

DEPARTMENT OF PUBLIC LANDS
(A GOVERNMENTAL FUND OF THE COMMONWEALTH
OF THE NORTHERN MARIANA ISLANDS)

INDEPENDENT AUDITORS' REPORT 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*

Mr. Pedro A. Tenorio
Acting Secretary
Department of Public Lands:

We have audited the financial statements of the Department of Public Lands (DPL) as of and for the year ended September 30, 2010, and have issued our report thereon dated June 10, 2013. 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

Management of DPL is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered DPL'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 DPL's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of DPL'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 was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Responses (pages 3 through 11), we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

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. We consider the deficiencies described in the accompanying Schedule of Findings and Responses as items 2010-1, 2010-2, 2010-3 and 2010-5 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether DPL'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 instances of noncompliance that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as items 2010-2, 2010-4, 2010-6 and 2010-7.

We noted certain matters that we reported to management of DPL in a separate letter dated June 10, 2013.

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

This report is intended solely for the information and use of management and is not intended to be and should not be used by anyone other than these specified parties.

Debbie J. Jones LLC

June 10, 2013

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses
Year Ended September 30, 2010

Purchases/Disbursements

Finding No. 2010-1

Criteria: An effective system of internal control provides for policies and procedures that require expenses to be recorded in the period incurred.

Condition: Tests of eighteen nonpayroll expenditures aggregating \$353,477, rental expenses totaling \$212,264 and twenty-three subsequent disbursements totaling \$580,034 noted the following:

1. Four nonpayroll expenses (document PV nos. 864362, 819172, 823071 and 831872) totaling \$120,822 relate to services incurred in a prior fiscal year but recorded as expenses upon payment during the current fiscal year.
2. Five rental expenses (document PV nos. 823061, 823063, 823065, 829652 and 829660) totaling \$98,184 included payment for months in the prior fiscal year aggregating \$58,846.

The above conditions were corrected through proposed audit adjustments.

3. Two subsequent disbursements (document PV nos. 969526 and 968437) totaling \$7,200 pertain to fiscal year 2010 but were not accrued as of September 30, 2010. Management did not consider the amount sufficiently material to the financial statements to warrant an adjustment.

Cause: The cause of the condition is the lack of monitoring procedures in place for cash disbursements.

Effect: The effect of the above condition is the misstatement of expenses.

Recommendation: We recommend DPL strengthen controls over processing, recording, and monitoring disbursements.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Evelyn J. Sablan, Finance Division

Corrective Action: CNMI Public Law 15-2 abolished the Marianas Public Lands Authority and created the Department of Public Lands (DPL) under the Executive Branch. The function of the DPL Accounting Division was transferred to the CNMI Department of Finance. DPL's Finance Division processes all accounts payable vouchers (APVs) and forwards the APVs to the CNMI Department of Finance for posting and processing of payments. DPL maintains a cash disbursement journal for recording and monitoring disbursements. The accounting staff will be more careful in recording expenses and will ensure that expenses incurred within the fiscal year are recognized.

Proposed Completion Date: Closing date of the audit report.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Revenue/Receipts

Finding No. 2010-2

Criteria: Management is responsible to enforce its policies for leasing public lands. Long-term lease contracts and temporary permits require that the lessee, not later than forty-five (45) days after the end of each calendar year of the lease or permit submit audited financial statements. Some leases and permits require that the financial statements be audited by certified public accountants.

Condition: In our tests of seventy-five receipts, we found seven long-term lease contracts and temporary permits that require the lessee to submit financial statements audited by accountants or by certified accountants; however, such audited financial statements were not in file. The lessee numbers are following:

Lessee No.

T0315S
L8648S
L9603S
T06019S
T0227S
LB8901S
T0921S

Cause: The cause of the above condition is the lack of monitoring procedures in place to determine which contracts and/or permits require financial statements or audited financial statements.

Effect: The effect of the above condition is the potential loss of revenues when contracts and/or permits are up for renewal and lease amounts are to be determined.

Recommendation: We recommend that management endeavor to update the lease contracts and permits and propose a standard threshold which would differentiate those lessees to be audited by certified public accountants from those by regular accountants, or by none at all.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Evelyn J. Sablan, Finance Division

Corrective Action: The rates of long-term leases are determined for the duration of the agreement and usually rates change based on the appraised market value of the property every five years. Upon renewal of the temporary permit, the permittee is required to submit an audited financial statement if their year end business gross receipts are more than \$500,000; otherwise, they are only required to submit a financial statement signed by their accountant and the president of the company. DPL is aggressively taking corrective action to ensure that the lessees and permittees adhere to the provisions provided in the agreement.

T0315S - DPL will strictly enforce strictly the submission of annual financial statements as stipulated in the agreement.

L8648S - Audited financial statements are on file.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Finding No. 2010-2, Continued

Auditee Response and Corrective Action Plan, Continued:

Corrective Action, Continued:

L9603S - Audited financial statements by a Certified Public Accountant are not required as the lessee's business gross receipts and assets are less than \$500,000; however, financial statements must be signed by the President and the Accountant of the company and should be submitted annually.

T06019S - DPL will ensure that audited financial statements be submitted annually.

T0227S - DPL will ensure that financial statements signed by the President and the Accountant are submitted; however, if assets are more than \$500,000, audited financial statements will be required.

LB8901S - An income statement and a balance sheet certified by the General Manager are on file.

T0921S - DPL will strictly enforce the submission of annual financial statements as stipulated in the agreement.

Proposed Completion Date: Closing date of the audit report.

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Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Expenses

Finding No. 2010-3

Criteria: Pursuant to Public Law 15-02 effective October 1, 2007, disbursement of DPL expenses, including land compensation claims, was centralized at the CNMI Department of Finance. DPL reimburses the CNMI for expenses paid on behalf of DPL.

Condition: Adjustments (GL account no. 46000) of \$544,151 were recorded by DPL to reconcile due to CNMI at September 30, 2010. Explanation or details related to the recorded amount were not available. Further, reconciliation between DPL and the CNMI Department of Finance is currently not evident.

Cause: The cause of the above condition is the lack of monitoring and timely reconciliation of transactions with the CNMI Department of Finance.

Effect: The effect of the above condition is a potential misstatement of expenditures.

Recommendation: We recommend DPL monitor and reconcile transactions with the CNMI Department of Finance in a timely manner.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Evelyn J. Sablan, Finance Division

Corrective Action: Effective fiscal year 2011, DPL has been remitting funds to the central government based on the processed APVs for easy reconciliation with the CNMI Department of Finance. DPL has been able to accurately tract the records by implementing this system. DPL is encountering difficulty reconciling records with the CNMI Department of Finance because of lack of manpower; however, DPL and the CNMI Department of Finance are cooperatively implementing a check and balance system.

Proposed Completion Date: Closing date of the audit report.

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Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Expenses

Finding No. 2010-4

Criteria: Personnel in accounting may transfer property, which is controlled in the Master Inventory Control Record, by initiating a "Request for Transfer Form" and receiving the approval of the Property Management Branch Manager.

Condition: We were not provided documentation to support one fixed asset that was transferred (APV # 07-169).

Cause: The cause of the condition is the lack of controls to maintain property records on file.

Effect: The effect of the condition is that DPL is not in compliance with applicable equipment and real property management requirement.

Recommendation: We recommend that DPL take reasonable steps to maintain documentation of all property records on file.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Evelyn J. Sablan, Finance Division

Corrective Action: DPL will ensure that documents requested are provided; however, the document mentioned is on file. The Xerox machine was purchased from IBSS and transferred to the Tinian office approval of which was signed by the Director on July 9, 2009. DPL will adhere to the policy of transferring property at all times.

Proposed Completion Date: Closing date of the audit report.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

General Ledger System

Finding No. 2010-5

Criteria: An effective system of internal control over financial reporting includes maintenance of a separate general ledger system that will record transactions and generate reliable and relevant financial information in a timely manner.

Condition: DPL has not maintained a separate general ledger system since fiscal year 2007. Cash transactions are summarized in the cash receipts and cash disbursements journals. We noted two different accounts payable vouchers (APV nos. 829652 and 829660) and payment checks (check nos. 363462 and 363998) were processed and issued for the same rental expense of \$12,096.

Cause: The cause of the above condition is the failure to implement available system controls over the financial reporting process and the lack of established monitoring control procedures to determine the accuracy and completeness of disbursements processed at CNMI Finance.

Effect: The effect of the above condition is the lack of reliable and relevant financial information and the inability to timely detect errors and inaccuracies.

Recommendation: We recommend that DPL implement a general ledger system to record transactions and generate reliable and relevant financial information. We further recommend that DPL establish monitoring control procedures over disbursements and perform periodic reconciliations with CNMI Finance to verify the accuracy and completeness of disbursements processed.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Evelyn J. Sablan, Finance Division

Corrective Action: The DPL Finance Division ensures that cash disbursements are recorded efficiently and accurately. Also, the cash disbursements journal is monitored and reconciled regularly to determine errors. Marianas Management Corporation and DPL have reconciled the accounts and agreed to offset the over payment against future payments.

Proposed Completion Date: Closing date of the audit report.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Local Noncompliance

Finding No. 2010-6

Criteria: Per the Procurement Administrative Code §70-30.3-201, *requirements for competition*, “officials with expenditure authority shall provide for full and open competition through use of the competitive procedures that are best suited to the circumstances. Further, the CNMI procurement regulations state the following:

- Bidding is not required for procurement under \$2,500
- Bidding is not required but is encouraged for procurement over \$2,500 and under \$10,000. The official with expenditure authority must obtain price quotations from at least three vendors and base the selection on competitive price and quality for procurement valued at \$2,500 to \$10,000. Any price quotations obtained must be written, documented, and submitted to the P&S Director for approval.
- Further, §70-30.3-215, permits contracting without full and open competition, subject to the following requirements:
 - (1) Small purchases (§ 70-30.3-220);
 - (2) Sole source procurement (§ 70-30.3-225);
 - (3) Emergency procurement (§ 70-30.3-230); and
 - (4) Expedited purchasing in special circumstances (§ 70-30.3-235).

Specifically for sole source procurement, in accordance with Section 3-106 (2) of the CNMI Procurement Regulations, a written justification for sole source procurement shall be prepared by the official with expenditure authority. The written sole source justification shall contain the following: a) the specific unique capabilities of the contractor selected; b) the specific reasons why such unique capabilities are required for the particular procurement; c) what specific efforts were made to obtain competition and d) what other specifically-named contractors and other sources, both on-island and off-island, have been considered and why they were not selected. Moreover, generalized statements are not adequate and documents to support the statements justifying the sole source procurement are mandatory.

Condition: Of eighteen non-payroll expenditures tested aggregating \$353,477, we noted the following:

1. There was no evidence that competitive procurement was performed for one item totaling \$15,000 (APV no. 820736, check no. 354528). Further, there was no supporting contract for this disbursement.
2. Two contracts (document no. 516163-OC and 522692-OC) were procured using sole source procurement. Although written justification for the sole source was obtained, there was inadequate documentation supporting 1) what specific efforts were made to obtain competition; and 2) what other specifically-named contractors and other sources, both on-island and off-island, have been considered and why they were not selected.
3. For one contract, (document no. EA07-017), pertinent procurement documents (i.e. bid summary, bids received, bid evaluation, etc.) evidencing competitive procurement were not provided.

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Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Finding No. 2010-6, Continued

Cause: The cause of the condition is the failure to comply with established CNMI procurement regulations and lack of proper and systematic filing of relevant documents supporting procurement.

Effect: The effect of the above condition is noncompliance with local procurement regulations.

Recommendation: We recommend that the DPL adhere to established CNMI Procurement Regulations. We further recommend that DPL work diligently with Procurement and Supply Office towards maintaining and filing all relevant procurement documents accordingly.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Evelyn J. Sablan, Finance Division

Corrective Action: Unfortunately, it was a management decision to proceed without adhering to procurement policies. For future contracts, DPL will adhere to CNMI Procurement regulations.

Proposed Completion Date:

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Local Noncompliance

Finding No. 2010-7

Criteria: The CNMI Constitution requires that all revenues received by DPL in excess of the amount necessary to meet reasonable expenses of administration and management, land surveying, homestead development, and any other expenses reasonably necessary for the accomplishment of its functions, must be transferred to the Marianas Public Land Trust (MPLT).

Condition: DPL has not obtained concurrence from MPLT regarding its method for determining amounts owed. DPL has also not determined the basis for reservation of fund balance of \$1,000,153 at September 30, 2010.

On June 10, 2010, DPL transferred \$2,500,000 to the CNMI pursuant to Public Law 17-6, which authorized the Governor to reprogram available funds including those funds available to all public corporations, agencies and entities of the CNMI, in order to help sustain public services during the State of Emergency declared in June 2010.

Cause: The cause of the above condition is the lack of agreement with MPLT and policies and procedures to determine restricted fund balance.

Effect: The effect of the above condition is potential noncompliance with DPL's constitutional mandate to transfer net revenues received to MPLT.

Recommendation: We recommend that DPL obtain a legal determination on the merits of this transfer.

Auditee Response and Corrective Action Plan:

Name of Contact Person:

Corrective Action: The Governor exercised his authority by invoking Article III § 10 under the CNMI Constitution: (1) suspend all statutory on regulatory provisions as required and (2) the reprogramming of the funds necessary to meet this emergency.

Nonetheless, DPL will ensure that any future funds shall be transferred to MPLT in order to comply with DPL's constitutional mandate.

Proposed Completion Date: Closing date of the audit report.

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Unresolved Prior Year Comments
Year Ended September 30, 2010

There are no unresolved findings from prior year audits of DPL.