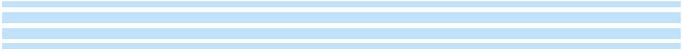




Office of the Public Auditor
Commonwealth of the Northern Mariana Islands

**Commonwealth Utilities Corporation
Audit of Personnel Hiring
From October 1, 1999 Through July 15, 2001**



Audit Report
AR-03-01

January 15, 2003

Mr. Francisco Q. De Leon Guerrero
Chairperson, Board of Directors
Commonwealth Utilities Corporation
Saipan, MP 96950

Ms. Lorraine Babauta
Executive Director
Commonwealth Utilities Corporation
Saipan, MP 96950

Dear Mr. De Leon Guerrero and Ms. Babauta:

Subject: Final Audit Report - Commonwealth Utilities Corporation - Audit of Personnel Hiring from October 1, 1999 Through July 15, 2001 (Report No. AR-03-01)

This report presents the results of the Office of the Public Auditor's (OPA) audit of the Commonwealth Utilities Corporation (CUC) personnel hiring from October 1, 1999, through July 15, 2001¹. The objectives of this audit were to determine whether: (1) CUC adopted adequate personnel policies based on a merit system mandated by law, and (2) personnel hiring practices complied with applicable personnel policies.

OPA found that CUC failed to develop and adopt comprehensive personnel rules and regulations based on the merit system. As a result, CUC hired 40 employees non-competitively during Fiscal Years 2000 and 2001. Although CUC has its own personnel manual, it does not address personnel practices such as limited term and provisional appointments. Also, OPA found that five CUC employees who were hired non-competitively worked beyond their terms and continued to be compensated without authorized personnel actions. In addition, CUC board involvement in hiring CUC employees has served to usurp management's role in daily operations. Furthermore, CUC has not adopted a salary scale as required, and therefore has no assurance that employees are fairly compensated. Finally, the absence of a permanent human resources manager may have contributed to CUC's failure to implement a merit based personnel system.

¹ In accordance with statutory restrictions in the Auditing and Ethics Acts, names of individuals are not disclosed in this report.

We recommended that CUC: (1) continue the effort to develop and adopt comprehensive personnel rules and regulations. If it determines that limited term appointments are necessary for CUC operations, it should define this practice in the proposed personnel regulations; (2) continue the effort to develop and adopt CUC's own Classification and Compensation Schedule and transmit it to the Legislature for review or adopt the salary scale applicable to autonomous agencies to ensure that its employees are fairly compensated; (3) strongly consider hiring a qualified permanent human resources manager to ensure that CUC follows the merit system to help CUC implement a comprehensive personnel manual; (4) develop a control procedure to ensure that all CUC employees receiving compensation have authorized personnel actions. We also recommended that the Chairman of the Board issue a directive to ensure that board members focus on policy matters and leave personnel hiring to the Executive Director and the human resources manager.

In its response dated December 10, 2002, (**Appendix A**), CUC agreed with two of our recommendations. Based on CUC's response, we consider Recommendations 1 and 2 resolved pending adoption of its Human Resources Policies and Procedures as well as its Classification and Compensation System. Recommendations 3, 4 and 5 are considered open as CUC did not respond to these three recommendations. The additional information or action required to close the recommendations is presented in **Appendix B**.

BACKGROUND

In the year 2001, OPA began planning an audit of Commonwealth Utilities Corporation (CUC) operations. After surveying selected CUC operations, OPA conducted four separate audits addressing CUC travel, personnel hiring, compensation, and procurement practices. This audit covers CUC personnel hiring during the period October 1, 1999, through July 15, 2001.

Commonwealth Utilities Corporation

CNMI Public Law 4-47, the CUC Act (4 CMC §8111 et seq.), established CUC as a public corporation and a component unit of the Government of the CNMI effective October 1, 1985. CUC is responsible for supervising the construction, maintenance, operation and regulation of all CNMI utility services, including power, sewerage, refuse collection, telephone, cable television, and water. It is governed by a Board of Directors composed of eight members appointed by the Governor, with the advice and consent of the CNMI Senate. The CUC Board appoints an Executive Director who administers CUC operations on behalf of the Board.

The CUC Act (4 CMC §8133(c)) exempts CUC from CNMI Civil Service Regulations and authorizes it to develop, adopt, and administer its own merit personnel system. It further specifies that the Board will establish rules and regulations governing the selection, promotion, performance evaluation, demotion, suspension, and dismissal of employees. On May 1, 1995, the Board approved a CUC Personnel Manual.

OBJECTIVE, SCOPE AND METHODOLOGY

The objectives of this audit were to determine whether: (1) CUC adopted adequate personnel policies based on a merit system as mandated by law, and (2) personnel hiring practices complied with applicable personnel policies.

Our review covered the 88 CUC employees hired from October 1, 1999, to July 15, 2001. To address these objectives, OPA: (1) reviewed CUC's Personnel Manual and applicable personnel policies; (2) examined documents in employees' personnel files such as job vacancy announcements, written examinations, interview sheets, and personnel actions of selected CUC employees; (3) interviewed responsible CUC employees; and (4) analyzed CUC's hiring of employees under job vacancy announcements, limited term appointments, and provisional hiring.

We performed our audit at the CUC offices in Saipan, Rota, and Tinian from July 2001 to April 2002. This audit was made in accordance with Government Auditing Standards issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures as were necessary in the circumstances.

As part of our audit, we evaluated CUC's internal control over the processing of personnel documents and compliance with applicable personnel rules and regulations. We found weaknesses in these areas which are discussed in the Findings and Recommendations sections of this report. Our recommendations when implemented should improve controls in these areas.

PRIOR AUDIT COVERAGE

While the Office of the Public Auditor has conducted other audits of the Commonwealth Utilities Corporation during the past five years, these audits did not address personnel hiring.

FINDING AND RECOMMENDATIONS

A. Absence of Written and Adequate Personnel Policies

Although CUC's enabling legislation requires it to develop and adopt its own personnel rules and regulations based on a merit system, it has not done so. CUC has its own personnel manual but it does not address many of CUC's personnel practices and it has never been published in the Commonwealth Register and therefore has no force and effect as a regulation. As a result, CUC failed to consistently comply with the merit principle system mandated by law.

The law requires that CUC implement a merit personnel system and that related regulations be published in the Commonwealth Register. The CUC Act, in 4 CMC §8133(c), provides that:

The corporation shall develop, adopt, and administer a merit personnel system that rewards productivity and service, provides management flexibility, and includes provisions for employees to appeal serious disciplinary action. The board shall establish rules and regulations governing the selection, promotion, performance evaluation, demotion, suspension, dismissal, and other disciplinary rules for employees of the corporation

Further, the Administrative Procedure Act, in 1 CMC §9102(d), requires that CNMI rules and regulations be published in the Commonwealth Register. More specifically this Act states:

No agency rule, order, or decision is valid or effective against any person or party nor may it be invoked by the agency until the rule, order, or decision has been published in accordance with subsection (a) of this section, and has been filed with the Registrar of Corporations and the Governor....

Our audit showed that CUC has not developed and adopted adequate personnel rules and regulations based on a merit system. CUC uses a 20 page personnel manual approved by the Board on May 1, 1995. This manual, however, has not been published in the Commonwealth Register and does not address many of CUC's personnel practices such as hiring of employees under limited term and provisional appointments. Thus, CUC human resources personnel frequently resort to following additional procedures and directives contained in internal memoranda of the former Executive Director, minutes of CUC board meetings, verbal instructions of CUC officials, and occasionally, the CNMI's Personnel Rules and Regulations. As a result, personnel staff have no definitive guidelines for implementing and documenting procedural steps in CUC's hiring process, and therefore, CUC cannot show that it is hiring based on merit and qualifications.

The absence of a comprehensive personnel rules and regulations has, in our opinion, been one of the reasons CUC failed to enforce compliance with the merit principle system mandated by law as discussed below.

B. Employees Hired Non-Competitively

CUC is required by its enabling legislation and its own personnel manual to hire employees on a competitive basis. This means that vacancies should be announced and procedures should be in place for the selection of the most qualified individual. OPA found, however, that CUC hired 40 employees non-competitively during Fiscal Years 2000 and 2001. The absence of a comprehensive personnel policy prohibiting non-competitive appointments may explain why CUC failed to enforce compliance with the applicable laws as concerns competitive hiring. As a result, CUC may have not hired the most qualified individuals.

As previously stated, 4 CMC §8133(c) provides that CUC “...shall develop, adopt, and administer a merit personnel system....” Under such system, CUC should hire personnel on a competitive basis. That means that vacancies should be announced or advertised, and that procedures should be in place to enable selection of the most qualified individuals.

CUC’s Personnel Manual serves to implement this enabling legislation. The Personnel Manual section 2.02 (B) states that:

Whenever a new position is created by the Board, or whenever a vacancy occurs in an existing position, the Executive Director, or his designee shall... prepare an announcement of the position...widely publicize the announcement...and the requesting official will select the applicant he/she thinks is best suited for the position and make recommendation to the Executive Director.

It further states that the Executive Director may waive the above procedure if, in his opinion, a qualified employee of CUC can be promoted to fill a vacancy.

Our audit showed that CUC did not comply with the merit personnel system mandated by law because 45 percent of its employees were hired non-competitively during Fiscal Years 2000 and 2001. Of 88 employees hired from October 1, 1999 to July 15, 2001, 40 were hired non-competitively, namely 32 under limited term appointments² and eight under provisional appointments³. This means that appointed individuals were hired without the position vacancies being announced, and without going through the normal selection process that involves written examinations, interviews, and screening of applicants. Also, we found no written justification demonstrating the need for these employees.

Our review of these 40 hiring actions showed that three were subsequently converted to permanent positions without announcements, two were terminated at the end of their terms of employment, and 18 had exceeded their one-year terms and were again extended without

² The CUC Personnel Manual does not define Limited Term Appointment. However, CNMI’s Personnel Service System Rules and Regulations (PSSRR) specifies that a Limited-Term Appointment is not to exceed one (1) year. An employee can either be given a full-time or part-time position and any person given this type of appointment must meet the minimum qualifications for the class of position to which appointed. A Limited-Term Appointment may be converted to Permanent at the end of one year provided the employee has demonstrated satisfactory performance for 52 consecutive weeks.

³ The CUC Personnel Manual does not define Provisional Appointment. However, CNMI’s PSSRR specifies that a Provisional Appointment is usually for ninety (90) days and is used to fill a permanent position in the absence of an appropriate eligibility list. The appointment can be extended for a maximum of one hundred and eighty (180) days when the examination fails to make available an adequate number of qualified candidates. Any person given a provisional appointment must meet the minimum qualifications for the class of position to which appointed.

any change in their employment status. Of the remaining 17, six have not yet completed their terms of employment, and 11 were converted to permanent employees after their positions were subsequently announced competitively.

Our analysis (as shown in **Figure 1** below) of hiring over the last three years indicates that limited term and provisional appointments were most significant in Fiscal Year 2001 when over half of all hires were such appointments. During Fiscal Year 2001, CUC did not have a human resources manager for ten months who could have helped enforce compliance with merit principles.

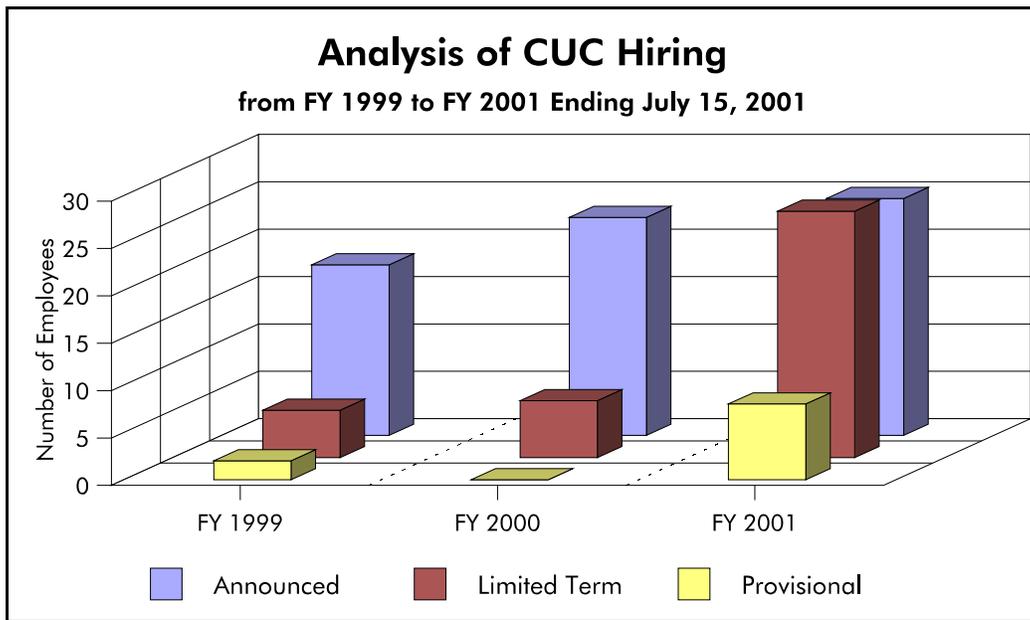


Figure 1

The absence of a comprehensive personnel policy addressing limited term and provisional appointments may explain why CUC failed to enforce compliance with the applicable laws as concerns competitive hiring. In addition, non-compliance may have occurred because board members became involved in hiring actions, hiring 12 employees under limited term and provisional appointments as discussed below. As a result, CUC failed to hire employees based on a merit principle system and may not have hired the best qualified employees. It is a concern because most of those employees hired under limited term and provisional appointments were subsequently made permanent employees. While CUC is taking steps to adopt comprehensive personnel rules and regulations, such regulations, as currently drafted, do not address limited term appointments.

Finally, OPA found that five CUC employees, hired under limited term and provisional appointments, worked beyond their appointment periods and continued to be compensated for between 7 to 20 months without any authorized personnel actions. It occurred because CUC did not establish a control procedure to ensure that only employees with authorized personnel actions receive compensation.

C. Board Members' Involvement in CUC Hiring Practices

The CUC Board is required by its enabling legislation to appoint an Executive Director to administer CUC's daily operations and both shall manage the corporation in a business-like manner. OPA found, however, that several board members directed the hiring of 17 employees and acted as final approving officials for personnel hiring. This occurred because the Board apparently interpreted its role to go beyond policy and oversight. As a result, the Board's hiring actions usurped management's role in efficiently and effectively operating the corporation as CUC may not have hired the most qualified individuals.

The CUC Act authorizes the CUC Board to appoint an Executive Director to administer daily operations. More specifically, 4 CMC §8133(a) states that:

The board shall appoint an executive director to administer the operations of the corporation on behalf of the board....

This means that the Board should entrust management with daily operations, including hiring, to the Executive Director. Further, CUC's Personnel Manual, adopted by the Board, gives the Executive Director authority to hire employees.

OPA found that several board members, however, were involved in CUC's daily operations, particularly in the hiring of CUC employees. To illustrate:

- *Board members directed the hiring of CUC employees.* Records and interviews showed that CUC board members directed the hiring of 17 employees as follows: 7 employees were hired under limited term appointments, 5 employees were hired under provisional appointments, and 5 employees were hired under job vacancy announcements. According to CUC division managers, 10 employees were hired based on direct instructions from the Board. Also, the Budget Request forms showed that 7 employees were hired under limited term and provisional appointments per the Board's request. In addition, 2 of the 5 employees whose positions were advertised subsequently failed the written examination but were instead directed to be hired by the Board.
- *Board members as final approving officials for personnel hiring.* In December 2000, the Board established two committees, each chaired by a board member, to administer final personnel hiring approvals. Accordingly, the chairperson of the Finance & Budget Committee now has final approval of funding for the salary of any new position, and the

chairperson of the Board Personnel Committee now has final approval over selection of applicants.

Much of the Board's involvement occurred during the first 10 months of Fiscal Year 2001 when CUC lacked a human resources manager. During that time, the Board was directly involved in daily hiring actions and also institutionalized the Board Chairman's involvement through the two committees cited above. The Board apparently interpreted its role as going beyond policy and oversight to one of directly managing hiring activities.

The Board's hiring of 12 employees non-competitively and the hiring of 2 employees despite their failing a written examination may have resulted in CUC not hiring the most qualified employees. Also, the Board's directing that division managers hire employees under limited term or provisional appointments may have resulted in CUC hiring employees who were not needed. Finally, such actions usurp management's role in efficiently and effectively operating CUC.

D. Absence of Compensation, Wage and Salary Scale

CUC may adopt a salary schedule as established pursuant to PL 6-23 for autonomous agencies, or alternatively it may, according to its enabling legislation, set its own compensation, wage, and salary scales whereupon it must submit it to the Legislature with changes from time to time.

Because CUC has neither adopted a salary schedule as established for autonomous agencies nor established its own compensation, wage, and salary scale, OPA believes CUC has no consistent basis for setting salaries and no assurance that its employees are fairly compensated. OPA found that the beginning salaries of 88 employees reviewed were instead based on: (1) salaries of the employees vacating the position, (2) internal memoranda issued either by the Board or the Executive Director, (3) an amount determined by a former financial analyst and requesting officials, or (4) a reference to CNMI's Classification and Compensation Index. According to CUC officials, CUC is currently establishing its own classification and compensation schedule.

CONCLUSION AND RECOMENDATIONS

OPA found that CUC failed to develop and adopt comprehensive personnel rules and regulations based on the merit system. As a result, CUC hired 40 employees non-competitively from October 1, 1999, through July 15, 2001. Although CUC has its own Personnel Manual, this manual does not address personnel practices such as limited term and provisional appointments. Also, 5 CUC employees who were hired non-competitively worked beyond their terms and continued to be compensated without authorized personnel actions. In addition, CUC board involvement in hiring CUC employees has served to usurp management's role in daily operations. Furthermore, CUC did not establish a classification and compensation scale as required, and

therefore has no assurance that employees are fairly compensated. Finally, the absence of a permanent human resources manager may have contributed to CUC's failure to implement a merit based personnel system.

Accordingly, we recommend that CUC:

- 1) Continue the effort to develop and adopt comprehensive personnel rules and regulations. If it determines that limited term appointments are necessary for CUC operations, it should define this practice in the proposed personnel regulations.
- 2) Continue the effort to develop and adopt CUC's own Classification and Compensation Schedule and transmit it to the Legislature for review or adopt the salary scale applicable to autonomous agencies to ensure that its employees are fairly compensated.
- 3) Strongly consider hiring a qualified permanent human resources manager to ensure that CUC follows the merit system and to help CUC implement a comprehensive personnel manual.
- 4) Develop a control procedure that ensures that all CUC employees receiving compensation have authorized personnel actions.

Finally we recommend that:

- 5) the Chairman of the Board issue a directive to ensure that board members focus on policy matters and leave personnel hiring to the Executive Director and the human resources manager.

Commonwealth Utilities Corporation Response

In its response dated December 10, 2002, (**Appendix A**), CUC agreed with two of the recommendations in the draft report and did not respond on the remaining three recommendations. The details are as follows:

Recommendation 1 - CUC agreed with this recommendation and stated that it is in the process of developing its own Human Resource Policies and Procedures that will be adopted at its next board meeting. It added that once the Board has adopted the policy, a copy will be provided to the Office of the Attorney General for review and will subsequently be published in the Commonwealth Register for public comment. A copy of the draft policies and procedures was also provided to us.

Recommendation 2 - CUC agreed with this recommendation and stated that it is in the process of developing its own Classification and Compensation System. CUC added that the Board intends to adopt this system by January 2, 2003.

Recommendations 3, 4 and 5 - CUC did not respond to these three recommendations.

OPA Comments

We commend CUC for its action in addressing two of our recommendations. The planned adoption of its Human Resources Policies and Procedures as well as its Classification and Compensation System will be a significant achievement in improving control over processing of personnel documents to comply with the merit personnel system mandated by law and in providing guidelines to ensure that CUC employees are fairly compensated.

Based on CUC's response, we consider Recommendations 1 and 2 resolved pending adoption of its Human Resources Policies and Procedures as well as its Classification and Compensation System. Recommendations 3, 4 and 5 are considered open as CUC did not respond to these three recommendations.

The additional information or action required to close the recommendations is presented in **Appendix B**.

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Our office has implemented an audit recommendation tracking system. All audit recommendations will be included in the tracking system as open or resolved until we have received evidence that the recommendations have been implemented. An *open* recommendation is one where no action or plan of action has been made by the client (department or agency). A *resolved* recommendation is one in which the auditors are satisfied that the client cannot take immediate action, but has established a reasonable plan and time frame of action. A *closed* recommendation is one in which the client has taken sufficient action to meet the intent of the recommendation or we have withdrawn it.

Please provide us the status of recommendation implementation within 30 days along with documentation showing the specific actions taken. If corrective actions will take longer than 30 days, please provide us additional information every 60 days until we notify you that the recommendation has been closed.

Sincerely,

Michael S. Sablan
Public Auditor, CPA

cc: Governor
Lt. Governor
Thirteenth CNMI Legislature (27 copies)
Comptroller, Commonwealth Utilities Corporation
Secretary of Finance
Special Assistant for Management and Budget
Attorney General
Press Secretary

**Commonwealth Utilities Corporation
Audit of Personnel Hiring from October 9, 1999 Through July 15, 2001**

STATUS OF RECOMMENDATIONS

Recommendations	Agency to Act	Status	Agency Response/ Action Required
1. Continue the effort to develop and adopt comprehensive personnel rules and regulations. If it determines that limited term appointments are necessary for CUC operation, it should define its practice in the proposed personnel regulations.	CUC	Resolved	CUC agreed with Recommendations 1 and 2, and stated that it is developing its own Human Resources Policies and Procedure that will be adopted at its next board meeting. It added that once the Board has adopted the policy, a copy will be provided to the Office of the Attorney General for review and will subsequently be published in the Commonwealth Register for public comment. CUC also stated that it is developing its own Classification and Compensation System and that the Board intends to adopt this system by January 2, 2003.
2. Continue the effort to develop and adopt CUC's own Classification and Compensation Schedule and transmit it to the Legislature for review or adopt the salary scale applicable to autonomous agencies to ensure that its employees are fairly compensated.	CUC	Resolved	Further Actions Needed CUC should provide OPA a copy of the adopted Human Resource Policies and Procedures and Classification and Compensation System.
3. Strongly consider hiring a qualified permanent human resource manager to ensure that CUC follows the merit system and to help CUC implement a comprehensive personnel manual.	CUC	Open	CUC did not respond to recommendations 3, 4 and 5.
4. Develop a control procedure to ensure that all CUC employees receiving compensation have authorized personnel actions.	CUC	Open	
5. The Chairman of the Board issue a directive to ensure that board members focus on policy matters and leave personnel hiring to the Executive Director and the human resources manager.	CUC	Open	