Liabilities</b>		
<b>Current liabilities:</b>		
Accounts payable	2,200,917	2,400,059
Other accrued expenses	364,073	579,641
Deferred revenues	5,346,995	5,983,836
Current portion of long-term debt	2,266,762	1,945,533
Total current liabilities	10,178,747	10,909,069
<b>Noncurrent liabilities:</b>		
Noncurrent portion of long-term debt	8,800,370	4,355,630
Total noncurrent liabilities	8,800,370	4,355,630
Total liabilities	18,979,117	15,264,699
<b>Net Assets</b>		
Investment in capital assets, net of related debt	35,755,850	32,293,948
Unrestricted	38,120,013	32,102,418
Total net assets	\$ 73,875,863	\$ 64,396,366

The notes to the financial statements are an integral part of these statements.

**Navajo Agricultural Products Industry**  
**Statements of Revenues, Expenses, and Changes in Net Assets**  
**For the Years Ended May 31, 2009 and 2008**

	<u>2009</u>	<u>2008</u>
Operating revenues:		
Crops	\$ 43,374,476	\$ 35,574,862
Agricultural-related leases	2,286,250	1,781,521
Sale of electric power rights	714,206	955,762
Indirect cost recovery	<u>938,109</u>	<u>249,253</u>
Total operating revenues	<u>47,313,041</u>	<u>38,561,398</u>
Operating expenses:		
Cost of crops and goods sold:		
Crops	32,005,267	28,167,808
Agricultural-related leases	788,767	669,983
Feedyard	10,552	11,890
Convenience store operation	<u>18,584</u>	<u>18,584</u>
Total cost of crops and goods sold	32,823,170	28,868,265
Selling and administrative	<u>4,594,626</u>	<u>3,892,127</u>
Total operating expenses	<u>37,417,796</u>	<u>32,760,392</u>
Operating income	<u>9,895,245</u>	<u>5,801,006</u>
Nonoperating revenues (expenses):		
Intergovernmental revenues	7,670,383	6,318,052
Costs associated with the Navajo Indian Irrigation		
Project and other related grants	(7,670,383)	(6,318,052)
Investment income	56,781	479,658
Interest and fiscal charges	(425,061)	(383,822)
Gain (loss) on sale of capital assets	(15,410)	38,667
Other	<u>(32,058)</u>	<u>279,141</u>
Total nonoperating revenues (expenses)	<u>(415,748)</u>	<u>413,644</u>
Income before contributions and transfers	9,479,497	6,214,650
Transfer out to Navajo Nation Scholarship Fund	<u>-</u>	<u>(500,000)</u>
Change in net assets	9,479,497	5,714,650
Net assets, beginning	<u>64,396,366</u>	<u>58,681,716</u>
Net assets, ending	<u>\$ 73,875,863</u>	<u>\$ 64,396,366</u>

The notes to the financial statements are an integral part of these statements.

**Navajo Agricultural Products Industry**  
**Statements of Cash Flows**  
For the Years Ended May 31, 2009 and 2008

	2009	2008
<b>Cash flows from operating activities:</b>		
Receipts from customers	\$ 46,555,487	\$ 38,698,586
Payments to suppliers	(29,791,728)	(26,332,951)
Payments to employees	(7,956,205)	(6,598,927)
Net cash provided by operating activities	8,807,554	5,766,708
<b>Cash flows from noncapital financing activities:</b>		
Net change in accounts receivable (Navajo Agricultural Marketing, Inc.)	4,701,858	(10,622,523)
Transfers to the Navajo Nation (Scholarship Fund)	-	(500,000)
Net borrowings under revolving line of credit	-	3,000,000
Principal paid on revolving line of credit	-	(3,000,000)
Net cash provided (used) by noncapital financing activities	4,701,858	(11,122,523)
<b>Cash flows from capital and related financing activities:</b>		
Subsidy from federal grants	7,758,299	5,895,272
Disbursements of federal grants	(7,495,000)	(6,207,821)
Acquisition and construction of capital assets	(4,816,343)	(291,459)
Proceeds from sale of capital assets	38,598	38,667
Principal paid on notes and capital leases	(1,984,333)	(2,455,310)
Interest paid on notes and capital leases	(425,061)	(383,822)
Other receipts	(32,058)	111,987
Net cash used by capital and related financing activities	(6,955,898)	(3,292,486)
<b>Cash flows from investing activities:</b>		
Interest and dividends	56,781	479,658
Net purchases and sales of investments	358,712	(1,747,581)
Net cash provided (used) by investing activities	415,493	(1,267,923)
Net increase (decrease) in cash and cash equivalents	6,969,007	(9,916,224)
Cash and cash equivalents, beginning	2,653,626	12,569,850
Cash and cash equivalents, ending	\$ 9,622,633	\$ 2,653,626
<b>Reconciliation of operating income to net cash provided by operating activities:</b>		
Operating income	\$ 9,895,245	\$ 5,801,006
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation	3,284,766	3,151,446
Change in assets and liabilities:		
(Increase) decrease in accounts receivable - trade	(32,797)	448,511
(Increase) decrease in inventories	(1,135,273)	(2,806,392)
(Increase) decrease in prepaid items	(50,930)	(51,392)
(Increase) decrease in deferred alfalfa stand costs	(1,957,286)	(725,126)
(Increase) decrease in deferred conservation program costs	160,852	14,406
(Increase) decrease in other assets	(42,173)	-
Increase (decrease) in accounts payable	(374,525)	154,018
Increase (decrease) in other accrued expenses	(215,568)	91,554
Increase (decrease) in deferred revenue	(724,757)	(311,323)
Net cash provided by operating activities	\$ 8,807,554	\$ 5,766,708

**Noncash Investing, Capital, and Financing Activities:**

The following is information about all investing, capital, and financing activities of the Navajo Agricultural Products Industry for years ended May 31, 2009 and 2008 that affect recognized assets or liabilities but do not result in cash receipt or payments:

1.) Capital assets acquired through long term debt.	\$ 6,750,302	\$ 4,222,284
2.) Capital assets acquired via trade-in of existing assets.	\$ -	\$ 44,245

The notes to the financial statements are an integral part of these statements.



**Navajo Agricultural Products Industry**  
**Notes to Financial Statements**  
**For the Years Ended May 31, 2009 and 2008**

**Note 1 - Nature of Operations**

Navajo Agricultural Products Industry (NAPI), an Enterprise of the Navajo Nation, was created in 1967 for the purpose of administering the development and farming of certain Navajo Nation lands in northwestern New Mexico totaling 110,630 acres. The irrigated farm represents the utilization by the Navajo Nation of a federally funded project [Navajo Indian Irrigation Project (NIIP) established under Public Law 87-483] for irrigation and diversion of water from the San Juan River. Expenditure of funds for planning and development of the irrigated farm commenced in July 1971.

Operation of the irrigated farm project, consisting of 11 separate blocks or tracts of land of approximately 10,000 acres each, commenced in 1976. Through May 31, 2009, Blocks I through VII and a portion of Block VIII have been placed into service (approximately 70,000 acres) and are available for irrigated farming purposes. Of the 13,000 acres in Block VIII, nearly all has been placed into service. During the next crop year, the final 239 acres in Block VIII will be placed into service. At May 31, 2009, Blocks IX through XI were yet to be fully developed. Future development of Blocks IX through XI is dependent on receipt of additional funding.

NAPI's customers are located primarily in the southwestern United States including New Mexico, Arizona, California, Nebraska, and Texas. Also, during fiscal year 2008 NAPI sold the majority of its bean crop to Mexico. NAPI's principal crops are alfalfa, corn, potatoes, small grains, and beans. The revenues from these crops as a percentage of total crop revenues for the years ended May 31, 2009 and 2008 are as follow:

	<u>2009</u>	<u>2008</u>
Alfalfa	32%	33%
Potatoes	28%	16%
Corn	20%	22%
Beans	11%	14%
Small grains	9%	15%

Since NAPI sells a commodity, revenues may fluctuate significantly from year to year, depending on the market prices of the crops. In addition, the quantity and quality of product NAPI has available for sale is impacted by weather conditions during the planting, growing, and harvesting cycles.

In addition to farming and related operations, portions of the farm and certain adjacent Navajo Nation lands are periodically leased to outside parties for the purpose of agricultural and other farm-related activities.

**Navajo Agricultural Products Industry**  
Notes to Financial Statements  
For the Years Ended May 31, 2009 and 2008

**Note 2 - Summary of Significant Accounting Policies**

The financial statements of the Navajo Agricultural Products Industry have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) as applied to Enterprises of governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of NAPI's accounting policies are described below.

**A. Reporting Entity**

The Navajo Agricultural Products Industry is an Enterprise of the Navajo Nation. The financial statements present only the financial position, changes in financial position and cash flows of NAPI and do not purport to, and do not present fairly the financial position of the Navajo Nation and the changes in its financial position and its cash flows where applicable, in conformity with U.S. generally accepted accounting principles.

**B. Basis of Presentation and Accounting**

The Navajo Agricultural Products Industry's activities are similar to those found in the private sector, where the determination of net income is necessary or useful to sound financial administration.

The financial transactions of NAPI are recorded and reported as an Enterprise since its operations are financed and operated in a manner similar to private business enterprises, in which the intent of NAPI is that costs (expenses, including depreciation) of providing goods or services on a continuing basis be financed or recovered primarily through user charges.

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place.

Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, NAPI has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, except for those that conflict with or contradict GASB pronouncements.

In fiscal year 2008, the Navajo Agricultural Products Industry changed its accounting policy relating to its investment in the Navajo Agricultural Marketing, Inc. (NAMI). In

**Navajo Agricultural Products Industry**  
Notes to Financial Statements  
For the Years Ended May 31, 2009 and 2008

fiscal year 2007 the financial activity of NAMI was “blended” with the Navajo Agricultural Products Industry. In fiscal year 2008, the Navajo Agricultural Products Industry recorded NAMI as an investment as stipulated by the provisions of Statement of Governmental Accounting Standards (GASB Statement) No. 14, *The Financial Reporting Entity*. Accordingly, the cumulative effect of the accounting change as of the beginning of the fiscal year is reported in the Statement of Revenues, Expenses, and Changes in Net Assets.

The financial statements include statements of net assets; statements of revenues, expenses, and changes in fund net assets; and statements of cash flows.

A statement of net assets provides information about the assets, liabilities, and net assets of NAPI at the end of the year. Assets and liabilities are classified as either current or noncurrent. Net assets are classified according to external restrictions or availability of assets to satisfy NAPI obligations. Invested in capital assets net of related debt represents the value of capital assets, net of accumulated depreciation, less any outstanding debt incurred to acquire or construct the asset. Unrestricted net assets include all other net assets, including those that have been designated by management to be used for other than general operating purposes.

A statement of revenues, expenses, and changes in fund net assets provides information about NAPI’s financial activities during the year. Revenues and expenses are classified as either operating or nonoperating, and all changes in net assets are reported, including capital contributions. Operating revenues and expenses result from providing services and producing and delivering goods in connection with NAPI principal ongoing operations. All other revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

A statement of cash flows provides information about NAPI’s sources and uses of cash and cash equivalents during the year. Increases and decreases in cash and cash equivalents are classified as either operating, noncapital financing, capital financing or investing.

*Cash and Cash Equivalents* - For purposes of the statements of cash flows, NAPI considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. NAPI maintains cash and cash equivalents at certain financial institutions that may exceed federally insured amounts.

*Inventories* - Crops in progress inventories are stated at cost, which represent costs incurred through the fiscal year end. Harvested crops available for immediate delivery and that have a readily determinable and realizable market value are stated at net realizable value. Other inventories are valued at the lower of cost or market on a first-in, first-out basis.

**Navajo Agricultural Products Industry**  
Notes to Financial Statements  
For the Years Ended May 31, 2009 and 2008

*Investments* – In accordance with GASB Statement 31 *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, the Navajo Agricultural Products Industry's investments are stated at fair value.

*Capital Assets* -

i. Land

The land occupied by present and anticipated future farm operations of NAPI consists of certain portions of the present Navajo Nation reservation and other designated federal, state, and privately owned lands acquired by the Navajo Nation and placed in trust with the Federal Government. The title to such property remains with the Navajo Nation and, therefore, the cost or other value of the property is not reflected in the accompanying financial statements.

ii. Primary Irrigation Facilities and Roads

The primary irrigation canal system, roads, and related facilities were financed by the Federal Government and are maintained primarily by the Federal Government and others for the benefit of the Navajo Nation through NAPI. Ownership rights to these facilities and roads have not been transferred to NAPI and, therefore, the cost or other value of these assets has not been reflected in the accompanying financial statements.

iii. Other

Purchased capital assets are reflected at cost. Except as noted elsewhere, contributed capital assets are stated at fair market value at the time of receipt. NAPI capitalizes the contract construction costs, its own incurred direct construction labor, certain related overhead costs of land improvements (Blocks I through VIII), and irrigation and sprinkler equipment. Such land improvement costs are generally incurred during the primary development stage of the respective blocks. Costs of leveling and other expenditures that become a permanent part of the land are capitalized as incurred and are not depreciated or amortized as they have an indefinite useful life. Depreciation or amortization of depreciable assets constructed begins when the acreage is put to use.

Renewals and betterments of capital assets that significantly add to the productive capacity or extend the useful life of an asset are capitalized. Maintenance and repairs are charged to operating costs and expenses as incurred.

**Navajo Agricultural Products Industry**  
**Notes to Financial Statements**  
**For the Years Ended May 31, 2009 and 2008**

*Depreciation and Amortization* - depreciation and amortization of capital assets are provided using the straight-line method over the estimated useful lives of the respective assets, as follows:

	Useful lives (years)
Buildings	10 to 20
Irrigation and sprinkler equipment	3 to 20
Farm, feedlot, shop, and other equipment	3 to 20
Automotive equipment	3 to 5
Office and communication equipment	5 to 10
Software	5

*Capital Asset Capitalization Threshold* – *Capital* assets are defined by NAPI as assets with an initial, individual cost of more than \$1,000 and an estimated useful life in excess of one year.

*Alfalfa-Stand Costs* - deferred alfalfa stand costs, net of amortization, represent the direct and indirect costs of preparing alfalfa stands for cultivation. Such deferred costs are amortized to operations over the lives of the alfalfa stands, which are estimated to be five years.

*Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed of* - NAPI reviews long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

*Contributed Water and Related Cost* - In the course of conducting farm operations, NAPI utilizes irrigation water provided by the Federal Government, as discussed previously under primary irrigation facilities and roads. Neither the cost nor the contribution of the water is reflected in the accompanying financial statements.

*Nonexchange Transactions* -

Statement No. 33 of the GASB, *Accounting and Financial Reporting for Nonexchange Transactions* (Statement No. 33), establishes accounting and financial reporting standards for nonexchange transactions involving financial or capital resources and is effective for periods beginning after June 15, 2000. NAPI adopted Statement No. 33 as of March 1, 2001. NAPI receives grants from certain Federal Government agencies, primarily the BIA and the Bureau of Reclamation, which meet the definition of nonexchange transactions in

**Navajo Agricultural Products Industry**  
Notes to Financial Statements  
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Statement No. 33. Also, as an Enterprise of the Navajo Nation, capital contributions received from the Navajo Nation meet the definition of nonexchange transactions in Statement No. 33.

The Federal Government grants and the capital contributions received by NAPI are classified as voluntary nonexchange transactions as defined by Statement No. 33 and, accordingly, NAPI recognizes revenue for these transactions when all eligibility requirements have been met. Monies received before the eligibility requirements have been fulfilled by NAPI are reported as deferred revenue.

*Crop Revenues and Cost Recognition* - Crop revenues and associated costs are recognized on a "crop year" basis. The crop year ends when the crop is harvested or when substantially all associated costs are incurred. Costs associated with crops are matched with the corresponding revenue for the crop year. Crop costs incurred subsequent to the crop year are recorded as crops in progress in the fiscal year incurred, and are matched with the corresponding revenues of the following crop year's harvest.

*Accounts Receivables* - receivables are recorded net of allowance for doubtful accounts to report the receivables at their net realizable values.

*Investment Income* – investment income is composed of interest, dividends, and net changes in the fair value of applicable investments.

*Federal Income Taxes* – The Navajo Nation is a recognized Indian Nation and is exempt from Federal and State income taxes. Accordingly, no provision for Federal and State income taxes has been made in the financial statements.

*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.

*Concentrations of Credit Risk* – NAPI's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable. NAPI places its cash with high credit worthy institutions. At times such cash may be in excess of the FDIC insurance limit. NAPI routinely assesses the financial strength of its customers and, as a consequence, believes that its accounts receivable credit risk is limited.

*Reclassifications* - Certain amounts related to how cash and investments were presented in the May 31, 2008 financial statements have been reclassified to conform to the presentation of the May 31, 2009 financial statements. The reclassifications had no effect on the change in net assets at May 31, 2008.

Navajo Agricultural Products Industry  
Notes to Financial Statements  
For the Years Ended May 31, 2009 and 2008

**Note 3 - Deposits and Investments**

At May 31, 2009 and 2008, cash and cash equivalents consisted of the following:

	2009	2008
Cash on hand	\$1,850	\$900
Cash in bank	2,091,902	392
Cash equivalents – repurchase agreements	7,528,881	2,652,334
Total	<u>\$9,622,633</u>	<u>\$2,653,626</u>

**Deposits** – At May 31, 2009, NAPI’s cash on hand was \$1,850. The carrying amount of NAPI’s deposits was \$2,091,902, and the bank balance was \$2,019,148. NAPI does not have a deposit policy for custodial credit risk.

At May 31, 2008, NAPI’s cash on hand was \$900. The carrying amount of NAPI’s deposits was \$392, and the bank balance was \$392. NAPI does not have a deposit policy for custodial credit risk.

**Investments** – NAPI’s investments at May 31, 2009 and 2008 were as follows:

Investment Type	2009	2008
Money market mutual funds	\$6,611,051	\$6,969,763
Repurchase agreements	7,528,881	2,652,334
Total	<u>\$14,139,932</u>	<u>\$9,622,097</u>

**Interest Rate Risk** – NAPI does not have a formal investment policy that limits investment maturities as a means a managing its exposure to fair value losses arising from increasing interest rates. At May 31, 2009, NAPI’s investment maturities are as follows:

Investment Type	Amount	Investment Maturities Less than 1 Year
Mutual funds	\$6,611,051	\$6,611,051
Repurchase agreements	7,528,881	7,528,881
Total	<u>\$14,139,932</u>	<u>\$14,139,932</u>

**Navajo Agricultural Products Industry**  
**Notes to Financial Statements**  
**For the Years Ended May 31, 2009 and 2008**

At May 31, 2008, NAPI's investment maturities are as follows:

Investment Type	Amount	Investment Maturities Less than 1 Year
Mutual funds	\$6,969,763	\$6,969,763
Repurchase agreements	2,652,334	2,652,334
<b>Total</b>	<b>\$9,622,097</b>	<b>\$9,622,097</b>

*Credit Risk – Investments.* NAPI's investment policy limits investments in U.S. agency securities and money market mutual funds to the following credit quality ratings: AAA – the highest degree of safety with overwhelming repayment capacity; AA – very high degree of safety and capacity for repayment; and A/A-1 strong degree of safety and capacity for repayment. At May 31, 2009, credit risk for NAPI's investments was as follows:

Investment Type	Rating	Rating Agency	Amount
Money market mutual funds	AAA	Standard & Poor's	\$6,611,051
Repurchase agreements	N/A		7,528,881
		<b>Total</b>	<b>\$14,139,932</b>

At May 31, 2008, credit risk for NAPI's investments was as follows:

Investment Type	Rating	Rating Agency	Amount
Money market mutual funds	AAA	Standard & Poor's	\$6,969,763
Repurchase agreements	N/A		2,652,334
		<b>Total</b>	<b>\$9,622,097</b>

*Navajo Agricultural Marketing, Inc.* - The Navajo Agricultural Products Industry (NAPI) is the sole common stock shareholder in the Navajo Agricultural Marketing, Inc., a State of New Mexico corporation, (NAMI). NAMI was incorporated to purchase agricultural products in local and regional markets and to market such products in various agricultural markets. NAMI also trades and/or markets agricultural products on the Chicago Board of Trade and the Kansas City Board of Trade, and other commodities exchange markets.

Due to the substantive economic relationship between NAPI and NAMI, management utilizes the equity method of accounting for the investment in NAMI. Under this method, the carrying amount of the investment in NAMI's common stock is periodically increased (decreased) by NAPI's proportionate share of the earnings (losses) and decreased by all dividends received.



**Navajo Agricultural Products Industry**  
**Notes to Financial Statements**  
**For the Years Ended May 31, 2009 and 2008**

During fiscal years 2009 and 2008, NAMI's losses exceeded the carrying amount of NAPI's investment in the common stock. Therefore, management decreased the carrying amount of the investment in NAMI common stock to \$0. This practice is in accordance with the equity method of accounting for investments, whereby the investor (NAPI) should discontinue applying the equity method and not recognize additional losses.

**Note 4 - Accounts Receivable**

At May 31, 2009 and 2008, accounts receivable - trade were as follows:

	<u>2009</u>	<u>2008</u>
Receivables:		
Crops	\$1,113,836	\$615,610
Other	95,293	537,991
Gross receivables	<u>1,209,129</u>	<u>1,153,601</u>
Less allowance for uncollectibles	<u>(81,040)</u>	<u>(58,309)</u>
Net total receivables	<u>\$1,128,089</u>	<u>\$1,095,292</u>

In addition, at May 31, 2009 and 2008, NAPI recognized an accounts receivable in the amount of \$6,374,579 and \$11,076,437 respectively, from the Navajo Agricultural Marketing, Inc. (NAMI). This accounts receivable represents items such as:

- Short-term cash loans to NAMI;
- Corn and wheat inventory sold to NAMI;
- Fees associated with granary facility storage;
- Other miscellaneous charges paid by NAPI on behalf of NAMI for items such as consultants, travel, and utilities.

NAPI management classified \$2,000,000 of the fiscal year 2009 NAMI receivable as "current" due to payments received by NAPI from NAMI through July 2009. In addition, NAPI management classified \$8,600,000 of the fiscal year 2008 NAMI receivable as "current" due to payments received by NAPI from NAMI through December 2008.

**Note 5 - Inventories**

At May 31, 2009 and 2008, inventories were as follows:

	<u>2009</u>	<u>2008</u>
Crops in progress	\$16,965,725	\$15,859,569
Repair parts and supplies	703,343	623,630
Fresh Pak supplies	-	50,596
	<u>\$17,669,068</u>	<u>\$16,533,795</u>

**Navajo Agricultural Products Industry**  
**Notes to Financial Statements**  
**For the Years Ended May 31, 2009 and 2008**

**Note 6 - Capital Assets**

Capital asset activity for the year ended May 31, 2009 was as follows:

	Beginning Balance	Increases	Decreases	Reclass	Ending Balance
Capital assets, not being depreciated:					
Construction in progress	\$187,249	\$10,469,649		\$(7,988,162)	\$2,668,736
Total capital assets, not being depreciated	187,249	10,469,649		(7,988,162)	\$2,668,736
Capital assets, being depreciated:					
Land improvements	18,975,594				18,975,594
Buildings	24,661,541	59,828			24,721,369
Irrigation and sprinkler equipment	28,917,220		\$ (585,777)	7,020,582	35,352,025
Farm, feedlot, shop and other equipment	17,492,470	286,908	(2,950)	967,580	18,744,008
Automotive equipment	2,078,284	448,663	(17,565)		2,509,382
Software, office and communications equipment	2,322,567	301,597			2,624,164
Total capital assets, being depreciated	94,447,676	1,096,996	(606,292)	7,988,162	102,926,542
Less accumulated depreciation for:					
Land improvements	(2,851,147)	(3,838)			(2,854,985)
Buildings	(18,538,603)	(788,618)			(19,327,221)
Irrigation and sprinkler equipment	(21,680,890)	(571,534)	532,438		(21,719,986)
Farm, feedlot, shop and other equipment	(10,054,023)	(1,555,620)	2,655		(11,606,988)
Automotive equipment	(1,639,555)	(115,929)	17,191		(1,738,293)
Software, office and communications equipment	(1,275,596)	(249,227)			(1,524,823)
Total accumulated depreciation	(56,039,814)	(3,284,766)	552,284		(58,772,296)
Total capital assets, being depreciated, net	38,407,862	(2,187,770)	(54,008)	7,988,162	44,154,246
Total capital assets, net	\$38,595,111	\$8,281,879	\$(54,008)	\$-0-	\$46,822,982

Capital asset activity for the year ended May 31, 2008 was as follows:

	Beginning Balance	Increases	Decreases	Reclass	Ending Balance
Capital assets, not being depreciated:					
Construction in progress	\$ 1,348,234	\$ 187,249		\$ (1,348,234)	\$ 187,249
Total capital assets, not being depreciated	1,348,234	187,249		(1,348,234)	187,249
Capital assets, being depreciated:					
Land improvements	18,930,067	45,527			18,975,594
Buildings	23,692,045	122,530		846,966	24,661,541
Irrigation and sprinkler equipment	28,738,709	4,219		174,292	28,917,220
Farm, feedlot, shop and other equipment	14,156,383	3,451,642	\$ (345,972)	230,417	17,492,470
Automotive equipment	2,105,164		(26,880)		2,078,284
Software, office and communications equipment	1,523,432	702,576		96,559	2,322,567
Total capital assets, being depreciated	89,145,800	4,326,494	(372,852)	1,348,234	94,447,676
Less accumulated depreciation for:					
Land improvements	(2,847,882)	(3,265)			(2,851,147)
Buildings	(17,753,073)	(785,530)			(18,538,603)

**Navajo Agricultural Products Industry**  
**Notes to Financial Statements**  
**For the Years Ended May 31, 2009 and 2008**

	Beginning Balance	Increases	Decreases	Reclass	Ending Balance
Irrigation and sprinkler equipment	(21,111,238)	(569,652)			(21,680,890)
Farm, feedlot, shop and other equipment	(8,949,626)	(1,367,457)	263,060		(10,054,023)
Automotive equipment	(1,417,001)	(249,434)	26,880		(1,639,555)
Software, office and communications equipment	(1,099,488)	(176,108)			(1,275,596)
Total accumulated depreciation	(53,178,308)	(3,151,446)	289,940		(56,039,814)
Total capital assets, being depreciated, net	35,967,492	1,175,048	(82,912)	1,348,234	38,407,862
Total capital assets, net	\$ 37,315,726	\$ 1,362,297	\$ (82,912)	\$ 0	\$ 38,595,111

**Note 7 - Short-term Debt – Revolving Line of Credit**

During fiscal year 2009, NAPI entered into a revolving line of credit with Wells Fargo Bank. This revolving line of credit is to provide for short-term working capital to be used for the purchasing, trading and/or marketing of agricultural products. The responsible parties under this revolving line of credit are NAPI and the Navajo Agricultural Marketing, Inc. (a wholly owned corporation of NAPI). This revolving line of credit is authorized up to \$9,100,000, carries an interest rate at 2.375%, and has a maturity date of June 30, 2009. Interest accrued on this revolving line of credit shall be payable on the 15<sup>th</sup> day of each month, commencing December 15, 2008. During fiscal year 2009, NAPI/NAMI did not utilize this revolving line of credit and it had a balance of \$-0- at May 31, 2009.

This obligation is secured by crops, inventory and accounts receivable of both responsible parties, in addition to the commodity bank account of the Navajo Agricultural Marketing, Inc.

In fiscal year 2008, NAPI utilized a revolving line of credit to provide for short-term working capital to be used for agricultural purposes. This revolving line of credit is authorized up to \$3,000,000 and is fully due and payable on February 28, and shall be renewed annually thereafter. The revolving line of credit carries an interest rate at the Prime rate minus 0.25%. Short-term debt activity for the year ended 2008, was as follows:

	June 1, 2007	Draws	Repayments	May 31, 2008
Line of Credit	\$ - 0 -	\$3,000,000	\$3,000,000	\$ - 0 -

At May 31, 2008, NAPI had let the aforementioned revolving line of credit expire.

**Note 8 - Long-Term Debt**

Capital Leases

NAPI has entered into various lease agreements as the lessee for financing the acquisition of agricultural equipment. These lease agreements qualify as capital

**Navajo Agricultural Products Industry**  
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leases for accounting purposes and, therefore, have been recorded at the present value of their future minimum lease payments as of the inception date.

At May 31, assets acquired through capital leases are as follows:

	May 31, 2009	May 31, 2008
Asset:		
Farm, feedlot, shop, and other equipment	\$3,200,142	\$2,970,011
Less: accumulated depreciation	(1,364,788)	(1,155,127)
Total	\$1,835,354	\$1,814,884

The future minimum lease obligations and the net present value of these minimum lease payments as of May 31, 2009

Year ending May 31,	
2010	\$ 698,877
2011	639,245
2012	317,158
2013	185,006
Total minimum lease payments	1,840,286
Less: amount representing interest	(158,248)
Present value of minimum lease payments	\$1,682,038

**Note Payable**

At May 31, 2009 and 2008, NAPI's note payable consisted of the following:

	2009	2008
Wells Fargo bank note payable, secured by equipment, payable in annual installment of \$1,199,546, including interest of 6.81%, due April 2016.	\$6,458,702	
Key Equipment Finance note payable, payable in monthly installments of \$48,017, including interest of 6.46%, due September 2013.	2,172,800	\$ 2,593,769
Wells Fargo bank note payable, secured by crops and accounts receivables, payable in monthly installments of \$52,225, including interest at 6.00%, due February 2010.	461,992	1,037,704
Wells Fargo bank note payable, secured by crops and account receivables, payable in monthly installments of \$75,627, including interest at 4.00%, due July 2008.		150,484
Wells Fargo bank note payable, secured by the hay barn, payable in monthly installments of \$8,548, including interest of 6.86%, due April 2009.		90,915

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	2009	2008
Total notes payable	9,093,494	3,872,872
Less: current portion of the notes payable	(1,656,692)	(1,241,829)
Noncurrent portion of the notes payable	\$7,436,802	\$2,631,043

As of May 31, 2009, annual debt service requirements to maturity for the note payable are as follows:

	Principal	Interest	Total
Year ending May 31,			
2010	\$ 1,656,692	\$ 592,833	\$2,249,525
2011	1,276,976	498,775	1,775,751
2012	1,364,924	410,828	1,775,752
2013	1,458,933	316,819	1,775,752
2014	1,167,968	223,648	1,391,616
2015-2016	2,168,001	231,091	2,399,092
Total	\$9,093,494	\$2,273,994	\$11,367,488

Changes in long-term liabilities

Long-term liability activity for the year ended May 31, 2009 was as follows:

	June 1, 2008	Additions	Reductions	May 31, 2009	Due Within One Year
Notes Payable	\$ 3,872,872	\$ 6,458,702	(\$1,238,080)	\$9,093,494	\$1,656,692
Capital leases	2,428,291	-	(746,253)	1,682,038	610,070
Credit agreement	-	291,600	-	291,600	-
Total	\$6,301,163	\$6,750,302	(\$1,984,333)	\$11,067,132	\$2,266,762

Long-term liability activity for the year ended May 31, 2008 was as follows:

	June 1, 2007	Additions	Reductions	May 31, 2008	Due Within One Year
Capital leases	\$ 1,735,445	\$ 1,362,566	\$ ( 669,720)	\$ 2,428,291	\$ 703,704
Notes payable	2,798,743	2,859,718	(1,785,589)	3,872,872	1,241,829
Total	\$ 4,534,188	\$ 4,222,284	\$ (2,455,309)	\$ 6,301,163	\$ 1,945,533

**Note 9 - Deferred Revenue**

At May 31, 2009 deferred revenue consisted of the following:

Agricultural operations related:

1.) Prepaid leases	\$1,210,087	
2.) Prepaid crop payments	1,159,081	
3.) Other	49,995	
Total agricultural operations related deferred revenue		\$2,419,163

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Navajo Indian Irrigation Project (NIIP) and related:

1.) Portion of grant reimbursements in excess of expenditures.		
U.S. Department of Interior	2,927,832	
Total NIIP and related deferred revenue	2,927,832	2,927,832
Total deferred revenue		\$5,346,995

At May 31, 2008 deferred revenue consisted of the following:

Agricultural operations related:

1.) Prepaid leases	\$288,590	
2.) Prepaid crop payments	2,779,699	
3.) Other	75,631	
Total agricultural operations related deferred revenue	3,143,920	\$3,143,920

Navajo Indian Irrigation Project (NIIP) and related:

1.) Portion of grant reimbursements in excess of expenditures.		
U.S. Department Interior	2,839,916	
Total NIIP and related deferred revenue	2,839,916	2,839,916
Total deferred revenue		\$5,983,836

**Note 10 - Risk Management**

NAPI is exposed to various risks of loss related to torts and civil rights; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees and non-employees; and natural disasters. NAPI participates in the Navajo Nation Risk Management Program (Risk Management), which was established to manage, control, and minimize this risk. Under this program, the Risk Management pool provides coverage for up to a maximum of \$500,000 for each incident. Risk Management purchases commercial insurance for claims in excess of coverage provided by the Risk Management pool.

**Note 11 - Operating Agreements**

At May 31, 2009 and 2008 NAPI had various operating agreements as follows:

- (a) Pumpkin Patch Fundraisers, Inc.

On February 2, 1998, NAPI entered into an operating agreement with Pumpkin Patch Fundraisers, Inc. (Pumpkin Patch) to plant, grow, harvest, market, sell, and ship pumpkins grown on NAPI land. The parties entered into a revised operating agreement on May 23, 2002. Under this agreement, NAPI provides land, water, maintenance of the NAPI water delivery system, and limited equipment, materials, and labor costs. NAPI receives reimbursement of specified costs, a base lease payment for office space,

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and a portion of the revenue generated from the sale of pumpkins, including a guaranteed minimum. During the years ended May 31, 2009 and 2008, NAPI recorded revenues of approximately \$231,498 and \$179,575 respectively, under this agreement. Such revenue is included in agricultural-related joint ventures revenue in the accompanying financial statements. This agreement expires on December 31, 2014.

(b) Upland Desert Popcorn, Ltd.

On September 12, 2003, NAPI entered into an Industrial Park Lease and Facilities Agreement with Upland Desert Popcorn, Ltd. (UDP) to use only the construction, repair and maintenance of storage bins for popcorn. As part of the consideration of Upland Desert Popcorn for the nominal lease payments to be made to NAPI, UDP shall construct and install utilities, roadways and other infrastructure and keep facilities free of liens or any other encumbrances. Under this agreement, UDP has the option to farm corn in rotation with pumpkins. If UDP does so exercise such option, UDP shall pay NAPI \$140 per acre per year. During the years ended May 31, 2009 and 2008, NAPI recorded revenues of approximately \$493,558 and \$108,759 respectively, under this agreement. Such revenue is included in agricultural-related joint ventures revenue in the accompanying financial statements. This agreement expires on December 31, 2014.

(c) Navajo Mesa Farms, LLC

On February 1, 2003, NAPI entered into an operating and lease agreement with Navajo Mesa Farms, LLC (Navajo Mesa) to plant, grow, harvest, and store potatoes grown on approximately 1,595 acres of NAPI land. Under this agreement, NAPI provides land and water, maintenance on the NAPI water delivery system, storage facilities, a disposal area for waste potatoes and wastewater, and reasonable services from NAPI's soils lab. Navajo Mesa provides seed, seed freight, cultivation, center plot irrigation labor, chemigation, pesticide applications, harvest, hauling, storage, shipping, and any costs associated with these operations. This agreement was amended in 2009 to increase the total acres to approximately 4,000 with additional storage as well. NAPI receives rental payments for irrigated croplands and potato storage facilities in the amount of \$400 per acre per annum or \$1,600,000 per year. In addition, in any year Navajo Mesa exceeds \$2,600 per acre of gross sales, Navajo Mesa shall pay NAPI 10% of gross sales in excess of \$2,600 per acre as participation rent. Further, NAPI also receives payments for the use of the potato storage facility and scales. During the years ended May 31, 2009 and 2008, NAPI recorded revenues of approximately \$1,492,799 and \$1,101,999 respectively, under this agreement. Such revenue is included in agricultural-related joint ventures

**Navajo Agricultural Products Industry**  
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For the Years Ended May 31, 2009 and 2008

revenue in the accompanying financial statements. The agreement expires on October 31, 2018.

(d) Wilbur-Ellis Company

On November 02, 2003 NAPI entered into a facilities and equipment lease, and product sales and application agreement with Wilbur-Ellis Company. Under this agreement, Wilbur-Ellis shall maintain adequate inventories or products at the Facilities to meet NAPI's expected demand for the products. Wilbur-Ellis shall apply aerial application of products on a timely basis as requested by NAPI. NAPI shall lease to Wilbur-Ellis certain facilities for the storage and distribution of the products on NAPI land. During the years ended May 31, 2009 and 2008, revenue of approximately \$71,900 and \$62,000 respectively, was recognized under this agreement. The agreement expires on October 31, 2010.

(e) Sterling Brothers Construction (a.k.a. Sterling Brothers Feedlot)

On September 03, 2004, NAPI entered into a feedlot agreement with Sterling Brothers Construction. Under this agreement, Sterling Brothers Construction shall perform and manage all its activities on NAPI lands in accordance to the highest standards of agricultural practices in maintaining the NAPI feedlot in accordance to US EPA, NPSES and CAFO regulations. This agreement is not a joint venture with NAPI so no revenue is recognized from the agreement and all costs related to their operations will be paid directly to NAPI. The agreement expires on August 31, 2009.

(f) Fruit Picking Agreement – Honorio Perez

On October 26, 2007, NAPI entered into fruit picking permit and agreement with Mr. Honorio Perez to pick fruit on Navajo Nation trust lands administered by NAPI. NAPI agrees to provide any agronomic needs to the crops to ensure their maximum production (water, and in return, the contractor agrees to do as much pruning as possible prior to the beginning of the growing seasons. The contractor will pay NAPI \$5,000 for picking fruit under this agreement. This agreement expires on December 31, 2010.

(g) Five Star Oil and Gas

On April 19, 2006, NAPI entered into a facilities agreement with Five Star Oil and Gas for Lessees' rent of Farm-N-Go Convenience Store located near Highway 371 and N3003. Under this agreement, the Contractor shall use the premises only for the repair, maintenance and operation of a service station and related facilities. Contractor also has the option to add on a Laundromat,



**Navajo Agricultural Products Industry**  
Notes to Financial Statements  
For the Years Ended May 31, 2009 and 2008

food mart and feed store at later dates. In lieu of monetary rental payments, Contractor shall provide fuel to NAPI for NAPI's on-farm needs at the Contractor's posted retail prices minus three cents per gallon for a period of one year from the effective date of the agreement. At the end of the one year, both parties shall have the option to enter into a profit-sharing arrangement, mutually agreeable to both parties. This agreement expires April 18, 2010.

(h) J & M Baling, Inc.

On October 31, 2008, NAPI entered into an Operations and Rental Agreement with J&M Baling, Inc. Under this agreement, Contractor will custom swath, bale and field stack up to 225,000 bales of three-twine or big bales wheat straw. NAPI will provide up to six combines and two stripper headers, and Contractor will provide four strip headers in good working condition. This agreement expires on October 31, 2009, with an option that it will automatically extend through October 31, 2010, on mutually agreed terms.

**Note 12 - Facilities and Equipment Lease, and Product Sales and Application Agreement**

In an effort to reduce costs and improve crop yields, NAPI entered into a Facilities and Equipment Lease, and Product Sales and Application Agreement with the Wilbur-Ellis Company (Wilbur-Ellis). According to the terms of the agreement the Wilbur-Ellis will sell and apply various agricultural chemicals, fertilizers, seeds, and micronutrients to NAPI fields. During the years ended May 31, 2009 and 2008, NAPI paid \$12,773,058 and \$9,523,380 respectively to Wilbur-Ellis for their services.

In conjunction with this, NAPI leases Wilbur-Ellis certain facilities and equipment for storage and distribution of the chemicals and fertilizer utilized to treat NAPI's fields. During the years ended May 31, 2009 and 2008, NAPI received approximately \$71,900 and \$62,000, respectively, in base rental revenue for the facilities and equipment, under the terms of this agreement. Although this agreement expired during fiscal year 2007, an amendment was made, effective November 1, 2006, extending the term three years through October 31, 2010.

**Note 13 - Contingencies**

All federal and state program expenditures are subject to audit by the various grantors, which may result in disallowed program expenditures. Generally, such audits must commence within three years of the program's termination date. No provision for disallowed costs has been made in the accompanying financial statements, as the disallowed costs, if any, will be recorded in the period they are determined.

**Navajo Agricultural Products Industry**  
**Notes to Financial Statements**  
**For the Years Ended May 31, 2009 and 2008**

NAPI is party to various legal proceedings in the normal course of business. In management's opinion, after consultation with outside legal council, the disposition of these matters will not materially affect the financial position of the farm.

**Note 14 - Guarantee of Debt**

During fiscal year 2008, the Navajo Agricultural Marketing Inc., a wholly-owned corporation of NAPI, executed a \$1,000,000 revolving credit line and a \$1,000,000 standby letter of credit with Wells Fargo Bank, N.A. The following is a recap of significant terms of the two credit lines:

- Revolving credit line – principal associated with this credit line is due and payable fourteen months from the effective date of the loan. The interest rate shall equal 4.38%. Interest payments are due on a monthly basis. As of May 31, 2008, the revolving credit line balance was \$1,000,000.
- Standby letter of credit – principal associated with the letter of credit is due and payable as one payment, no later than September 30, 2008. The interest rate shall equal the Wells Fargo Bank Prime Rate minus .88% (floating). Interest payments are due on a monthly basis. As of May 31, 2008, the standby letter of credit balance was \$-0-.

These obligations are secured by funds held by NAPI in a money market mutual fund.

This guarantee of debt arrangement between NAPI and NAMI noted above was cancelled during fiscal year 2009 as a result of the establishment of the revolving line of credit discussed at Note 7.

**Note 15 - Prior Period Adjustment**

The net assets of the governmental activities at June 1, 2007 have been restated from amounts previously reported for the following item:

Net assets, June 1, 2007, as previously reported	\$ 57,791,417
1. Elimination of an inactive grant investment account established in fiscal year 2006.	(256,186)
2. To eliminate NAMI financial activity which was incorrectly blended with NAPI in the prior fiscal year.	1,146,485
Net assets, June 1, 2007, as restated	\$ 58,681,716

**Navajo Agricultural Products Industry**  
Notes to Financial Statements  
For the Years Ended May 31, 2009 and 2008

**Note 16 - Related Party Transactions**

In June 2005, the Navajo Agricultural Marketing, Inc. (a State of New Mexico corporation) was established for the following purposes:

1. To purchase agricultural products in local and regional markets and to market such products in various agricultural markets;
2. To trade or market agricultural products on the Chicago Board of Trade, Kansas City Board of Trade, and other commodities exchange markets.

The Navajo Agricultural Marketing, Inc. (NAMI) is wholly owned by the Navajo Agricultural Products Industry (NAPI). During fiscal year 2009, the Navajo Agricultural Products Industry transacted the following business transactions with the Navajo Agricultural Marketing, Inc.:

1. NAPI sold corn and wheat inventory to NAMI "on account" in the amount of \$10,073,823.
2. During fiscal year 2009, the Company repaid \$15,537,212 back to NAPI for corn and wheat inventory purchases, granary charges, and other miscellaneous items incurred during both fiscal years 2008 and 2009.
3. NAMI utilized NAPI's granary facilities to store its purchased corn and wheat inventory. NAPI charged NAMI \$645,449 for this storage service;
4. At May 31, 2009, NAPI has recognized an accounts receivable due from NAMI in the amount of \$6,374,579.

During fiscal year 2008, the Navajo Agricultural Products Industry transacted the following business transactions with the Navajo Agricultural Marketing, Inc.:

1. Short-term cash loans to NAMI in the amount of \$3,789,067, of which \$3,000,000 was repaid back to NAPI by year-end;
2. NAPI sold corn and wheat inventory to NAMI "on account" in the amount of \$9,479,744; of which \$1,078,743 was repaid back to NAPI by year-end;
3. NAMI utilized NAPI's granary facilities to store its purchased corn and wheat inventory. NAPI charged NAMI \$694,048 for this storage service;
4. NAPI paid for various costs totaling \$284,493 for consultants, legal, travel, utility and audit on behalf of NAMI. NAPI established a receivable from NAMI for these costs;
5. At May 31, 2008 NAPI has recognized an accounts receivable due from NAMI in the amount of \$11,076,437.

**Navajo Agricultural Products Industry**  
Notes to Financial Statements  
For the Years Ended May 31, 2009 and 2008

**Note 17 - Corn/Wheat Sales Contracts Commitments**

The Navajo Agricultural Products Industry entered into various corn/wheat sales contracts by year-end with the Navajo Agricultural Marketing, Inc. The provisions of these contracts stipulated that NAPI is required to deliver a specific number of bushels at a contracted price.

The following schedule provides a brief recap by fiscal year of these outstanding forward purchase contracts at May 31, 2009:

<u>Crop</u>	<u>Fiscal Year</u>	<u>Bushels</u>	<u>Average Price Per Bushel</u>	<u>Extended Amount</u>
Corn	2010	500,000	\$3.94815	\$1,974,075
Wheat	2010	150,000	7.2000	1,080,000
Corn	2011	500,000	3.9423	1,971,150

The following schedule provides a brief recap by fiscal year of these outstanding forward purchase contracts at May 31, 2008:

<u>Crop</u>	<u>Fiscal Year</u>	<u>Bushels</u>	<u>Average Price Per Bushel</u>	<u>Extended Amount</u>
Corn	2009	1,620,000	\$3.07	\$4,973,400
Wheat	2009	421,732	6.27	2,644,260
Corn	2010	750,000	3.86	2,895,000
Wheat	2010	150,000	7.45	1,117,500
Corn	2011	750,000	3.85	2,887,500

## Supplementary Information

Navajo Agricultural Products Industry  
Schedule of Expenditures of Federal Awards  
For the Year Ended May 31, 2009

Federal Grantor/Pass-Through Grantor/Program Title	CFDA Number	Pass-Through Grantor's Number	Expenditures
<b>U.S. Department of the Interior</b>			
Bureau of Indian Affairs			
Navajo Indian Irrigation Project	15.CTN00X10213	N/A	\$ 7,349,253
Bureau of Reclamation:			
Navajo Indian Irrigation Project	15.04-NA-40-2095	N/A	293,881
Cooperative Agreement for Minor Construction	15.05-NA-40-2290	N/A	3,584
E-40	15.9-07-40-R0860	N/A	23,665
Total U.S. Department of Interior			<u>7,670,383</u>
Total Expenditures of Federal Awards			<u>\$ 7,670,383</u>

See accompanying notes to schedule.

**Navajo Agricultural Products Industry**  
Notes to Schedule of Expenditures of Federal Awards  
For the Year Ended May 31, 2009

**Note 1 - Basis of Accounting**

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Navajo Agricultural Products Industry and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial statements.

**Note 2 - Catalog of Federal Domestic Assistance (CFDA) Numbers**

The program titles and CFDA numbers were obtained from the federal or pass-through grantor or the 2008 Catalog of Federal Domestic Assistance. When no CFDA number had been assigned to a program, the two-digit federal agency identifier, a period, and the federal contract number was used. When there was no federal contract number, the two-digit federal agency identifier, a period, and the word "unknown" was used.

**Note 3 – Subrecipients**

The Navajo Agricultural Products Industry did not provide federal awards to subrecipients during the year ended May 31, 2009.

## Reports on Compliance and Internal Control



**Independent Auditor's 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***

Honorable Chairman and Members of the Board of Directors  
Navajo Agricultural Products Industry  
Farmington, New Mexico

We have audited the financial statements of the Navajo Agricultural Products Industry (NAPI), an Enterprise of the Navajo Nation, as of and for the year ended May 31, 2009, and have issued our report thereon dated August 21, 2009, which was modified due to the financial statements presenting only NAPI's and not purported to, and not presenting fairly, the financial position of the Navajo Nation as of May 31, 2009, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered NAPI's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of NAPI's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of NAPI's internal control over financial reporting.

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

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of a control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of NAPI's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider items **09-1** through **09-3** as described in the accompanying schedule of findings and questioned costs, to be significant deficiencies in internal control over financial reporting.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item **09-1** to be a material weakness.

### **Compliance and Other Matters**

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

We noted certain matters that we reported to management of NAPI in a separate letter dated August 21, 2009.

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

*Mulla, Allen & Co PC*

August 21, 2009

**Independent Auditor's Report on Compliance With Requirements  
Applicable to Each Major Program and on Internal Control Over Compliance in  
Accordance With OMB Circular A-133**

Honorable Chairman and Members of the Board of Directors  
Navajo Agricultural Products Industry  
Farmington, New Mexico

**Compliance**

We have audited the compliance of the Navajo Agricultural Products Industry (NAPI), an Enterprise of the Navajo Nation, with the types of compliance requirements described in the Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended May 31, 2009. NAPI's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of NAPI's management. Our responsibility is to express an opinion on NAPI's compliance based on our audit.

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

As described in items **09-4** and **09-5** in the accompanying schedule of findings and questioned costs, NAPI did not comply with requirements regarding federal reporting that are applicable to the Navajo Indian Irrigation Project program. Compliance with such requirements is necessary, in our opinion, for the Navajo Agricultural Products Industry to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Navajo Agricultural Products Industry complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended May 31, 2009. The results of our auditing procedures also disclosed an instance of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133

and which are described in the accompanying schedule of findings and questioned costs as item **09-6**.

### **Internal Control Over Compliance**

The management of the Navajo Agricultural Products Industry is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered NAPI's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, 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 NAPI's internal control over compliance.

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

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item **09-7** to be a significant deficiency.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, we consider item **09-7** to be a material weakness.

NAPI's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit NAPI's responses and, accordingly, we express no opinion on it.

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

*Meth, Allen J. CPA*

August 21, 2009

**Navajo Agricultural Products Industry  
Schedule of Findings and Questioned Costs  
For the Year Ended May 31, 2009**

**Section I – Summary of Auditor’s Results**

***Financial Statements***

Type of auditor's report issued:

**Unqualified**

**YES                      NO**

Material weaknesses identified in internal control over financial reporting?

  X                        \_\_\_\_\_

Significant deficiencies identified not considered to be material weaknesses?

  X                        \_\_\_\_\_

Noncompliance material to the financial statements noted?

\_\_\_\_\_                        X  

***Federal Awards***

Material weaknesses identified in internal control over major programs?

  X                        \_\_\_\_\_

Significant deficiencies identified not considered to be material weaknesses?

\_\_\_\_\_                        X    
(None Reported)

Type of auditor's report issued on compliance for major programs:

**Qualified**

Any audit findings disclosed that are required to be reported in accordance with Circular A-133 (section .510[a])?

  X                        \_\_\_\_\_

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
15.CTN00X10213	Navajo Indian Irrigation Project
15.04-NA-40-2095	Navajo Indian Irrigation Project

Dollar threshold used to distinguish between Type A and Type B programs:

\$300,000

Auditee qualified as low-risk auditee?

\_\_\_\_\_                        X  

***Other Matters***

Auditee's Summary Schedule of Prior Audit Findings required to be reported in Accordance with Circular A-133 (section .315[b])?

  X                        \_\_\_\_\_

Navajo Agricultural Products Industry  
Schedule of Findings and Questioned Costs  
For the Year Ended May 31, 2009

**Section II - Financial Statement Findings**

**Item: 09-1 [Repeat Finding]**

*Criteria:* Individuals charged with governance, management and other personnel are responsible for designing and implementing the appropriate "internal controls" to provide reasonable assurance about the achievement of the entity's objectives with regards to the reliability of financial reporting.

*Condition:* Policies and procedures requiring the review of the entity's trial balance and/or general ledger on a monthly basis was not performed. In addition, the reconciliation of certain subsidiary ledgers and/or other accounting records to the general ledger was not performed. This resulted in the following misstatements not being identified until the annual audit:

1. To correct for fiscal year 2008 adjustments that were posted in 2009 incorrectly in the amount of \$2,220,538;
2. To state the current and noncurrent portion of the long-term debt in the amount of \$185,556;
3. The elimination of an erroneous client adjustment to accounts receivable related to Navajo Agricultural Marketing, Inc. (NAMI) in the amount of \$335,419;
4. Incorrect posting of a "sweep" account in the amount of \$182,583 as a account receivable;
5. An audit adjustment in the amount of \$361,182 was necessary to reconcile capital asset subsidiary schedules and the detail general ledger.
6. An audit adjustment in the amount of \$161,032 was necessary to reconcile beginning net assets to the prior fiscal year;
7. To record accounts payable in the amount of \$503,884;
8. To properly state deferred conservation costs in the amount \$160,852.
9. The book balance on a bank reconciliation did not agree to the trial balance. This error resulted in an understatement of cash in the amount of \$134,479.
10. Bank reconciliations were not performed during fiscal year 2009 for a NAPI bank account which was opened in February 2009 and had a wire transfer into this account in the amount of \$1,970,417 in April 2009. This error resulted in an understatement of cash in the amount of \$215 as of May 31, 2009.
11. The bank reconciliation for the contained stale dated checks greater than one year in the amount of \$13,573.
12. A reconciliation was not performed to agree the weight tickets to the bill of ladings given to drivers to verify the cash received. This resulted in a fraud of cash misappropriated from the scale house at 371 in the amount of \$35,340.

*Effect:* The entity's objective of achieving reliable financial reporting process has been limited.

*Cause:* Policies and procedures have not been developed and implemented requiring the monthly review of the entity's trial balance and the reconciliation to subsidiary ledgers and/or other accounting records is not being performed.

*Recommendation:* Policies and procedures should be developed and implemented requiring the monthly review of the entity's trial balance and the reconciliation to subsidiary ledgers and/or other account records.

**Navajo Agricultural Products Industry**  
**Schedule of Findings and Questioned Costs**  
**For the Year Ended May 31, 2009**

*Response:* Many of the policies and procedures were developed several years ago and have not been updated. A new position has been added for a Technical Writer. This position has been filled and the employee is helping to update all policies and procedures including checklists and methods to ensure compliance.

**Item: 09-2 [Repeat Finding]**

*Criteria:* The concentration of incompatible duties in a limited number of personnel should be evaluated by individuals charged with governance, management and other personnel on an on-going basis.

*Condition:* Checks are received and logged by the same individual who reconciles the accounts receivable subsidiary ledgers.

*Effect:* The concentration of incompatible duties in a limited number of personnel could create a control situation that would allow personnel to misappropriate assets.

*Cause:* The limited number of personnel in the accounting department created the situation of concentration of incompatible duties.

*Recommendation:* The Board, management and other personnel should be constantly mindful that the concentration of incompatible duties in a limited number of personnel could create control situations that would allow personnel to misappropriate assets. The Board and management should consider taking steps to separate incompatible duties.

*Response:* Steps have been taken to separate incompatible duties. We are now focusing on ensuring that those providing backup do not create incompatible duties.

**Item: 09-3**

*Criteria:* Individuals charged with management and other personnel are responsible for designing and implementing the appropriate internal controls over cash to provide reasonable assurance about the achievement of the entity's objectives with regards to the reliability of financial reporting.

*Condition:* Policies and procedures requiring a review of the cash bank reconciliations was not adequately performed during fiscal year 2009. This resulted in the following significant deficiencies in internal controls not being identified until the annual audit:

1. The responsible official that performs the second signature on the checks does not review the supporting documentation at the time of signature.
2. A review from a responsible official over bank reconciliations was not performed over the first 10 months of fiscal year 2009 until May 2009.

*Effect:* NAPI's objective of achieving reliable financial reporting process has been limited.

*Cause:* The monthly review of the NAPI's bank reconciliations is not being adequately performed.

**Navajo Agricultural Products Industry**  
**Schedule of Findings and Questioned Costs**  
**For the Year Ended May 31, 2009**

*Recommendations:* Procedures should be developed to ensure that NAPI's bank reconciliations are being adequately reviewed by a responsible official

*Response:* Several reconciliations were not done timely this past year. We will focus this year on ensuring that the reconciliations are done timely, including the review by a second employee. Furthermore, the accounts payable clerks have been instructed to include all backup with the checks and the employee that performs the second signature on all checks is now reviewing supporting documentation at the time of signing.



Navajo Agricultural Products Industry  
Schedule of Findings and Questioned Costs  
For the Year Ended May 31, 2009

**Section III - Federal Award Findings and Questioned Costs**

**Item: 09-4**

*CFDA Number:* 15.04-NA-40-2095

*Program:* Navajo Indian Irrigation Project

*Agency:* U.S. Department of the Interior – Bureau of Reclamation

*Award Year:* June 1, 2008 – May 31, 2009

*Award Number:* 04-NA-40-2095

*Criteria:* The Navajo Indian Irrigation Project (NIIP Grant) contract requires that annual SF-269 financial reports be prepared and submitted to the awarding agency within 90 days after the end of the reporting period and that the performance report be prepared and submitted to the awarding agency and to the NAPI Board of Directors within 90 days after the close of the contract funding period.

*Condition:* The annual SF-269 report was not submitted for fiscal year 2009.

*Cause:* Control procedures have not been developed and implemented to ensure that contract reporting requirements are met.

*Effect:* The program did not comply with contract requirements relating to the submission of annual financial report. The federal awarding agency might restrict funding, limit future award amounts, or impose additional conditions if contract stipulations are deemed to have been not met.

*Recommendation:* To comply with contract requirements, policies and procedures should be established to ensure all required reports are prepared and submitted in a timely manner.

**Item: 09-5**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Agency:* U.S. Department of the Interior – Bureau of Indian Affairs

*Award Year:* June 1, 2008 – May 31, 2009

*Award Number:* CTN00X10213

**Navajo Agricultural Products Industry**  
**Schedule of Findings and Questioned Costs**  
**For the Year Ended May 31, 2009**

*Criteria:* The Navajo Indian Irrigation Project (NIIP Grant) contract and OMB Circular A-87 require that financial reports of grant expenditures should be compiled using the general ledger as basis for the report.

*Condition:* The quarterly SF-269 reports for fiscal year 2009 were improperly compiled and do not agree to NAPI's general ledger.

*Cause:* Control procedures have not been effectively applied to ensure that contract reporting requirements are met and that the general ledger is used for reporting actual grant award expenditures.

*Effect:* The program did not comply with contract and OMB Circular A-87 requirements relating to the general ledger being used as the source for reporting grant award expenditures. The federal awarding agency may restrict funding, limit future award amounts, or impose additional conditions if contract stipulations are deemed to have been not met.

*Recommendation:* Controls should be followed by appropriate management to ensure that the required quarterly and annual financial reports are proper and are compiled using actual amounts from the general ledger.

**Item: 09-6**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Agency:* U.S. Department of the Interior – Bureau of Indian Affairs

*Award Year:* June 1, 2008 – May 31, 2009

*Award Number:* CTN00X10213

*Criteria:* To satisfy the requirements for recipients of federal awards, a physical inventory of capital assets should be performed and reconciled to the asset listing at least every two years.

*Condition:* NAPI performed a physical inventory of its capital assets, however, was unable to provide support of that inventory to the auditors.

*Cause:* Control procedures have not developed to ensure proper documentation of the physical inventory over capital assets be maintained.

*Effect:* Failure to periodically inventory capital assets increases the risk that assets could be misappropriated or errors in the accounting records could occur and not be detected.

**Navajo Agricultural Products Industry**  
**Schedule of Findings and Questioned Costs**  
**For the Year Ended May 31, 2009**

*Questioned Costs:* Not applicable

*Recommendation:* Policies and procedures should be implemented that include assigning responsibility of custody and recordkeeping of the assets to a responsible official.

**Item: 09-7** [Repeat Finding]

*CFDA Numbers:* 15.CTN00X10213, 15.04-NA-40-2095

*Program:* Navajo Indian Irrigation Project

*Agency:* U.S. Department of the Interior (Bureau of Indian Affairs, Bureau of Reclamation)

*Award Year:* June 1, 2008 – May 31, 2009

*Award Numbers:* CTN00X10213, 04-NA-40-2095

*Condition:* Policies and procedures requiring the review of the entity's trial balance and/or general ledger on a monthly basis was not performed. In addition, the reconciliation of certain subsidiary ledgers and/or other accounting records to the general ledger was not performed. See Section II – Financial Statement Findings, Item **09-1**.

*Questioned Costs:* Not Applicable

*Recommendation:* Policies and procedures should be developed and implemented requiring the monthly review of the entity's trial balance and the reconciliation to subsidiary ledgers and/or other account records.

## NAPI Responses

Navajo Agricultural Products Industry  
Corrective Action Plan  
Year Ended May 31, 2009

**Federal Award Findings and Questioned Costs**

**Item: 09-4**

*CFDA Number:* 15.04-NA-40-2095

*Program:* Navajo Indian Irrigation Project

*Name of Contact Person:* Mr. Russell M. Litke, Chief Financial Officer

*Anticipated Completion Date:* August 13, 2009

*Corrective Action:* The SF-269 for Contract No. 04-NA-40-2095 had never been filed in the past and it was not brought up until this audit. The contract does state that that the SF-269 shall be submitted annually. We have worked with BOR and filed a SF-269 from the inception of the contract through the end of calendar year 2008 (December 31, 2008). This will be submitted on an annual basis going forward. We have also employed a Technical Writer (through indirect costs) to help us update all policies and procedures including checklists and methods to ensure compliance.

**Item: 09-5**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Name of Contact Person:* Mr. Russell M. Litke, Chief Financial Officer

*Anticipated Completion Date:* April 30, 2010

*Corrective Action:* We began completing the SF-269 using the general ledger as backup after the last audit. Some adjustments were made after completing the SF-269 and an amended SF-269 was not filed, causing the out of balance situation for the year. We must verify YTD numbers each quarter and at year end. We have employed a Technical Writer (through indirect costs) to help us update all policies and procedures including checklists and methods to ensure compliance.

**Item: 09-6**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Name of Contact Person:* Russell M. Litke, Chief Financial Officer

*Anticipated Completion Date:* May 31, 2010

Navajo Agricultural Products Industry  
Corrective Action Plan  
Year Ended May 31, 2009

*Corrective Action:* Our O&M Department Manager is working with BIA to update/fully implement the MAXIMO system which will include assigning responsibility of this important process to a specific employee. We have also employed a Technical Writer (through indirect costs) to help us update all policies and procedures including checklists and methods to ensure compliance.

**Item: 09-7**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Name of Contact Person:* Mr. Russell M. Litke, Chief Financial Officer

*Anticipated Completion Date:* November 30, 2009

*Corrective Action:* Many of the policies and procedures were developed several years ago and have not been updated. A new position has been added for a Technical Writer. This position has been filled and the employee is helping to update all policies and procedures including checklists and methods to ensure compliance. Several reconciliations were not done timely this past year. We will focus this year on ensuring that the reconciliations are done timely, including the review by a second employee.

Navajo Agricultural Products Industry  
Summary Schedule of Prior Audit Findings  
Year Ended May 31, 2009

**Status of Prior Year Federal Award Findings and Questioned Costs**

**Finding Number: 06-01; 08-4**

*CFDA Number:* 15.CTN00X10212 and 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Status:* Corrected.

*Corrective Action:* Not required.

**Finding Number: 08-5**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Status:* Not Corrected.

*Corrective Action:* We began completing the SF-269 using the general ledger as backup after the last audit. Some adjustments were made after completing the SF-269 and an amended SF-269 was not filed, causing the out of balance situation for the year. We must verify YTD numbers each quarter and at year end. We have employed a Technical Writer (through indirect costs) to help us update all policies and procedures including checklists and methods to ensure compliance.

**Finding Number: 08-6**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Status:* Corrected.

*Corrective Action:* Not required.

**Finding Number: 08-7**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Status:* Not Corrected.

Navajo Agricultural Products Industry  
Summary Schedule of Prior Audit Findings  
Year Ended May 31, 2009

*Corrective Action:* Several reconciliations were not done timely this past year. We will focus this year on ensuring that the reconciliations are done timely, including the review by a second employee. We have employed a Technical Writer (through indirect costs) to help us update all policies and procedures including checklists and methods to ensure compliance.

**Finding Number: 08-8**

*CFDA Number:* 15.CTN00X10213

*Program:* Navajo Indian Irrigation Project

*Status:* Corrected.

*Corrective Action:* Not required.