

COMMONWEALTH PORTS AUTHORITY
(A COMPONENT UNIT OF THE COMMONWEALTH
OF THE NORTHERN MARIANA ISLANDS)

INDEPENDENT AUDITORS' REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2010

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

Board of Directors
Commonwealth Ports Authority:

We have audited the financial statements of the Commonwealth Ports Authority (CPA) as of and for the year ended September 30, 2010, and have issued our report thereon dated August 5, 2011. 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 CPA'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 CPA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of CPA's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

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

We noted certain matters that we reported to management of CPA in a separate letter dated August 5, 2011.

This report is intended solely for the information and use of management and the Board of Directors of CPA, others within the entity, federal awarding agencies, and the cognizant audit and other federal agencies and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLC

August 5, 2011

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 AND ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Board of Directors
Commonwealth Ports Authority:

Compliance

We have audited the Commonwealth Ports Authority's (CPA) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of CPA's major federal programs for the year ended September 30, 2010. CPA's major federal program is identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (pages 8 through 14). Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of CPA's management. Our responsibility is to express an opinion on CPA'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 CPA'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 of CPA's compliance with those requirements.

As described in items 2010-1 through 2010-3 in the accompanying Schedule of Findings and Questioned Costs, CPA did not comply with requirements regarding allowable costs/cost principles, equipment and real property management and reporting that are applicable to its CFDA # 20.106 Airport Improvement Program. Compliance with such requirements is necessary, in our opinion, for CPA to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, CPA complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended September 30, 2010.

Internal Control Over Compliance

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

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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies as described in the accompanying Schedule of Findings and Questioned Costs as items 2010-1, 2010-2 and 2010-3. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of CPA as of and for the year ended September 30, 2010, and have issued our report thereon dated August 5, 2011. Our audit was performed for the purpose of forming our opinion on CPA's basic financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards (page 6) is presented for purposes of additional analysis as required by OMB Circular A-133 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 basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

CPA's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit CPA's responses and, accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of management and the Board of Directors of CPA, others within the entity, federal awarding agencies and the cognizant audit and other federal agencies and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLC

August 5, 2011

COMMONWEALTH PORTS AUTHORITY

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2010

Program Title	Federal CFDA Number/ Grantor I.D. No.	Expenditures
<u>U.S. Department of Transportation</u>		
<u>Airport Improvement Program</u>	20.106	
Direct Grants:		
Saipan International Airport - Saipan Rehabilitation Phase I, II, III, IV & V	3-69-0002-31/32/50/53/58/63	\$ 5,106,660
Saipan International Airport - Saipan Rehabilitation Phase VI (ARRA)	3-69-0002-60	3,863,780
Saipan International Airport - Rehabilitate Apron Taxilane	3-69-0002-43	258,476
Saipan International Airport - Security Enhancement Phase I	3-69-0002-38/41/52/55	84,313
Saipan International Airport - Emergency Generator/Procurement/Install	3-69-0002-57/59/61	4,204,932
Saipan International Airport - Improve Terminal Building	3-69-0002-62	385,234
Saipan International Airport - ARFF Training Facility Improvement	3-69-0002-68	859,296
Rota International Airport - Extended Runway	3-69-0003-19/20	2,775,314
Tinian International Airport - Strengthen Parallel Taxiway - Phase I	3-69-0011-15/17/19/20	7,196
Tinian International Airport - ARFF Building Relocation Phase I	3-69-0011-18	2,689
		<u>17,547,890</u>
<u>Transportation Security Administration</u>		
National Explosives Detection Canine Team Program (NEDCTP)	97.072	119,167
Saipan International Airport - Reimbursement Agreement	HSTS0208HSLR157	76,977
		<u>196,144</u>
<u>U.S. Department of Homeland Security</u>		
Port Security Grant Program	97.056	<u>317,001</u>
<u>U.S. Department of the Interior</u>		
OMIP CNMI-CPA-2007-1 Specialized Equipment/Training	15.875	9,755
OMIP CNMI-CPA-2006-4 2nd Year ARFF Training	15.875	28,029
Pass through the Government of the CNMI:		
Tinian Terminal Improvement	15.875	128,369
		<u>166,153</u>
		<u>\$ 18,227,188</u>
Reconciliation:		
Expenditures per Statement of Revenues, Expenses and Changes in Net Assets:		
Capital contributions		\$ 13,621,618
Other grant revenues and contributions		4,612,402
Less: Contributions from the CNMI government		<u>(6,832)</u>
		<u>\$ 18,227,188</u>

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

COMMONWEALTH PORTS AUTHORITY

Notes to the Schedule of Expenditures of Federal Awards Year Ended September 30, 2010

(1) Scope of Audit

The Commonwealth Ports Authority (CPA) was established as a public corporation by the Commonwealth of the Northern Mariana Islands (CNMI) by Public Law 2-48, effective November 8, 1981. All significant operations of CPA are included in the scope of the OMB Circular A-133 audit (the "Single Audit"). The U.S. Department of the Interior's Office of the Inspector General has been designated as CPA's cognizant agency for the Single Audit.

All of the programs presented in the Schedule of Expenditures of Federal Awards are subject to the Single Audit.

(2) Summary of Significant Accounting Policies

a. Basis of Accounting

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

Any federal funds expended in excess of federal funds received are recorded as a receivable from the grantor agency and any federal funds received in excess of federal funds expended are recorded as a payable to the grantor agency.

b. Indirect Cost Allocation

CPA has an approved indirect cost allocation rate of 16.3%, however, no indirect costs were recorded against any federal program for fiscal year 2010. The Federal Aviation Administration programs do allow, upon grantor approval, certain administrative expenses to be charged against the grants.

c. Matching Requirements

In allocating project expenditures between the federal share and the local share, a percentage is used based upon local matching requirements, unless funds are specifically identified to a certain phase of the project.

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs
Year Ended September 30, 2010

A. SUMMARY OF AUDITORS' RESULTS

Financial Statements

- | | |
|---|-------------|
| 1. Type of auditors' report issued: | Unqualified |
| Internal control over financial reporting: | |
| 2. Material weakness(es) identified? | No |
| 3. Significant deficiency(ies) identified that is not considered to be a material weakness? | No |
| 4. Noncompliance material to the financial statements noted? | No |

Federal Awards

- | | |
|--|-----------|
| Internal control over major programs: | |
| 5. Material weakness(es) identified? | No |
| 6. Significant deficiency(ies) identified that is not considered to be a material weakness? | Yes |
| 7. Type of auditors' report issued on compliance for major programs: | Qualified |
| 8. Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? | Yes |
| 9. CPA's major program was as follows: | |
| CFDA | |
| <u>Number</u> <u>Federal Program</u> | |
| 20.106 Airport Improvement Program | |
| 10. Dollar threshold used to distinguish between Type A and Type B Programs, as those terms are defined in OMB Circular A-133: | \$546,815 |
| 11. CPA qualified as a low-risk auditee, as that term is defined in OMB Circular A-133? | No |

B. FINDINGS RELATING TO THE FINANCIAL STATEMENTS, WHICH ARE REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

No findings reported.

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs
Year Ended September 30, 2010

**C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS
AUDIT**

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>	<u>Refer Page #</u>
2010-1	Allowable Costs/Cost Principles	\$ -	10 - 11
2010-2	Equipment and Real Property Management	\$ -	12 - 13
2010-3	Reporting	\$ -	14

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2010

**C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS
AUDIT**

Finding No.: 2010-1
Federal Agency: U.S. Department of Transportation
CFDA Program: 20.106 Airport Improvement Program
Federal Award No.: AIP No. 3-69-0002-59
Federal Award Periods Ended: 09/01/13
Area: Allowable Costs/Cost Principles
Questioned Costs: \$-0-

Criteria: Construction projects funded by federal grants are required to include the Buy American clause within the contract.

Condition: Our tests of project specifications and notice to bidders for the Public Address System Replacement project and the Emergency Generator project did not note the inclusion of the Buy American clause.

Cause: The cause of the above condition is the lack of controls to ensure compliance with federal contract requirements.

Effect: The effect of the above condition is lack of compliance with grant requirements. No questioned costs result as the both contractors adhered to requirements of the Buy American clause.

Recommendation: We recommend management ensure all provisions required by federal grant awards are included in contracts and/or project specifications.

Prior Year Status: Noncompliance with Buy American clause requirement was reported as a finding in the Single Audit of the CPA for fiscal year 2009.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Derek T. Sasamoto, Comptroller

Corrective Action: The exclusion of the Buy American Clause in the proposal package for the SIA Generator Project was an oversight on the A/E consultant and CPA's Engineering Department at the time. However, CPA did verify with the contractor through all payment applications that all manufactured items procured for that project were purchased in the USA.

As for the SIA PA System, the clause was originally included in the project documents along with all other federal requirements. However, during the bidding stage, contractors were inquiring on the Buy American requirement for certain items such as Sony or Toshiba stereo players, etc., that are not made in the USA. In the response to the inquiries, CPA's Staff Engineer at that time advised CPA Engineering's Contract Administrator to issue an email advising that the clause would be removed. This email was sent to all prospective contractors on March 12, 2009. It should be noted that the proposal documents still required all equipment to be FCC approved and UL listed. During the 2010 audit, CPA Engineering reviewed the submittals for this project and also found that all equipment from speakers to LEDs were all procured in the USA.

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2010

Finding No.: 2010-1, Continued
Federal Agency: U.S. Department of Transportation
CFDA Program: 20.106 Airport Improvement Program
Federal Award No.: AIP No. 3-69-0002-59
Federal Award Periods Ended: 09/01/13
Area: Allowable Costs/Cost Principles
Questioned Costs: \$-0-

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

CPA will ensure that this condition does not occur again. CPA's Engineering Department is aware of this requirement, and that it is a repeat finding from FY 2009. The Department is adamant in ensuring compliance with the Buy American clause. Moreover, in the event that a new Staff Engineer is hired, CPA's current Engineering staff will ensure that he/she is aware of this requirement.

Finally, it should also be noted that CPA's 2009 audit was completed in late August 2010, one month before the end of the FY. As such, timing was an issue when CPA received its FY 2009 audit findings, CPA had already made its decisions in FY 2010 for the projects identified above in terms of them being recognized as non-compliant with the Buy American clause. Thus, the repeat finding was not intentional nor a "true" oversight, but rather CPA was unaware that the situation was occurring until the 2009 audit was released which unfortunately took place close to the end of FY 2010.

Proposed Completion Date: Ongoing

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2010

Finding No.: 2010-2
Federal Agency: U.S. Department of Transportation
CFDA Program: 20.106 Airport Improvement Program
Federal Award Nos.: All AIP Grants
Area: Equipment and Real Property Management
Questioned Costs: \$-0-

Criteria: In accordance with applicable equipment and real property management requirements, procedures for managing equipment (including replacement equipment), whether acquired in whole or in part with grant funds, until disposition takes place will, as a minimum, meet the following requirements:

- (1) Property records must include a description of the property, a serial number or other identification number, the source of property, who holds title, the acquisition date, cost of the property, percentage of Federal participation in the cost of the property, the location, use and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property;
- (2) A physical inventory of the property must be taken and the results reconciled with the property records at least once every two years;
- (3) A control system must be developed to ensure adequate safeguards to prevent loss, damage, or theft of the property. Any loss, damage, or theft shall be investigated;
- (4) Adequate maintenance procedures must be developed to keep the property in good condition; and
- (5) If the grantee or subgrantee is authorized or required to sell the property, proper sales procedures must be established to ensure the highest possible return.

Condition: CPA performed a physical inventory of its fixed assets during fiscal year 2010; however, we were advised that it was still ongoing and results had not been reflected in the general ledger at September 30, 2010. In addition, a log indicating the location of equipment is not being maintained. Total fixed asset additions related to CPA's major program amounted to \$13,147,492, \$11,051,139 and \$9,826,975 during fiscal years 2010, 2009 and 2008, respectively. Of the total additions, \$13,076,085, \$10,734,776 and \$9,778,502 represent additions to construction in progress during the fiscal years ended September 30, 2010, 2009 and 2008, respectively.

Cause: The cause of the above condition is the lack of controls to ensure compliance with equipment management requirements.

Effect: The effect of the above condition is noncompliance with equipment and real property management requirements.

Recommendation: We recommend that management ensure a physical inventory of equipment is conducted at least once every two years. We also recommend that documentation procedures be established to ensure fixed asset records are maintained.

Prior Year Status: The lack of compliance with equipment and real property management requirements was reported as a finding in the Single Audits of CPA for fiscal years 2008 and 2009.

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2010

Finding No.: 2010-2, Continued
Federal Agency: U.S. Department of Transportation
CFDA Program: 20.106 Airport Improvement Program
Federal Award Nos.: All AIP Grants
Area: Equipment and Real Property Management
Questioned Costs: \$-0-

Auditee Response and Corrective Action Plan:

Name of Contact Person: Derek T. Sasamoto, Comptroller

CPA acknowledges the finding. CPA did conduct a physical inventory in FY 2010. This was completed in September 2010 and did include fixed assets. No distinction was made, in terms of what is to be inventoried, between federally funded and CPA funded items/equipment. All items/equipment were inventoried. Funding sources, though, are indicated on the inventory log. The physical inventory covered all airports and seaports for all islands. In fact, a new inventory log was created, as well, to ensure property management compliance. However, the updated inventory results were not posted/updated to the general ledger (fixed asset disposal, for example) and thus it was not recognized/updated in FY 2010. CPA's accounting Manager is aware of the situation and has assured the Comptroller that this condition has been rectified in FY 2011 and will be complied with onward.

Proposed Completion Date: Ongoing

COMMONWEALTH PORTS AUTHORITY

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2010

Finding No.: 2010-3
Federal Agency: U.S. Department of Transportation
CFDA Program: 20.106 Airport Improvement Program
Federal Award Nos.: All AIP Grants
Area: Reporting
Questioned Costs: \$-0-

Criteria: Sponsors of commercial service airports are required to submit FAA Form 5100-127, *Operating and Financial Summary (OMB No. 2120-0557)*, which captures revenues and expenses at the airport, including revenue surplus.

Condition: CPA did not submit FAA Form 5100-127 to the grantor agency.

Cause: The cause of the above condition is lack of documentation evidencing that the grantor does not require the form, or that CPA complied through submission of the audited financial statements to the grantor.

Effect: The effect of the above condition is possible noncompliance with applicable reporting requirements. No questioned costs resulted from the finding.

Recommendation: We recommend CPA consult with the grantor regarding disposition of this issue.

Auditee Response and Corrective Action Plan:

Name of Contact Person:

Corrective Action: This requirement was unknown to CPA at the time this finding was established. In fact, CPA cannot find any record of filing this form nor can CPA find record of being cited by the FAA for non-compliance with this requirement. Moreover, upon inquiring with FAA representatives, the particulars of this form were not immediately known. However, a later communication from the FAA advised CPA to submit the form. As such, CPA will be submitting the form (all submissions are electronic and public access to view reports is available) for FY 2010 and will comply with this requirement in FY 2011 onward. Moreover, CPA understands that this report is due within 120 days of the end of each fiscal year for all airports that: agreed to AIP grant assurances on or after January 1, 1995, have enplanements of 2,500 or more passengers in a calendar year, and that provided commercial service in the preceding calendar year for at least 2,500 enplanements. Finally, CPA has reviewed Advisory Circular 150/5100-19D dated June 23, 2011, which is the most up-to-date circular governing FAA forms 5100-127 and 5100-126. As such, CPA is taking the necessary steps to ensure compliance with this requirement.

Proposed Completion Date:

COMMONWEALTH PORTS AUTHORITY

Unresolved Prior Year Comments
Year Ended September 30, 2010

Questioned Costs

The prior year Single Audit report on compliance with laws and regulations noted the following questioned costs and comments that were unresolved at September 30, 2010:

Questioned costs as previously reported	\$ 508,458
Questioned costs of fiscal year 2010 Single Audit	<u> -</u>
Unresolved questioned costs at September 30, 2010	\$ <u>508,458</u>

Unresolved Findings

The status of unresolved prior year findings is discussed within the Schedule of Findings and Questioned Costs section of this report (pages 8 through 14).



COMMONWEALTH PORTS AUTHORITY

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SUMMARY OF SCHEDULE OF PRIOR AUDIT FINDINGS

Status of audit findings included in the schedule of findings and questioned costs for the year ended September 30, 2009:

FINDINGS RELATING TO THE FINANCIAL STATEMENTS, WHICH ARE REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

Finding No. 2009-1 - Corrective action was taken.

FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS AUDIT

Finding No. 2009-2 - Not corrected. See corrective action plan to Finding No. 2010-1.

Finding No. 2009-3 - Not corrected. See corrective action plan to Finding No. 2010-2.

Finding No. 2009-4 - Corrective action was taken.