Navajo Agricultural Products Industry
An Enterprise Fund of the Navajo Nation

Single Audit Reporting Package
May 31, 2008

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MILLER, ALLEN & CO., P.C.
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(1931 - 1992)

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 fund of the Navajo Nation, as of and for the year ended May 31, 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, 2008 and the changes in its financial position, or, where applicable, its cash flows for the year 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, 2008, and the changes in its financial position and its cash flows for the year 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 November 16, 2008, 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

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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 basic 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 basic financial statements taken as a whole.

Miller, Allen & Co PC

November 16, 2008

NAVAJO PRIDE

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

November 16, 2008

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 year ended May 31, 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 2008. The assets of NAPI exceeded its liabilities at the close of the fiscal year by $64,396,366. Included in this amount is $32,102,418, which may be used to meet NAPI's ongoing mission of operating a profitable commercial farm.
- NAPI's total net assets increased by $5,714,650.
- At May 31, 2008, total NAPI assets were $79,661,065, compared to $72,245,191 at May 31, 2007. NAPI's most significant current asset is crops in progress of $15,859,569 at May 31, 2008, compared to $11,073,432 at May 31, 2007.
- At May 31, 2008, NAPI's current assets of $31,870,797 were sufficient to cover current liabilities of $10,909,069 (current ratio of 2.92). At May 31, 2007, NAPI's current assets of $28,084,527 exceeded current liabilities of $11,078,527 (current ratio of 2.54).
- NAPI's liabilities totaled $15,264,699 at May 31, 2008 compared to $13,563,475 at May 31, 2007. A $2,593,768 long-term note payable to Key Equipment Finance represents the largest liability as of May 31, 2008.
- The Navajo Agricultural Products Industry total debt increased by $1,766,975 (39%).
- NAPI's gross crop revenues were $35,574,862 and $35,787,697 for the years ended May 31, 2008 and 2007, respectively. This represented a decrease in crop revenue of $212,835 from the previous fiscal year. Crop revenues were relatively flat as a result of economic uncertainty both nationally and globally, affecting market prices and costs related to crop production.

- Funding for the Navajo Indian Irrigation Project and other related grants was $6,318,052 and $6,654,420 for the years ended May 31, 2008 and 2007, respectively. This represented a decrease in intergovernmental revenue of $336,368 or 5% from the previous fiscal year. Governmental appropriations continue to be cut as a result of federal government's obligations both locally and internationally.
- Income from agricultural-related leases was $1,781,521 and $2,331,105 for the years ended May 31, 2008 and 2007, respectively. This represented a decrease of $549,584 or 24% from the previous fiscal year. This decrease was a result of reduced production on several of the leases and a corresponding decrease in revenue sharing.
- Selling and administrative expenses were $3,892,127 and $3,062,946 for the years ended May 31, 2008 and 2007, respectively. This represented an increase of $829,181 or 27% from the previous fiscal year. The increase represents changes of administrative staff and procedures, especially in the areas of finance and accounting.
- Interest and fiscal charges were $383,822 and $202,813 for the years ended May 31, 2008 and 2007, respectively. This represented an increase of $181,009 or 89% from the previous fiscal year due to the increase of notes payable for the purpose of acquisition and construction of capital assets.

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, 2008 and 2007. 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, 2008 and 2007. 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.

The Statement of Cash Flows presents the inflows and outflows of cash and cash equivalents for the years ended May 31, 2008 and 2007. 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 Statement of Net Assets
As of May 31, 2008 and 2007

	May 31, 2008	May 31, 2007
Assets:		
Current assets	$ 31,870,797	$ 28,084,527
Noncurrent assets, other than capital assets	9,195,157	6,843,939
Capital assets, net	38,595,111	37,316,725
Total assets	$ 79,661,065	$ 72,245,191
Liabilities:		
Current liabilities	$ 10,909,069	$ 11,078,527
Noncurrent liabilities	4,355,630	2,484,948
Total liabilities	$ 15,264,699	$ 13,563,475
Net assets:		
Invested in capital assets, net of related debt	$ 32,293,948	$ 32,814,820
Unrestricted net assets	32,102,418	25,866,896
Total net assets	$ 64,396,366	$ 58,681,716

At May 31, 2008, total NAPI assets were $79,661,065, compared to $72,245,191 at May 31, 2007. NAPI's most significant current asset is crops in progress of $15,859,569 at May 31, 2008, compared to $11,073,432 at May 31, 2007.

At May 31, 2008, NAPI's current assets of $31,870,797 were sufficient to cover current liabilities of $10,909,069 (current ratio of 2.92). At May 31, 2007, NAPI's current assets of $28,084,527 exceeded current liabilities of $11,078,527 (current ratio of 2.54).

NAPI's liabilities totaled $15,264,699 at May 31, 2008 compared to $13,563,475 at May 31, 2007. A $2,593,768 long-term note payable to Key Equipment Finance represents the largest liability as of May 31, 2008.

The Navajo Agricultural Products Industry total debt increased by $1,766,975 (39%).

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 $64,396,366 at the close of the most recent fiscal year.

By far the largest portion of the Navajo Agricultural Products Industry's net assets (50%) 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.

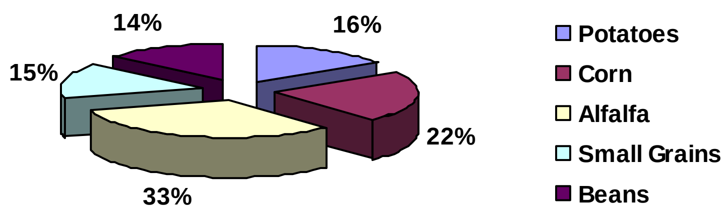
Condensed Statement of Revenues, Expenses, and Changes in Net Assets
For the Years Ended May 31, 2008 and 2007

	May 31, 2008	May 31, 2007
Revenues:		
Operating:		
Crops	$ 35,574,862	$ 35,787,697
Agricultural-related leases	1,781,521	2,331,105
Sale of electric power rights	955,762	
Indirect cost recovery	249,253	262,300
Nonoperating:		
Intergovernmental	6,318,052	6,654,420
Investment income	479,658	47,827
Other	279,141	914,138
Gain on sale of capital assets	38,667	7,872
Total revenues	45,676,916	46,005,359

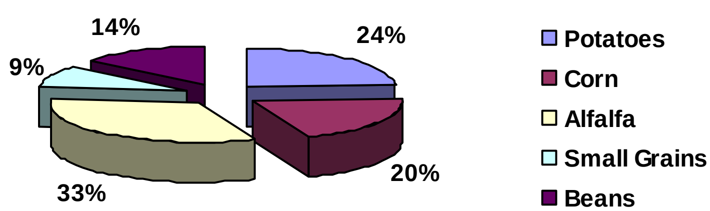
Condensed Statement of Revenues, Expenses, and Changes in Net Assets
For the Years Ended May 31, 2008 and 2007

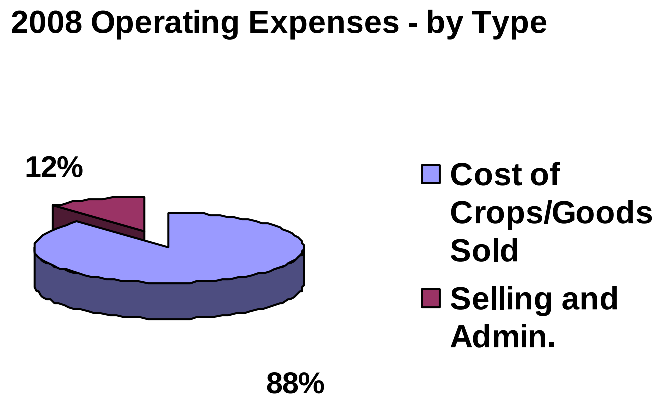
	May 31, 2008	May 31, 2007
Expenses:		
Operating:		
Cost of crops and goods sold:		
Crops	28,868,265	31,592,132
Selling and administrative	3,892,127	3,062,946
Nonoperating:		
Costs associated with the Navajo Indian Irrigation Project and other related grants	6,318,052	5,801,677
Interest and fiscal charges	383,822	202,813
Total expenses	39,462,266	40,659,568
Income before contributions and transfers	6,214,650	5,345,791
Transfers to the Navajo Nation – Scholarship Fund	(500,000)	
Change in net assets	5,714,650	5,345,791
Net assets, beginning, as restated	58,681,716	53,335,925
Net assets, ending	$ 64,396,366	$ 58,681,716

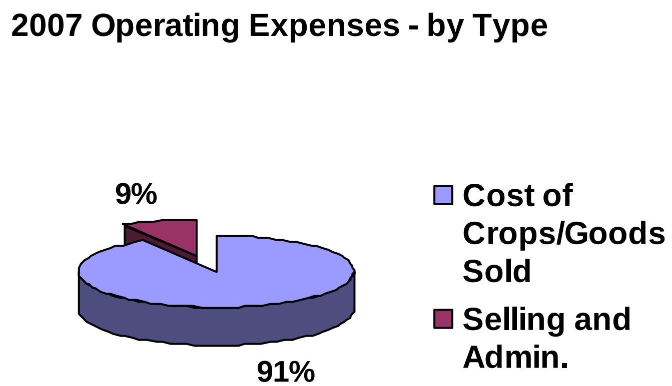
2008 Sigificant Crop Revenue - by Crop



2007 Significant Crop Revenue - by Crop







NAPI's gross crop revenues were $35,574,862 and $35,787,697 for the years ended May 31, 2008 and 2007, respectively. This represented an increase in crop revenue of $212,835 from the previous fiscal year. Crop revenues were relatively flat as a result of economic uncertainty both nationally and globally, affecting market prices and costs related to crop production.

Funding for the Navajo Indian Irrigation Project and other related grants was $6,318,052 and $6,654,420 for the years ended May 31, 2008 and 2007, respectively. This represented a decrease in intergovernmental revenue of $336,368 or 5% from the previous fiscal year. Governmental appropriations continue to be cut as a result of federal government's obligations to the Iraq war and natural disaster recovery continuance.

Income from agricultural-related leases was $1,781,521 and $2,331,105 for the years ended May 31, 2008 and 2007, respectively. This represented a decrease of $549,584 or 24% from the previous fiscal year. This decrease was a result of reduced production on several of the leases and a corresponding decrease in revenue sharing.

Selling and administrative expenses were $3,892,127 and $3,062,946 for the years ended May 31, 2008 and 2007, respectively. This represented an increase of $829,181 or 27% from the previous fiscal year. The increase represents changes of administrative staff and procedures, especially in the areas of finance and accounting.

Interest and fiscal charges were $383,822 and $202,813 for the years ended May 31, 2008 and 2007, respectively. This represented an increase of $181,009 or 89% from the previous fiscal year due to the increase of notes payable for the purpose of acquisition and construction of capital assets.

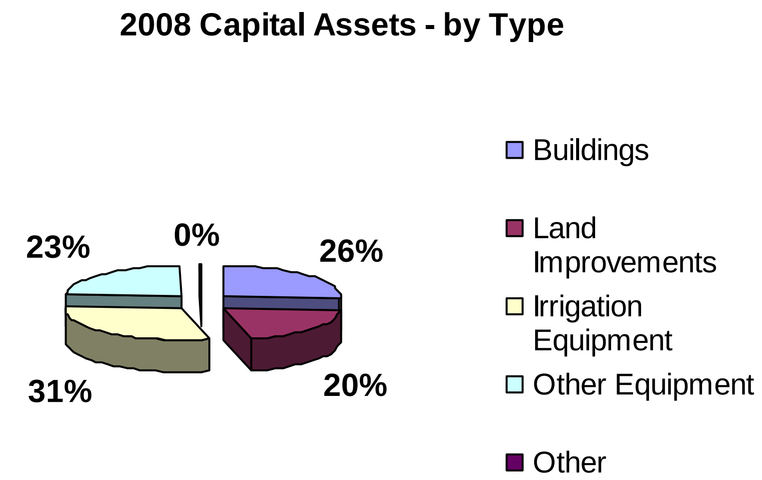
Capital Assets and Debt Administration:

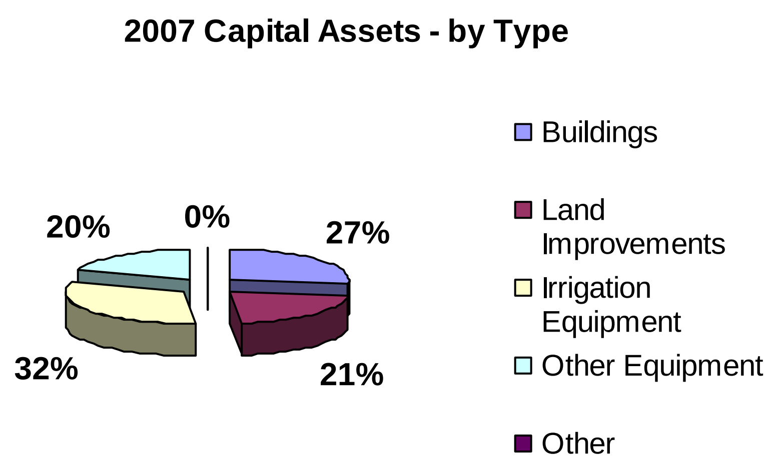
Capital assets – The Navajo Agricultural Products Industry's investment in capital assets (net of accumulated depreciation) as of May 31, 2008 and 2007 amounts to $38,595,111 and $37,315,725, respectively. This investment in capital assets includes land improvements, buildings, irrigation and sprinkler 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 3%.

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

- Fresh Pack Facility & Equipment = $2,859,459;
- Radio Communication Project = $780,791;
- Silo Monitor System = $243,158;
- Farm Equipment/Machinery = $1,121,975.

The following chart depicts the distribution of NAPI's capital assets – by type at May 31, 2008 and 2007, respectively.





Additional information on the Navajo Agricultural Products Industry's capital assets can be found in Note 6 to the financial statements on page 27.

Long-term debt – As of May 31, 2008 and 2007, NAPI had total long-term debt of $6,301,163 and $4,534,188, respectively. This long-term debt comprised of four bank note payables and equipment purchase agreements. To finance the purchase of farm equipment, NAPI secured new capital lease debt of $1,362,566 for the year ended May 31, 2008 and $1,759,169 for the year ended May 31, 2007. During the years ended May 31, 2008 and 2007, NAPI repaid long-term debt in the amounts of $2,455,310 and $2,772,952, respectively.

Navajo Agricultural Products Industry's Outstanding Debt

	2008	2007
Capital leases	$ 2,428,291	$ 1,735,445
Notes payable	3,872,872	2,798,743
Total	$ 6,301,163	$ 4,534,188

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 $6,318,052 for the year ended May 31, 2008 and $6,654,420 for the year ended May 31, 2007. Recognized expenditures of such funds were $6,318,052 and $5,801,677 for the year ended May 31, 2008 and for the year ended May 31, 2007, respectively.

Economic Outlook and Agricultural Outlook:

Economic Outlook –

- GDP (Gross Domestic Product) was projected to increase to 2.1 percent after inflation in 2007 and by 2.9 percent in 2008; however, with the substantial slowing in 2007, GDP growth is currently projected 2.8 percent or lower for 2008.
- Unemployment is projected to remain near its current 4.9 percent through 2008; however, with the certain indicators predicting some uncertainty of the US economy, this could change significantly.
- CPI (Consumer Price Index) is projected to decline from 2.8 percent for 2007 to 2.3 percent for 2008.
- Real GDP growth among the United States' major trading partners is forecast to remain above 4 percent which is significantly higher than growth in the United States. Average growth during the 2007-2008 is expected to be about 5 percent for the Asian Pacific countries, about 4.5 percent for Latin America, and about 2.5 percent for Western Europe and Canada.

- The expectation exists for the federal funds rate to decrease by 50 basis points by the fall of 2007 and by a total of 100 basis points by the spring of 2008.
- The interest rate on 3-month Treasury bills is expected to rise and average 4.84 percent through 2008; however, this could change significantly based on the status of the US economy in 2008.
- The interest rate on 10-year Treasury notes is projected to rise to 5 percent in 2008.
- Crude oil prices in 2008 are expected to rise approximately 7 percent from 2007.
- Gasoline and diesel prices will be up 7 to 8 percent, respectively.
- Farm fertilizer prices are projected to increase significantly by 30 percent in 2008 as a result of the increase in the price of natural gas.

Agricultural Outlook –

- Exports:
  - Compared to an earlier forecast in May 2007, the economic environment is now perceived as more favorable to US farm exports as the rest of the world's growth is stronger and the US dollar is a little weaker in several major markets.
  - Grains are forecast at a record $23 billion in fiscal 2008, up $400 million from the revised 2007 estimate. While feed exports are expected to be at a record $15.3 billion, up $500 million from the revised 2007 estimate.
  - Larger export volumes drive the total value increase for all grains, but higher unit values for wheat and coarse grains due to tight global supplies are also a factor.
  - The projected 2007 US corn crop production increase of 24% supports both the expansion of exports and domestic ethanol production. Driven by demand, farmers are anticipating increases their total corn acreage for 2008.
  - Fiscal 2008 wheat exports increase to an approximate $1.3 billion from the 2007 estimate due to stronger global demand, esp. North Africa and higher unit values. Tight global stocks sustain prices above 2007 levels, although stronger competition from key suppliers such as Australia and Russia may constrain US export growth for lower-protein wheat.
  - Total US potato exports are expected to increase in value to a record high of over $1.1 billion in 2008. The projected price of potatoes is expected to increase 18 percent from 2007 to 2008.

- Imports:
  - The revised import forecast for 2008 is $79 billion, 11 percent ($8.4 billion) more than 2007.
  - The result of domestic economic conditions and the dollar's exchange rate could slow the import growth in 2008 with higher US interest rates, weaker domestic economic activity, higher prices, as well as the weak dollar combine.
  - Initial import projections for 2008 show significant gains for grains and feed which are predicted to increase $600 million or more over 2007.
  - US imports of bulk grains are up nearly 60 percent in value through the first three quarters of fiscal 2007, particularly for wheat, which rose by 120 percent over the

2006 level. All other grains, feeds, and grain product groups jumped by double-digit rates based on value. These imports are spurred by higher domestic prices and reduced domestic supply as more farm acreage in planted to corn. Only import prices of feeds and fodders have decreased.

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 decreased over previous levels for 2008 and 2007. 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
Statement of Net Assets
May 31, 2008

	2008
Assets	
Current assets:	
Cash and cash equivalents	$ 2,552,631
Investments	2,974,937
Accounts receivable - trade (net of allowance for uncollectibles)	1,095,292
Accounts receivable - Navajo Agricultural Marketing, Inc.	8,600,000
Inventories	16,533,795
Prepaid items	114,142
Total current assets	31,870,797
Noncurrent assets:	
Accounts receivable - Navajo Agricultural Marketing, Inc.	2,476,437
Temporarily restricted:	
Cash and cash equivalents	4,044,255
Investments	51,566
Deferred alfalfa stand costs	2,404,247
Deferred conservation program costs	200,991
Other assets	17,661
Capital assets, net	38,595,111
Total noncurrent assets	47,790,268
Total assets	$ 79,661,065
Liabilities	
Current liabilities:	
Accounts payable	$ 2,400,059
Other accrued expenses	579,641
Deferred revenues	5,983,836
Current portion of long-term debt	1,945,533
Total current liabilities	10,909,069
Noncurrent liabilities:	
Noncurrent portion of long-term debt	4,355,630
Total noncurrent liabilities	4,355,630
Total liabilities	15,264,699
Net Assets	
Investment in capital assets, net of related debt	32,293,948
Unrestricted	32,102,418
Total net assets	$ 64,396,366

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

Navajo Agricultural Products Industry
Statement of Revenues, Expenses, and Changes in Net Assets
For the Year Ended May 31, 2008

	2008
Operating revenues:	
Crops	$ 35,574,862
Agricultural-related leases	1,781,521
Sale of electric power rights	955,762
Indirect cost recovery	249,253
Total operating revenues	38,561,398
Operating expenses:	
Cost of crops and goods sold:	
Crops	28,167,808
Agricultural-related leases	669,983
Feedyard	11,890
Convenience store operation	18,584
Total cost of crops and goods sold	28,868,265
Selling and administrative	3,892,127
Total operating expenses	32,760,392
Operating income	5,801,006
Nonoperating revenues (expenses):	
Intergovernmental revenues	6,318,052
Costs associated with the Navajo Indian Irrigation Project and other related grants	(6,318,052)
Investment income	479,658
Interest and fiscal charges	(383,822)
Gain on sale of capital assets	38,667
Other	279,141
Total nonoperating revenues (expenses)	413,644
Income before contributions and transfers	6,214,650
Transfer out to Navajo Nation Scholarship Fund	(500,000)
Change in net assets	5,714,650
Net assets, beginning, as restated	58,681,716
Net assets, ending	$ 64,396,366

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

Navajo Agricultural Products Industry
Statement of Cash Flows
For the Year Ended May 31, 2008

	2008
Cash flows from operating activities:	
Receipts from customers	$ 38,698,586
Payments to suppliers	(26,332,951)
Payments to employees	(6,598,927)
Net cash provided by operating activities	5,766,708
Cash flows from noncapital financing activities:	
Net increase in accounts receivable (Navajo Agricultural Marketing, Inc.)	(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 used by noncapital financing activities	(11,122,523)
Cash flows from capital and related financing activities:	
Subsidy from federal grants	5,895,272
Disbursements of federal grants	(6,207,821)
Acquisition and construction of capital assets	(291,459)
Proceeds from sale of capital assets	38,667
Principal paid on notes and capital leases	(2,455,310)
Interest paid on notes and capital leases	(383,822)
Other receipts	111,987
Net cash used by capital and related financing activities	(3,292,486)
Cash flows from investing activities:	
Interest and dividends	479,658
Net proceeds from investment maturities	2,195,679
Net cash provided by investing activities	2,675,337
Net decrease in cash and cash equivalents	(5,972,964)
Cash and cash equivalents, beginning	12,569,850
Cash and cash equivalents, ending	$ 6,596,886
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	$ 5,801,006
Adjustments to reconcile operating income to net cash provided by operating activities	
Depreciation	3,151,446
Change in assets and liabilities:	
(Increase) decrease in accounts receivable - trade	448,511
(Increase) decrease in inventories	(2,806,392)
(Increase) decrease in prepaid items	(51,392)
(Increase) decrease in deferred alfalfa stand costs	(725,126)
(Increase) decrease in deferred conservation program costs	14,406
Increase (decrease) in accounts payable	154,018
Increase (decrease) in other accrued expenses	91,554
Increase (decrease) in deferred revenue	(311,323)
Net cash provided by operating activities	$ 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 the year ended May 31, 2008 that affect recognized assets or liabilities but do not result in cash receipt or payments:

1.) Capital assets valued at $4,222,284 were acquired through capital leases and notes payable.
2.) Capital assets valued at $44,245 were acquired via trade-in of existing assets.

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

Note 1 - Nature of Operations

Navajo Agricultural Products Industry (NAPI), an enterprise fund 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, 2008, 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, approximately 11,500 acres have been placed into service. During the next crop year, 1,000 acres in Block VIII will be placed into service. At May 31, 2008, 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, 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, 2008 are as follow:

	2008
Alfalfa	33%
Corn	22%
Potatoes	16%
Small grains	15%
Beans	14%

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.

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 enterprise funds 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 fund 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 fund 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.

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

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.

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 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 Statement No. 33. Also, as an enterprise fund 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.

Note 3 - Deposits and Investments

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

	2008
Cash on hand	$ 900
Cash in bank	392
Cash equivalents – money market mutual funds	6,595,594
Total	$ 6,596,886

Deposits – 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, 2008 were as follows:

Investment Type	2008
Repurchase agreement	$ 3,026,503
Total	$ 3,026,503

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.

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

Investment Type	Rating	Rating Agency	Amount
Money market mutual funds	AAA	Standard & Poor's	$ 6,595,594
Repurchase agreements	AAA	Standard & Poor's	3,026,503
		Total	$ 9,622,097

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.

During fiscal year 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, accounts receivable - trade were as follows:

	2008
Receivables:	
Crops	$ 615,610
Other	537,991
Gross receivables	1,153,601
Less allowance for uncollectibles	(58,309)
Net total receivables	$ 1,095,292

In addition, at May 31, 2008, NAPI recognized an accounts receivable in the amount of $11,076,437 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 $8,600,000 of the $11,076,437 as a "current receivable" due to payments received by NAPI from NAMI through December 2008.

Note 5 - Inventories

At May 31, inventories were as follows:

	2008
Crops in progress	$ 15,859,569
Repair parts and supplies	623,630
Fresh Pak supplies	50,596
	$ 16,533,795

Note 6 - Capital Assets

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)
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

NAPI utilizes 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 in 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 May 31, 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. Management is currently in the process of negotiating an operating line of credit with a respectable financial institution.

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 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, 2008
Asset:	
Farm, feedlot, shop, and other equipment	$ 2,970,011
Less: accumulated depreciation	(1,155,127)
Total	$ 1,814,884

The future minimum lease obligations and the net present value of these minimum lease payments as of May 31, 2008.

Year ending May 31,	
2009	$ 834,632
2010	736,396
2011	647,469
2012	317,158
2013	185,008
Total minimum lease payments	2,720,663
Less: amount representing interest	(292,372)
Present value of minimum lease payments	$ 2,428,291

Note Payable

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

	2008
Key Equipment Finance note payable, payable in monthly installments of $48,017, including interest of 6.46%, due September 2013.	$ 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.	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

Total notes payable	3,872,872
Less: current portion of the notes payable	(1,241,829)
Noncurrent portion of the notes payable	$ 2,631,043

Annual debt service requirements to maturity for the note payable are as follows:

	Principal	Interest	Total
Year ending May 31,			
2009	$ 1,241,829	$ 206,458	$ 1,448,287
2010	907,226	139,006	1,046,232
2011	478,861	97,345	576,206
2012	510,728	65,478	576,206
2013	734,228	34,048	768,276
Total	$ 3,872,872	$ 542,335	$ 4,415,207

Changes in long-term liabilities

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	$ 669,721	$ 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	$ 2,455,310	$ 6,301,163	$ 1,945,533

Note 9 - Deferred Revenue

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
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
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, 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 March 5, 2008. 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, and a portion of the revenue generated from the sale of pumpkins, including a guaranteed minimum. During the year ended May 31, 2008 NAPI recorded revenues of approximately $179,575 under this agreement. Such revenue is included in agricultural-related lease 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 year ended May 31, 2008 NAPI recorded revenues of approximately $108,759, under this agreement. Such revenue is included in agricultural-related lease 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 2,600 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. NAPI receives rental payments for irrigated croplands and potato storage facilities in the amount of $400 per acre per annum or $1,040,000 per year for the first five years. 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 year ended May 31, 2008, NAPI recorded revenues of approximately $1,101,999 under this agreement. Such revenue is included in agricultural-related lease revenue in the accompanying financial statements. The agreement expires on August 31, 2011.

(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 year ended May 31, 2008 revenue of approximately $62,000 was recognized under this agreement. The agreement expires on October 31, 2010.

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

On September 3, 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 an agricultural lease 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 a 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, 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) 4-Corners Hay Harvesters

On December 8, 2003, NAPI entered into a Custom Swathing Alfalfa Agreement with 4-Corners Hay Harvesters. Under this agreement, Contractor agrees to swath NAPI's anticipated crop of alfalfa of approximately 12,000 acres, agrees to supply all equipment, personnel, fuel, supplies and materials necessary. NAP1 agrees to grow and have swathed by Contractor approximately 12,000 acres of crop located on NAPI lands and will compensate the Contractor at $13.75/acre of swathed alfalfa. This agreement expires on October 31, 2008.

(i) J & M Bailing, Inc.

On February 9, 2004, 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 3, 2008.

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 year ended May 31, 2008, NAPI paid $9,523,380 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 year ended May 31, 2008, NAPI received $62,000 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.

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

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.

Note 15 - Prior Period Adjustment

The net assets of the governmental activities at October 1, 2005 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

Note 16 - Subsequent Event

NAPI has entered into agreements with construction contractors for the Block 2 Pivot Redevelopment Project. The project consists of replacing 44 pivots, pads, wiring, radios, mainlines, engineering, etc. The project is estimated to cost approximately $7.3 million and the anticipated completion date is March 2009.

Note 17 - 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 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.

Note 18 - 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 of these outstanding sales contracts:

Crop	Delivery Date	Bushels	Contract Price Per Bushel
Corn	12/31/08	200,000	$ 2.6350
Corn	12/31/08	15,000	2.9000
Corn	12/31/08	85,000	2.9100
Corn	12/31/08	175,000	3.7500
Corn	12/31/08	25,000	3.7525
Corn	12/31/08	120,000	4.1375
Corn	12/31/08	500,000	2.4125
Corn	12/31/08	250,000	2.4650
Corn	12/31/08	250,000	2.6375
Corn	12/31/09	120,000	3.8050
Corn	12/31/09	130,000	3.8075
Corn	12/31/09	250,000	4.0900
Corn	12/31/09	250,000	3.7500
Corn	12/31/10	200,000	3.8125
Corn	12/31/10	15,000	3.8175
Corn	12/31/10	10,000	3.8200
Corn	12/31/10	25,000	3.8275
Corn	12/31/10	250,000	4.0700
Corn	12/31/10	250,000	3.7500
Wheat	6/30/08	104	7.8500
Wheat	6/30/08	5,228	7.5500
Wheat	6/30/08	8,108	8.1500
Wheat	6/30/08	8,694	7.2800
Wheat	6/30/08	4,554	3.1700
Wheat	6/30/08	16,410	4.2700
Wheat	6/30/08	27,776	4.3300
Wheat	7/31/08	16,667	7.5500
Wheat	7/31/08	16,667	7.5500
Wheat	7/31/08	857	6.5500
Wheat	7/31/08	100,000	4.6400
Wheat	7/31/08	65,000	4.7500
Wheat	7/31/08	35,000	4.7500
Wheat	7/31/08	50,000	7.9200
Wheat	7/31/08	50,000	7.9600
Wheat	9/30/08	16,667	6.0500
Wheat	7/31/09	150,000	7.4500

Supplementary Information

Navajo Agricultural Products Industry
Schedule of Expenditures of Federal Awards
For the Year Ended May 31, 2008

Federal Grantor/Pass-Through Grantor/Program Title	CFDA Number	Pass-Through Grantor's Number	Expenditures
U.S. Department of the Interior			
Bureau of Indian Affairs			
Navajo Indian Irrigation Project	15.CTN00X10213	N/A	$ 5,903,290
Bureau of Reclamation:			
Navajo Indian Irrigation Project	15.04-NA-40-2095	N/A	319,191
Cooperative Agreement for Minor Construction	15.05-NA-40-2290	N/A	14,254
E-40	15.9-07-40-R0860	N/A	81,317
Total U.S. Department of Interior			6,318,052
Total Expenditures of Federal Awards			$ 6,318,052

See accompanying notes to schedule.

Navajo Agricultural Products Industry
Notes to Schedule of Expenditures of Federal Awards
For the Year Ended May 31, 2008

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, 2008.

Reports on Compliance and Internal Control

MILLER, ALLEN & CO., P.C.
CERTIFIED PUBLIC ACCOUNTANTS

Mark L. Landy, CPA
Stephen T. Harris, CPA
Thomas L. Friend, CPA
Robert N. Snyder, CPA

Robert L. Miller, CPA
(1931 - 1992)

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 fund of the Navajo Nation, as of and for the year ended May 31, 2008, and have issued our report thereon dated November 16, 2008. 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 NAPI'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 misstatement of NAPI's financial statements that is more than inconsequential will not be prevented or detected by NAPI's internal control. We consider items **08-1** through **08-3** as described in the accompanying schedule of findings and questioned costs, to be significant deficiencies in internal control over financial reporting.

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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 NAPI'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 **08-1** to be a material weakness.

We noted certain matters that we reported to management of NAPI in a separate letter dated November 16, 2008.

NAPI's responses to the findings identified in our audit on pages 45 through 47. We did not audit the NAPI's responses and, accordingly, we express no opinion on them.

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.*

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.

Moss, Adams & Co PC

November 16, 2008

MILLER, ALLEN & CO., P.C.
CERTIFIED PUBLIC ACCOUNTANTS

Mark L. Landy, CPA
Stephen T. Harris, CPA
Thomas L. Friend, CPA
Robert N. Snyder, CPA

Robert L. Miller, CPA
(1931 - 1992)

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 fund of the Navajo Nation, with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended May 31, 2008. 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 **08-4** and **08-5** 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, 2008. The results of our auditing procedures also disclosed another instance of noncompliance

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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 **08-6**.

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 the 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 the 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 NAPI's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies and another that we consider to be a material weakness.

A *control deficiency* is 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 deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items **08-7** through **08-8** to be significant deficiencies.

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 **08-7** to be a material weakness.

NAPI's response to the findings identified in our audit are presented on pages 53 through 54. We did not audit NAPI's response 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.

Moss, Adams & Co PC

November 16, 2008

Navajo Agricultural Products Industry

Schedule of Findings and Questioned Costs
For the Year Ended May 31, 2008

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	
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:

CFDA Number	Name of Federal Program or Cluster
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	

Section II - Financial Statement Findings

Item: 08-1

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. Voided checks not being reinstated to cash in the amount of $171,164;
2. Incorrect posting of a reimbursement of overpayment of payroll taxes to accounts receivable rather than to the appropriate payroll tax expense account in the amount of $19,998;
3. The elimination of an erroneous payable due to the Navajo Nation in the amount of $126,113. NAPI received $126,113 from the Navajo Nation in fiscal year 2006 which was for the reimbursement for "overpaid" taxes to NAPI vendors. These amounts were then incorrectly recorded as a liability due to the Nation;
4. Incorrect posting of a "sweep" account in the amount of $51,566 as a account receivable;
5. Fiscal year 2007 receivable associated with "agricultural leases" was not reversed in the subsequent fiscal year in the amount of $270,553;
6. The incorrect establishment of the beginning balances for the "E-40 Trust Account" and "BOR Minor Const Trust Acct" cash accounts as interest income rather than the actual asset accounts in the amount of $161,114;
7. Intercompany transactions in the amount $134,479 were incorrectly recorded which resulted in the overstatement of accounts receivable;
8. Receipts received under the agreement NAPI and the Navajo Tribal Utility Authority in the amount of $955,762 was reclassified from "other income" to a more specific revenue classification such as "sale of electric power" rights;
9. An audit adjustment in the amount of $3,909,181 was necessary to reconcile beginning net assets to the prior fiscal year;
10. To record accounts payable in the amount of $224,063;
11. To reverse FY 2007 accrued wages in the amount $95,447.

Subsequent to the auditor being furnished the 2008 trial balance numerous "post closing" adjustments were submitted by accounting personnel. The following is a brief recap of such post closing adjustments:

1. To reclassify farm equipment and building capital assets in the amount of $84,844;
2. To record the disposal of farm vehicle and the related accumulated depreciation in the amount of $26,880;
3. To write down parts and irrigation parts inventory in the amount of $334,936;
4. To establish a receivable from NAMI in the amount of $694,048 for granary storage cost;

5. To adjust the deferred stand – alfalfa in the amount $1,327,007;
6. To record construction in progress in the amount of $37,765;
7. Incorrect posting of a "equipment lease" payment to accounts receivable rather than the appropriate expense account in the amount of $42,311;
8. The elimination of the purchase order clearing account in the amount of $450,550.

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.

Response: Due to restructuring of the accounting department the focus was to get financial statements current. Statements are now current and the department is now focusing on tightening up internal policies and procedures. Policies and procedures are currently being developed (in writing) and we are working on implementing further procedures to aid in the accurate and timely reporting of financial information. A checklist has been developed to aid in the completion of all required entries each month and is being implemented to further ensure that all entries are properly reviewed and approved. Another checklist is being developed to track the monthly reconciliations of all balance sheet accounts and to verify that they are properly documented and approved with any necessary adjustments being made timely - the month following the reconciliation. Furthermore, all journal entries and reconciliations will be filed in a central location instead of by the employee that performed the function.

Item: 08-2

Criteria: The concentration of incompatible duties in a limited number of personnel should 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: Through the restructuring of the accounting department, the department was short handed for several months. Our final open position in the accounting department was filled with the employee beginning 7/14/2008. Currently there is one employee that handles receipts through the deposit phase, another employee that enters the receipts into the system, with a third reconciling accounts receivable.

Item: 08-3

Criteria: All vacation and sick leave absences should be properly supported by documentation.

Condition: Supporting documentation for 3 of 23 sampled vacation and sick leave transactions could not be located.

Effect: The proper authorization and legitimacy of vacation and sick leave can not be substantiated.

Cause: Policies and procedures have not been consistently applied requiring that vacation and sick leave be supported by documentation.

Recommendation: To determine that proper authorization has been obtained and that charges are legitimate all vacation and sick leave absences should be supported with documentation.

Response: There was turnover in the payroll functions this past year which resulted in changes being made without proper training. The payroll accountant will be more careful and another employee will periodically review work to verify all is being done according to policy.

Section III - Federal Award Findings and Questioned Costs

Item: 08-4

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

Agency: U.S. Department of the Interior

Award Year: June 1, 2007 – May 31, 2008

Award Numbers: CTN00X10213; 04-NA-40-2095

Criteria: The Navajo Indian Irrigation Project (NIIP Grant) contract requires that quarterly 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 annual financial and 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: Three of four quarterly SF-269 reports submitted for the fiscal year 2008 were not submitted before the specified deadline. The annual financial and performance reports had not been submitted to the awarding agency or made available to the NAPI Board of Directors.

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 quarterly and annual financial reports and annual performance reports. 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: 08-5

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

Agency: U.S. Department of the Interior

Award Year: June 1, 2007 – May 31, 2008

Award Numbers: CTN00X10213; 04-NA-40-2095

Criteria: Quarterly and annual financial status reports should be based on the general ledger.

Condition: The quarterly financial status reports for fiscal year 2008 were improperly compiled using bank statement records instead of using the general ledger as the source of data for the reports.

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 utilization of bank statements as the basis for preparing the financial status reports does not take into account timing differences caused by outstanding checks and accruals, etc...

Questioned Costs: Unknown

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

Item: 08-6

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

Agency: U.S. Department of the Interior

Award Year: June 1, 2007 – May 31, 2008

Award Numbers: CTN00X10213; 04-NA-40-2095

Criteria: The Navajo Indian Irrigation Project (NIIP Grant) contract and the OMB Circular A-87 require that the expenditures of federal awards be only for costs and charges deemed allowable by the program.

Condition: During fiscal year 2008 an administrative employee for the Navajo Indian Irrigation Project (NIIP Grant) perpetrated the misuse of award monies resulting in credit card charges of $8,908.15 and payroll charges for overtime of $2,421.21 that were later determined by NAPI management to be inappropriate and not allowable by the program.

The employee had deliberately misrepresented the number of hours worked which resulted in inappropriate and unauthorized payroll charges. Payroll controls did detect the fabricated timesheets which led to further investigation of employee. Upon further investigation it was determined that the employee had deliberately circumvented and bypassed established controls surrounding credit card purchases and made unauthorized purchases that had not been detected; however, specific controls over the approval and authorization of credit card purchases should have detected the misuse of funds.

Cause: Control procedures have not been monitored to ensure that controls are operating effectively to deter, prevent, and detect financial misstatement due to error or fraud.

Effect: The program did not comply with contract requirements relating to allowable costs. The federal awarding agency might restrict funding, limit future award amounts, or impose additional conditions if contract stipulations are deemed to have not been met.

Questioned Costs: $11,329.36

Recommendation: Controls should be monitored to ensure that they are operating such that they are effective in preventing, deterring, and detecting financial misstatement and misappropriation of assets due to error or fraud.

Item: 08-7

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

Agency: U.S. Department of the Interior

Award Year: June 1, 2007 – May 31, 2008

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 **08-1**.

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.

Item: 08-8

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

Agency: U.S. Department of the Interior

Award Year: June 1, 2007 – May 31, 2008

Award Numbers: CTN00X10213; 04-NA-40-2095

Condition: Supporting documentation for vacation and sick leave for 3 out of a sample of 23 were missing. See Section II – Financial Statement Findings, item **08-3**.

Questioned Costs: Not Applicable

Recommendation: To determine that proper authorization has been obtained and that charges are legitimate all vacation and sick leave absences should be supported with documentation.

NAPI Responses

Navajo Agricultural Products Industry
Corrective Action Plan
Year Ended May 31, 2008

Federal Award Findings and Questioned Costs

Item: 08-4

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

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

Anticipated Completion Date: November 21, 2008

Corrective Action: We have already contacted the BIA to discuss this item with them. We have verified the proper reports to be filed and the proper documentation. The last quarter report is currently being completed on the proper forms, ensuring the numbers tie to the general ledger, and that the proper support is included. The accountant responsible for this has been instructed that these can no longer be late for any reason and the Controller and/or CFO will follow up with this each quarter to ensure timely, accurately filings.

Item: 08-5

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

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

Anticipated Completion Date: November 21, 2008

Corrective Action: We have already contacted the BIA to discuss this item with them. We have verified the proper reports to be filed and the proper documentation. The last quarter report is currently being completed on the proper forms, ensuring the numbers tie to the general ledger, and that the proper support is included. The accountant responsible for this has been instructed that these can no longer be late for any reason and the Controller and/or CFO will follow up with this each quarter to ensure timely, accurately filings.

Item: 08-6

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

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

Anticipated Completion Date: November 14, 2008

Corrective Action: Accounts Payable procedures found items in an expense report that were not properly authorized or reported. While working towards resolution on this (the expenses were not reimbursed), the payroll accountant determined that there were improper overtime charges with the same employee. An exhaustive analysis was done to determine the depth of these misappropriations. During the course of the analysis it was determined that it involved one employee and said employee quit. We have turned over our evidence to the authorities and have contacted the employee for a reimbursement plan. The employee agreed to a repayment plan but has yet to fulfill the agreement. We will continue to work towards full collection of these misappropriated funds. We have also learned from this event that when deficiencies are found we must work quickly to remedy the situation.

Item: 08-7

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

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

Anticipated Completion Date: January 21, 2009

Corrective Action: Due to restructuring of the accounting department the focus was to get financial statements current. Statements are now current and the department is now focusing on tightening up internal policies and procedures. Policies and procedures are currently being developed (in writing) and we are working on implementing further procedures to aid in the accurate and timely reporting of financial information. A checklist has been developed to aid in the completion of all required entries each month and is being implemented to further ensure that all entries are properly reviewed and approved. Another checklist is being developed to track the monthly reconciliations of all balance sheet accounts and to verify that they are properly documented and approved with any necessary adjustments being made timely - the month following the reconciliation. Furthermore, all journal entries and reconciliations will be filed in a central location instead of by the employee that performed the function.

Item: 08-8

CFDA Numbers: 15.CTN00X10213; 15.04-NA-40-2095

Program: Navajo Indian Irrigation Project

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

Anticipated Completion Date: November 24, 2008

Corrective Action: There was turnover in the payroll functions this past year which resulted in changes being made without proper training. The payroll accountant will be more careful and another employee will periodically review work to verify all is being done according to policy.

Navajo Agricultural Products Industry
Summary Schedule of Prior Audit Findings
Year Ended May 31, 2008

Status of Prior Year Federal Award Findings and Questioned Costs

Finding Number: 06-01

CFDA Number: 15.CTN00X10212

Program: Navajo Indian Irrigation Project

Status: Not Corrected.

Corrective Action: We have already contacted the BIA to discuss this item with them. We have verified the proper reports to be filed and the proper documentation. The last quarter report is currently being completed on the proper forms, ensuring the numbers tie to the general ledger, and that the proper support is included. The accountant responsible for this has been instructed that these can no longer be late for any reason and the Controller and/or CFO will follow up with this each quarter to ensure timely, accurately filings.