

PUBLIC SCHOOL SYSTEM

**INDEPENDENT AUDITOR'S REPORT
AND
FINANCIAL STATEMENTS**

Year Ended September 30, 2013

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

COMPREHENSIVE ANNUAL FINANCIAL REPORT

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September 30, 2013

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**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**
(A Component Unit of the CNMI Government)

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INDEPENDENT AUDITOR'S REPORT

To the State Board of Education of the
Commonwealth of the Northern Mariana Islands
Public School System

Report on the Financial Statements

I have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Commonwealth of the Northern Mariana Islands Public School System (PSS), as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise PSS' basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

My responsibility is to express opinions on these financial statements based on my audit. I conducted my 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 I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, I express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of PSS, as of September 30, 2013, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 4 through 17 and page 23 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. I have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge I obtained during my audit of the basic financial statements. I do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise PSS' basic financial statements. The combining nonmajor fund financial statements and the Schedule of Expenditures/Expense, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards 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 also not a required part of the basic financial statements.

The combining nonmajor fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In my opinion, the combining nonmajor fund financial statements and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, I have also issued my report dated May 15, 2014, on my consideration of PSS' internal control over financial reporting and on my 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 my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering PSS' internal control over financial reporting and compliance.


Saipan, Commonwealth of the Northern Mariana Islands
May 15, 2014



COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS



STATE BOARD OF EDUCATION
PUBLIC SCHOOL SYSTEM
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SAIPAN, MP 96950

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This section of the CNMI Public School System financial report represents management's discussion and analysis of the financial performance of PSS for the year ended September 30, 2013. Because the intent of this management discussion and analysis is to look at financial performance as a whole, readers should also review the financial statements and notes to the basic financial statements to further enhance their understanding of PSS' financial performance.

FINANCIAL HIGHLIGHTS

At the close of Fiscal year 2013, PSS' net position amounted to \$50,171,249, a decrease of \$2,462,223, from \$52,633,472 in fiscal year 2012. This decrease was primarily due to excess expenses over revenues which resulted to increase in payable to the retirement fund by \$689,157 and payable to the Commonwealth Utilities Corporation by \$1,490,222, excluding penalties. PSS total expenses for fiscal year 2013 amounted to \$63,762,359 with aggregate support from Federal Agencies, CNMI appropriations and other revenues of only \$60,559,808.

PSS' net position includes investment in capital assets, net of accumulated depreciation, of \$80,458,805, capital improvement projects in-progress of \$1,051,447, restricted for special purpose of \$1,087,689 and a deficit of \$32,426,692.

PSS' enrollment of for school year 2012-2013 was 10,107 students. There was a 398 decrease from 10,505, students for school year 2011-2012.

OVERVIEW OF THE FINANCIAL STATEMENTS

Government Accounting Standards requires the presentation of the MD&A and the basic financial statements. The basic financial statements consist of district-wide statements, fund financial statements, notes to the financial statements, and required supplemental sections.

Management Discussion and Analysis (MD&A)

The MD&A is intended to be a "plain English" narrative section that introduces the basic financial statements. It should give readers an objective and easily readable analysis of PSS' financial performance for the year.

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**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

District-wide Statements

The first two financial statements presented are highly condensed and are somewhat based on the accounting model used by private sector businesses. The district-wide statements are presented on the full accrual basis of accounting and include the Statement of Net Position and the Statement of Activities.

Statement of Net Position

The Statement of Net Position includes all of the CNMI Public School System assets and liabilities. Assets and liabilities are classified in the order of relative liquidity for assets and due date for liabilities. This Statement provides a summary of the school system's investment in assets and obligations to creditors. Liquidity and financial flexibility can be evaluated using the information contained in this Statement.

Net position, which is the difference between the school system's assets plus deferred outflows of resources and liabilities plus deferred inflows of resources, is one way to measure the district's financial health or position. Over time, increases or decreases in PSS' net position are an indicator of whether its financial position is improving or deteriorating.

Statement of Activities

The Statement of Activities summarizes the school system's revenues and expenses for the current year. It is based on full accrual accounting rather than the traditional modified accrual. Depreciation of capital assets is recognized as an expense. A net revenue (expense) format is used to indicate to what extent each function is self-sufficient.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

Governmental-fund Financial Statements

The second type of statement included in the basic financial statements is the Governmental-fund Financial Statement, which is presented for the school system's governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the district-wide financial statements. However, unlike the district-wide financial statements, governmental-fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year for spending in future years. Such information may be useful in evaluating a government's near-term financing requirements.

These funds are reported using the modified accrual method of accounting, which measures cash and all other financial assets that can be readily converted to cash. Governmental-fund financial statements provide a detailed short-term view of the school district's operations and the services it provides. Because the focus of governmental funds is narrower than that of the district-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund *balance sheet* and the *governmental fund statement of revenues, expenditures, and changes in fund balance* provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The fund financial statements provide more detailed information about the school system's funds, focusing on its most significant or "major" funds - not the school system as a whole. Funds are accounting devices the school system use to keep track of specific sources of funding and spending on particular programs.

PSS' major funds are:

General Fund - Accounts for all financial resources except for those required to be accounted for in another fund. The General Fund is PSS' major operating fund.

Federal Fund - Accounts for PSS' Grants from Federal Agencies.

Non-major Funds - Accounts for the proceeds of the other specific revenue sources and the other funds that are not major.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

Condensed Statement of Net Position

| | Governmental Activities | | | |
|---|--------------------------|--------------------------|---------------------------|------------|
| | 2013 | 2012 | Difference | % Change |
| Current assets | \$ 5,740,906 | \$ 8,888,543 | \$ (3,147,637) | (35.41) |
| Capital improvement projects in-progress (CIP) | 1,051,447 | 1,890,803 | (839,356) | (44.39) |
| Capital assets, net | <u>80,458,805</u> | <u>81,033,173</u> | <u>(574,368)</u> | (0.71) |
| Total assets | <u>\$ 87,251,158</u> | <u>\$ 91,812,519</u> | <u>\$ (4,561,361)</u> | (4.97) |
| Current liabilities | \$ 10,623,375 | \$ 12,816,032 | \$ (2,192,657) | (17.11) |
| Noncurrent liabilities | <u>25,162,535</u> | <u>24,823,165</u> | <u>339,370</u> | 1.37 |
| Total liabilities | <u>\$ 35,785,910</u> | <u>\$ 37,639,197</u> | <u>\$ (1,853,287)</u> | (4.92) |
| Deferrred inflows of resources | <u>\$ 1,293,999</u> | <u>\$ 1,539,850</u> | <u>\$ (245,851)</u> | (15.97) |
| Investment in capital assets | \$ 80,458,805 | \$ 81,033,173 | \$ (574,368) | (0.71) |
| Investment in CIP | 1,051,447 | 1,890,803 | (839,356) | (44.39) |
| Restricted for special purpose | 1,087,689 | 1,095,886 | (8,197) | (0.75) |
| Deficit | <u>(32,426,692)</u> | <u>(31,386,390)</u> | <u>(1,040,302)</u> | 3.31 |
| Net position | <u>\$ 50,171,249</u> | <u>\$ 52,633,472</u> | <u>\$ (2,462,223)</u> | (4.68) |

| | Governmental Activities | | | |
|---|-------------------------|----------------------|-----------------------|----------|
| | 2012 | 2011 | Difference | % Change |
| Current assets | \$ 8,888,543 | \$ 14,153,501 | \$ (5,264,958) | (37.20) |
| Capital improvement projects in-progress (CIP) | 1,890,803 | 1,890,803 | - | - |
| Capital assets, net | <u>81,033,173</u> | <u>82,757,685</u> | <u>(1,724,512)</u> | (2.08) |
| Total assets | <u>\$ 91,812,519</u> | <u>\$ 98,801,989</u> | <u>\$ (6,989,470)</u> | (7.07) |
| Current liabilities | \$ 14,355,882 | \$ 17,162,563 | \$ (2,806,681) | (16.35) |
| Noncurrent liabilities | <u>24,823,165</u> | <u>21,347,569</u> | <u>3,475,596</u> | 16.28 |
| Total liabilities | <u>\$ 39,179,047</u> | <u>\$ 38,510,132</u> | <u>\$ 668,915</u> | 1.74 |
| Investment in capital assets | \$ 81,033,173 | \$ 82,757,685 | \$ (1,724,512) | (2.08) |
| Investment in CIP | 1,890,803 | 1,890,803 | - | - |
| Restricted for special purpose | 1,095,886 | 1,109,228 | (13,342) | (1.20) |
| Deficit | <u>(31,386,390)</u> | <u>(25,465,859)</u> | <u>(5,920,531)</u> | 23.25 |
| Net position | <u>\$ 52,633,472</u> | <u>\$ 60,291,857</u> | <u>\$ (7,658,385)</u> | (12.70) |

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

- Current assets of \$5,740,906 as of September 30, 2013 decreased by \$3,147,637 compared to \$8,888,543 as of September 30, 2012 due to the collection of receivables from federal grantor agencies. Collections were subsequently used to payoff payables to vendors and contractors.
- Two construction contracts were completed in fiscal year 2013 and subsequently transferred to fixed assets
- The decrease in capital assets is primarily due to depreciation expense.
- Current liabilities of \$10,623,375 as of September 30, 2013 decreased by \$2,192,657 compared to \$12,816,032 as of September 30, 2012 due to payments to vendors and contractors. The majority of the payables outstanding as of September 30, 2013 pertains to utilities payable to the Commonwealth Utilities Corporation amounting to \$4,975,781 (excluding penalties) and compensated absences due in one year amounting to \$1,141,747.
- Noncurrent liabilities, which consist primarily of the unfunded payable to the Northern Mariana Islands Retirement Fund (Retirement Fund) increased, increased by \$339,370. This is because the appropriation received by the PSS was not sufficient to meet PSS current obligations to the Retirement Fund.
- Deferred inflows of resources pertains to monies received from federal and local sources decreased by \$245,851.
- Overall deficit increased by \$1,040,302 or 3.31% from \$31,386,390 in 2012 to \$32,426,692 in 2013. This means that for PSS to pay all its creditors, including the Retirement Fund, PSS needs \$32,426,692. PSS as a public school does not generate its own revenue and relies heavily upon grants and appropriations to finance its current operations and to pay its past obligations. If the level of appropriation continue to drop, it would not be sufficient to finance current operations and the deficit will continue to increase.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

Condensed Statements of Activities

| | Governmental Activities | | | |
|--------------------------|-------------------------|----------------------|-----------------------|----------|
| | 2013 | 2012 | Difference | % Change |
| Revenues: | | | | |
| Program revenues | \$ 29,538,995 | \$ 33,345,815 | \$ (3,806,820) | (11.42) |
| General revenues | <u>31,020,813</u> | <u>31,439,537</u> | <u>(418,724)</u> | (1.33) |
| | <u>60,559,808</u> | <u>64,785,352</u> | <u>(4,225,544)</u> | (6.52) |
| Expenses: | | | | |
| Instruction | 57,458,511 | 58,446,697 | (988,186) | (1.69) |
| Support services | <u>6,069,833</u> | <u>13,997,040</u> | <u>(7,927,207)</u> | (56.63) |
| | <u>63,528,344</u> | <u>72,443,737</u> | <u>(8,915,393)</u> | (12.31) |
| Change in net position | (2,968,536) | (7,658,385) | 4,689,849 | (61.24) |
| Prior year restatement | 506,313 | - | 506,313 | - |
| Net position - beginning | <u>52,633,472</u> | <u>60,291,857</u> | <u>(7,658,385)</u> | (12.70) |
| Net position - ending | <u>\$ 50,171,249</u> | <u>\$ 52,633,472</u> | <u>\$ (2,462,223)</u> | (4.68) |

| | Governmental Activities | | | |
|--------------------------|-------------------------|----------------------|-----------------------|----------|
| | 2012 | 2011 | Difference | % Change |
| Revenues: | | | | |
| Program revenues | \$ 33,345,815 | \$ 58,888,052 | \$ (25,542,237) | (43.37) |
| General revenues | <u>31,439,537</u> | <u>29,354,159</u> | <u>2,085,378</u> | 7.10 |
| | <u>64,785,352</u> | <u>88,242,211</u> | <u>(23,456,859)</u> | (26.58) |
| Expenses: | | | | |
| Instruction | 58,446,697 | 69,059,544 | (10,612,847) | (15.37) |
| Support services | <u>13,997,040</u> | <u>27,547,168</u> | <u>(13,550,128)</u> | (49.19) |
| | <u>72,443,737</u> | <u>96,606,712</u> | <u>(24,162,975)</u> | (25.01) |
| Change in net position | (7,658,385) | (8,364,501) | 706,116 | (8.44) |
| Net position - beginning | <u>60,291,857</u> | <u>68,656,358</u> | <u>(8,364,501)</u> | (12.18) |
| Net position - ending | <u>\$ 52,633,472</u> | <u>\$ 60,291,857</u> | <u>\$ (7,658,385)</u> | (12.70) |

- The overall decrease in revenues and related expenses is due the American Recovery and Reinvestment Act (ARRA) funding provided in fiscal year 2012.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

Revenues

| | <u>2013</u> | <u>2012</u> | <u>Difference</u> | <u>% Change</u> |
|----------------------------------|----------------------|----------------------|-----------------------|-----------------|
| Revenues: | | | | |
| Program revenues: | | | | |
| Charges for services | \$ 1,006,314 | \$ 592,631 | \$ 413,683 | 69.80 |
| Grants and contributions | <u>28,532,681</u> | <u>32,753,184</u> | <u>(4,220,503)</u> | (12.89) |
| Total program revenues: | <u>29,538,995</u> | <u>33,345,815</u> | <u>(3,806,820)</u> | (11.42) |
| General revenues: | | | | |
| Unrestricted CNMI appropriations | 30,239,861 | 29,619,462 | 620,399 | 2.09 |
| Miscellaneous | <u>780,952</u> | <u>1,820,075</u> | <u>(1,039,123)</u> | (57.09) |
| Total general revenues: | <u>31,020,813</u> | <u>31,439,537</u> | <u>(418,724)</u> | (1.33) |
| Total revenues | <u>\$ 60,559,808</u> | <u>\$ 64,785,352</u> | <u>\$ (4,225,544)</u> | (6.52) |

| | <u>2012</u> | <u>2011</u> | <u>Difference</u> | <u>% Change</u> |
|----------------------------------|----------------------|----------------------|------------------------|-----------------|
| Revenues: | | | | |
| Program revenues: | | | | |
| Charges for services | \$ 592,631 | \$ 812,625 | \$ (219,994) | (27.07) |
| Grants and contributions | <u>32,753,184</u> | <u>58,075,427</u> | <u>(25,322,243)</u> | (43.60) |
| Total program revenues: | <u>33,345,815</u> | <u>58,888,052</u> | <u>(25,542,237)</u> | (43.37) |
| General revenues: | | | | |
| Unrestricted CNMI appropriations | 29,619,462 | 28,932,119 | 687,343 | 2.38 |
| Miscellaneous, unrestricted | <u>1,820,075</u> | <u>422,040</u> | <u>1,398,035</u> | 331.26 |
| Total general revenues: | <u>31,439,537</u> | <u>29,354,159</u> | <u>2,085,378</u> | 7.10 |
| Total revenues | <u>\$ 64,785,352</u> | <u>\$ 88,242,211</u> | <u>\$ (23,456,859)</u> | (26.58) |

Total revenues for fiscal year 2013 is \$60,559,808, a \$4,225,544 or 6.52% decrease from fiscal year 2012. The decrease 2013 in revenue is primarily due to decrease in revenue from federal grants.

Total revenues for fiscal year 2012 is \$64,785,352, a \$23,456,859 or 26.58% decrease from fiscal year 2011. The decrease 2012 in revenue is primarily from funding received through the ARRA funds in fiscal year 2011.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

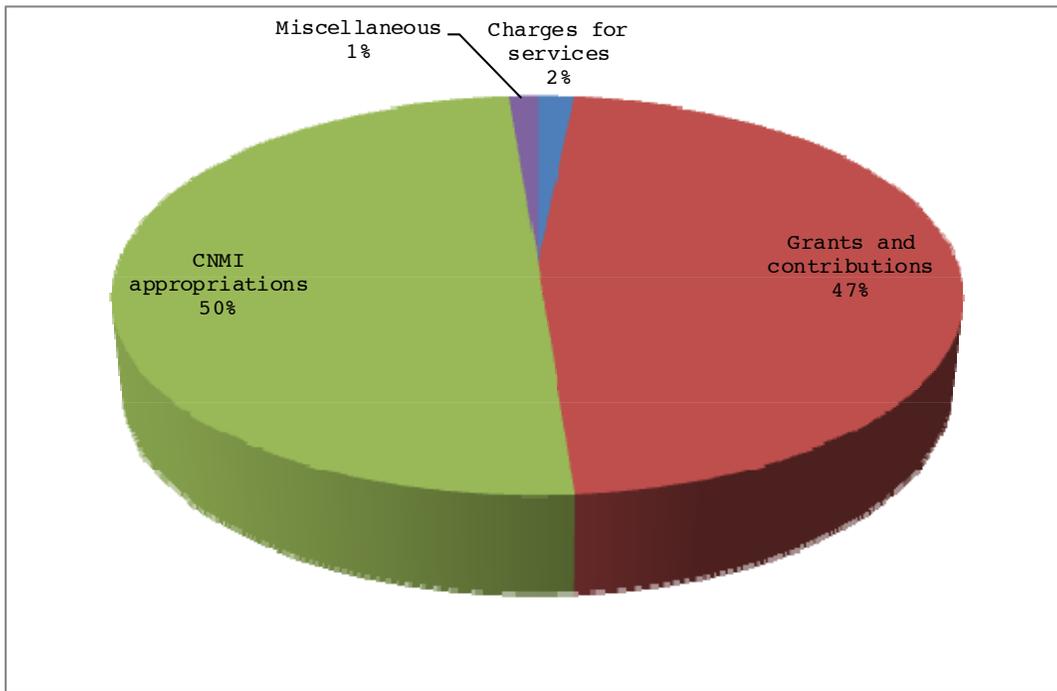
(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

Revenues are classified as either program or general.

Program revenues are those directly generated by a function or activity of the government entity. Revenue reported as program revenues by PSS pertains to Federal grants, local donations, charges for services and indirect costs allocation.

The *general revenue* classification includes appropriations, interest and other income not identifiable to specific activities.



**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

Expenses

Total district-wide expenses by function were as follows:

| | <u>2013</u> | <u>2012</u> | <u>Difference</u> | <u>% Change</u> |
|----------------------------|----------------------|----------------------|---------------------|-----------------|
| Instruction: | | | | |
| Regular | \$ 33,515,406 | \$ 34,421,129 | \$ 905,723 | 2.63 |
| Special education | 8,244,887 | 8,237,442 | (7,445) | (0.09) |
| Co-curricular | 3,606,553 | 3,239,005 | (367,548) | (11.35) |
| Student services | <u>12,091,665</u> | <u>12,549,121</u> | <u>457,456</u> | 3.65 |
| Total instruction | <u>57,458,511</u> | <u>58,446,697</u> | <u>988,186</u> | 1.69 |
| Support services: | | | | |
| General administration | 1,458,537 | 1,698,909 | 240,372 | 14.15 |
| School administration | 1,899,836 | 1,498,630 | (401,206) | (26.77) |
| Other support | 609,089 | 5,005,337 | 4,396,248 | 87.83 |
| Maintenance | 171,382 | 3,282,651 | 3,111,269 | 94.78 |
| Individual programs | 519,352 | 427,230 | (92,122) | (21.56) |
| Depreciation - unallocated | <u>1,411,637</u> | <u>2,084,283</u> | <u>672,646</u> | 32.27 |
| Total support services | <u>6,069,833</u> | <u>13,997,040</u> | <u>7,927,207</u> | 56.63 |
| Total expenses | <u>\$ 63,528,344</u> | <u>\$ 72,443,737</u> | <u>\$ 8,915,393</u> | 12.31 |

| | <u>2012</u> | <u>2011</u> | <u>Difference</u> | <u>% Change</u> |
|----------------------------|----------------------|----------------------|----------------------|-----------------|
| Instruction: | | | | |
| Regular | \$ 34,421,129 | \$ 45,174,554 | \$ 10,753,425 | 23.80 |
| Special education | 8,237,442 | 8,462,886 | 225,444 | 2.66 |
| Co-curricular | 3,239,005 | 2,802,450 | (436,555) | (15.58) |
| Student services | <u>12,549,121</u> | <u>12,619,654</u> | <u>70,533</u> | 0.56 |
| Total instruction | <u>58,446,697</u> | <u>69,059,544</u> | <u>10,612,847</u> | 15.37 |
| Support services: | | | | |
| General administration | 1,698,909 | 2,679,072 | 980,163 | 36.59 |
| School administration | 1,498,630 | 1,700,295 | 201,665 | 11.86 |
| Other support | 5,005,337 | 11,628,731 | 6,623,394 | 56.96 |
| Maintenance | 3,282,651 | 8,951,259 | 5,668,608 | 63.33 |
| Individual programs | 427,230 | 636,537 | 209,307 | 32.88 |
| Depreciation - unallocated | <u>2,084,283</u> | <u>1,951,274</u> | <u>(133,009)</u> | (6.82) |
| Total support services | <u>13,997,040</u> | <u>27,547,168</u> | <u>13,550,128</u> | 49.19 |
| Total expenses | <u>\$ 72,443,737</u> | <u>\$ 96,606,712</u> | <u>\$ 24,162,975</u> | 25.01 |

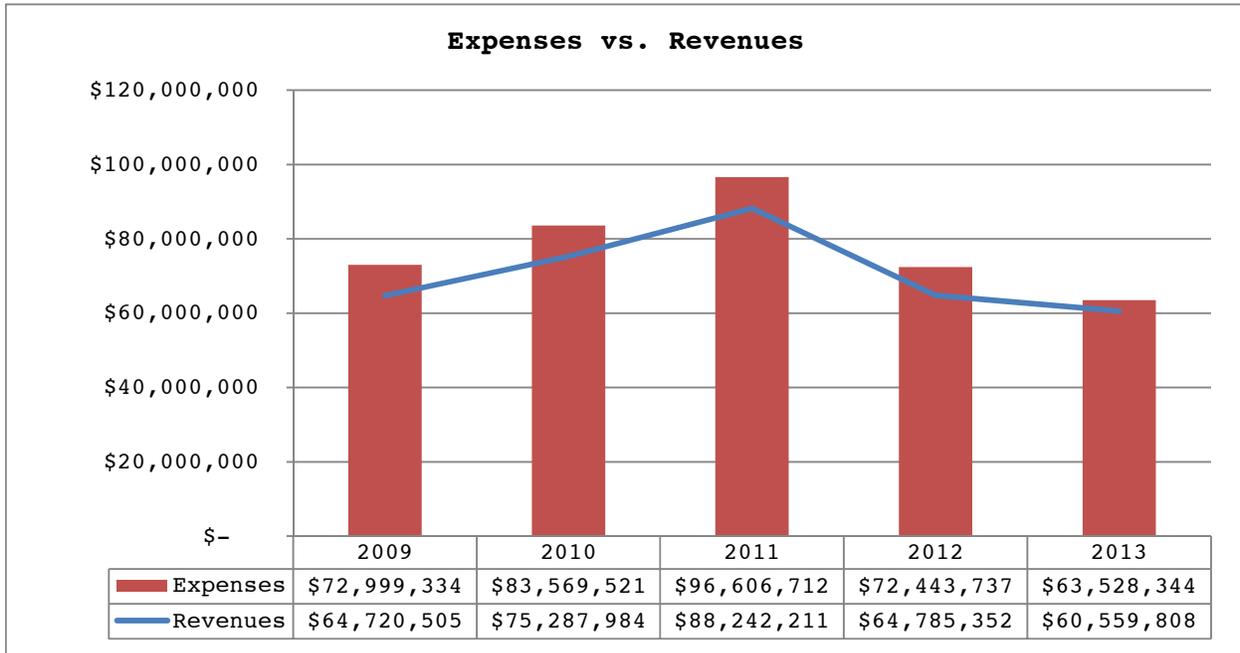
Total expenses in 2013 decreased by \$8,915,393 or 12.31% as compared to fiscal year 2012. The significant decrease in fiscal year 2013 is due to decrease in expenditures authorized through the federal funding.

Total expenses in 2012 decreased by \$24,162,975 or 25.01% as compared to fiscal year 2011. The significant decrease in fiscal year 2012 is due to expenditures authorized through the funding from ARRA in 2011. The ARRA funds afforded the PSS with funding for staff development and training, improvement in instruction materials, improvements and maintenance of the facilities and equipment.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013



The chart above shows the relationship of revenues and expenses for the past five years. The expenses exceeded revenues in all five years which contributed to PSS deficit of \$32,426,692 as of September 30, 2013.

FUND ANALYSIS

| | FUND ANALYSIS | | | |
|---|----------------|--------------|----------------|----------------|
| | General Fund | Federal Fund | Non Major Fund | Total |
| Fund balance (Deficit), beginning of year | \$ (5,977,438) | \$ 984,186 | \$ 573,832 | \$ (4,419,420) |
| Fund balance (Deficit), end of year | (6,648,181) | 984,202 | 629,258 | (5,034,721) |
| Change in fund balance (deficit) | \$ (670,743) | \$ 16 | \$ 55,426 | \$ (615,301) |
| Percentage change | 11% | 0% | 10% | 14% |

The General Fund deficit continues to increase due to the accrual of unappropriated expenses. Included in these unappropriated expenses are the significant portion of the schools' utilities.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

BUDGETARY ANALYSIS

| | General Fund | | | | Variance Favorable (Unfavorable) |
|--|-------------------|----------------|--------------------|----------------------|--|
| | Budget | | Final | Actual | |
| | Original | Revision | | | |
| EXPENDITURES: | | | | | |
| Personnel | \$ 26,751,308 | \$ - | \$26,751,308 | \$26,649,956 | \$ 101,352 |
| All other | <u>4,299,729</u> | <u>186,964</u> | <u>4,486,693</u> | <u>5,594,804</u> | <u>(1,108,111)</u> |
| Total expenditures | <u>31,051,037</u> | <u>186,964</u> | <u>31,238,001</u> | <u>32,244,760</u> | <u>(1,006,759)</u> |
| OPERATING TRANSFERS-IN | <u>31,051,037</u> | <u>186,964</u> | <u>31,238,001</u> | <u>31,238,001</u> | <u>-</u> |
| Excess of revenues and other financing sources over expenditures and other financing uses | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$(1,006,759)</u> | <u>\$(1,006,759)</u> |
| RECONCILIATION OF BUDGET TO GAAP BASIS | | | | | |
| 2013 Budget | | | | | |
| Appropriation including Compact Impact funds and Commonwealth Worker Fund | | | | \$31,238,001 | |
| Other income, ASC forfeitures | | | | <u>336,016</u> | |
| Total available appropriation | | | | 31,574,017 | |
| 2012 Expenditure | | | | | |
| Actual (GAAP) | | | \$32,244,760 | | |
| Less 2013 accrual of unappropriated utilities | | | <u>(1,490,222)</u> | <u>30,754,538</u> | |
| Favorable variance | | | | <u>\$ 819,479</u> | |

At initial glance, PSS appears to have over expended its appropriations. This is due to the accrual of unappropriated utilities. If the utilities expense were not recorded, PSS would have a favorable budget balance of \$819,479.

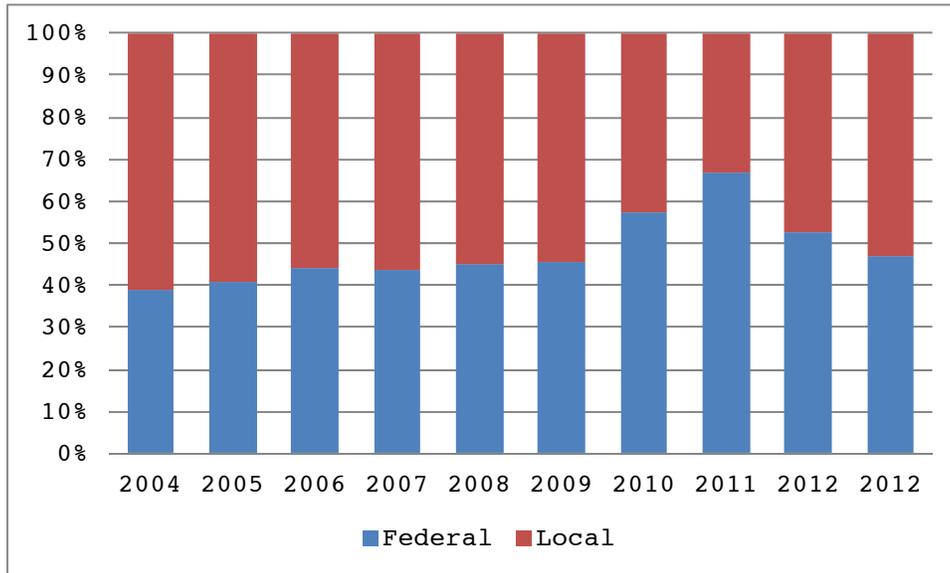
**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

Federal and Local Budget Review

| <u>Year</u> | <u>Total Funding</u> | <u>Federal Funding</u> | | <u>Local Funding</u> | |
|-------------|----------------------|------------------------|----------|----------------------|----------|
| | | <u>Amount</u> | <u>%</u> | <u>Amount</u> | <u>%</u> |
| 2004 | \$60,730,342 | \$23,500,000 | 39% | \$37,230,342 | 61% |
| 2005 | \$63,032,129 | \$25,801,787 | 41% | \$37,230,342 | 59% |
| 2006 | \$66,582,346 | \$29,372,418 | 44% | \$37,209,928 | 56% |
| 2007 | \$65,357,368 | \$28,635,954 | 44% | \$36,721,414 | 56% |
| 2008 | \$65,381,534 | \$29,534,090 | 45% | \$35,847,444 | 55% |
| 2009 | \$63,308,437 | \$28,706,673 | 45% | \$34,601,764 | 55% |
| 2010 | \$72,908,603 | \$41,688,947 | 57% | \$31,219,656 | 43% |
| 2011 | \$87,123,334 | \$58,191,215 | 67% | \$28,932,119 | 33% |
| 2012 | \$62,399,197 | \$32,779,735 | 53% | \$29,619,462 | 47% |
| 2013 | \$60,559,808 | \$28,532,681 | 47% | \$32,027,127 | 53% |



The table and the chart above show the relationship between federal and local funding.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

CAPITAL ASSETS

PSS' investment in capital assets, net of accumulated depreciation, as of September 30, 2013, 2012 and 2011 was \$80,458,805, \$81,033,173 and \$82,757,685, respectively. Depreciation expense for the 2013, 2012 and 2011 was \$2,370,618 and \$2,084,283 and \$1,951,274, respectively.

More detailed information on capital assets is on pages 32 (Note 3) of the basic financial statements.

FUTURE PLANS AND ECONOMIC OUTLOOK

Federal grants have effectively funded quality education initiatives such as the one laptop per student grades 7-12, direct allocation of funds to schools for the purchase of instructional materials and supplies, teacher and school administrator evaluation systems; research-based instructional strategies and classroom best practices; continuous professional development programs; adoption of Common Core State Standards (with rigorous standards in English Language Arts and Math); and system-wide/district-wide accreditation through North Central Accreditation (for all schools, Central Office and Board of Education). To meet student technology needs, laptops are provided to each student from grades 7 to 12 and online courses are provided to assist high school students in meeting their course and graduation requirements. We can project that these federal initiatives will continue.

The challenge for the PSS includes a declining local investment in public education that is now approximately \$3,000 per student. This level of funding is not conducive in fully supporting the vision, mission, and goals of the Public School System. Moreover, PSS funding levels pale in comparison to other US School Districts. Six out of every ten children attending our public schools come from families with incomes below the federal poverty guideline. The CNMI economy has declined from 2.7 billion in business gross receipts in 1997 to less than \$1 billion two years ago. The economic and population trends continue on a downward spiral. Yet, student achievement continues to grow with 65% of our graduating seniors planning to attend college, 30% joining the military and the rest hoping to find a job in the local economy or be a homemaker. These positive outcomes, despite the immense funding challenges faced by PSS, are a testament to the determined and innovative efforts of the PSS team. If given more funding, more results and outputs can be realized.

PSS continues to pursue a fair annual appropriation from the CNMI Government that meets or exceeds the annual maintenance of effort requirement (MOE) of the federal government. The PSS would also like to hire a few more teachers, reduce class sizes and provide funding for buses, school operations, maintenance and utilities. Given that PSS does not generate revenues, these issues will continue to plague PSS until adequate appropriations are provided.

Despite the existence of these material funding issues, the Public School System is committed to Students First and the pursuit of quality education for all students in the CNMI.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Management's Discussion and Analysis
September 30, 2013

REQUESTS FOR INFORMATION

This report is intended to provide a summary of the financial condition of the Public School System of the Commonwealth of the Northern Mariana Islands. Questions or requests for additional information should be addressed to:

Director of Finance
PO Box 501370
Saipan, MP 96950

<http://www.cnmipss.org/>

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Statement of Net Position
September 30, 2013

ASSETS

Current assets:

| | |
|--------------------------------------|----------------|
| Cash and cash equivalents | \$ 3,184,570 |
| Receivables from the CNMI Government | 1,487,371 |
| Receivables from Federal agencies | 661,463 |
| Other receivables, net | <u>407,502</u> |

Total current assets 5,740,906

Noncurrent assets:

| | |
|--|-------------------|
| Capital improvement projects in-progress | 1,051,447 |
| Capital assets, net | <u>80,458,805</u> |

Total current assets 81,510,252

TOTAL ASSETS 87,251,158

LIABILITIES

Current liabilities:

| | |
|---------------------------------------|------------------|
| Bank overdraft | 4,742 |
| Accounts payable and accrued expenses | 9,476,886 |
| Compensated absences due in one year | <u>1,141,747</u> |

Total current liabilities 10,623,375

Noncurrent liabilities:

| | |
|----------------------------------|------------------|
| Retirement contributions payable | 23,767,066 |
| Compensated absences | <u>1,395,469</u> |

Total noncurrent liabilities 25,162,535

TOTAL LIABILITIES 35,785,910

DEFERRED INFLOWS OF RESOURCES

| | |
|-----------------|------------------|
| Grants received | <u>1,293,999</u> |
|-----------------|------------------|

NET POSITION

| | |
|--|---------------------|
| Investment in: | |
| Capital assets | 80,458,805 |
| Capital improvement projects in progress | 1,051,447 |
| Restricted for special purpose | 1,087,689 |
| Deficit | <u>(32,426,692)</u> |

NET POSITION \$ 50,171,249

See accompanying notes to basic financial statements.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Statement of Activities
For the Year Ended September 30, 2013

| <u>Functions/Programs</u> | <u>Expenses</u> | Program Revenues | | <u>Net</u> |
|--------------------------------------|-------------------------|-------------------------|--------------------------|-------------------------|
| | | <u>Charges for</u> | <u>Operating</u> | <u>(Expenses)</u> |
| | | <u>Services</u> | <u>Grants and</u> | <u>Revenues</u> |
| | | | <u>Contributions</u> | |
| Governmental activities: | | | | |
| Instruction: | | | | |
| Regular | \$33,515,406 | \$ 449,114 | \$ 9,443,804 | \$ (23,622,488) |
| Special education | 8,244,887 | - | 6,643,194 | (1,601,693) |
| Co-curricular | 3,606,553 | - | 1,424,674 | (2,181,879) |
| Student services | <u>12,091,665</u> | <u>-</u> | <u>10,319,186</u> | <u>(1,772,479)</u> |
| Total instruction | <u>57,458,511</u> | <u>449,114</u> | <u>27,830,858</u> | <u>(29,178,539)</u> |
| Support services: | | | | |
| General administration | 1,458,537 | - | - | (1,458,537) |
| School administration | 1,899,836 | 338,602 | 129,965 | (1,431,269) |
| Other support | 609,089 | - | - | (609,089) |
| Maintenance | 171,382 | 171,382 | - | - |
| Individual programs | 519,352 | 47,216 | 571,858 | 99,722 |
| Depreciation - unallocated | <u>1,411,637</u> | <u>-</u> | <u>-</u> | <u>(1,411,637)</u> |
| Total support services | <u>6,069,833</u> | <u>557,200</u> | <u>701,823</u> | <u>(4,810,810)</u> |
| Total governmental activities | <u>\$63,528,344</u> | <u>\$ 1,006,314</u> | <u>\$ 28,532,681</u> | <u>(33,989,349)</u> |
| Unrestricted CNMI appropriations | | | | 30,239,861 |
| Capital contribution | | | | 444,936 |
| Miscellaneous | | | | <u>336,016</u> |
| Subtotal, general revenues | | | | <u>31,020,813</u> |
| Changes in net position | | | | (2,968,536) |
| Prior year restatement | | | | 506,313 |
| Net position, beginning of year | | | | <u>52,633,472</u> |
| Net position, end of year | | | | <u>\$ 50,171,249</u> |

See accompanying notes to basic financial statements.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Balance Sheet
Governmental Funds
September 30, 2013

| | General Fund | Federal Funds | Non-major Funds | Total |
|---|----------------------------|----------------------------|----------------------------|----------------------------|
| <u>ASSETS</u> | | | | |
| Current Assets: | | | | |
| Cash and cash equivalents | \$ 3,184,570 | \$ - | \$ - | \$ 3,184,570 |
| Receivables from CNMI | 1,487,371 | - | - | 1,487,371 |
| Receivables from Federal agencies | - | 661,463 | - | 661,463 |
| Other receivables | 368,544 | 38,958 | - | 407,502 |
| Due from other funds | <u>(2,691,698)</u> | <u>734,364</u> | <u>1,957,334</u> | <u>-</u> |
| TOTAL ASSETS | <u>\$ 2,348,787</u> | <u>\$ 1,434,785</u> | <u>\$ 1,957,334</u> | <u>\$ 5,740,906</u> |
| <u>LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCES</u> | | | | |
| Liabilities: | | | | |
| Bank overdraft | \$ 4,742 | \$ - | \$ - | \$ 4,742 |
| Accounts payable and accrued expenses | <u>8,992,226</u> | <u>325,786</u> | <u>158,874</u> | <u>9,476,886</u> |
| Total liabilities | <u>8,996,968</u> | <u>450,583</u> | <u>1,328,076</u> | <u>10,775,627</u> |
| Deferred Inflows of Resources: | | | | |
| Grants received | <u>-</u> | <u>124,797</u> | <u>1,169,202</u> | <u>1,293,999</u> |
| Total deferred inflows of resources | <u>-</u> | <u>124,797</u> | <u>1,169,202</u> | <u>1,293,999</u> |
| Fund Balances: | | | | |
| Unreserved | <u>(6,648,181)</u> | <u>984,202</u> | <u>629,258</u> | <u>(5,034,721)</u> |
| Total fund balances | <u>(6,648,181)</u> | <u>984,202</u> | <u>629,258</u> | <u>(5,034,721)</u> |
| TOTAL LIABILITIES AND DEFERRED INFLWS OF RESOURCES AND FUND BALANCES | <u>\$ 2,348,787</u> | <u>\$ 1,559,582</u> | <u>\$ 3,126,536</u> | |

Capital assets used in governmental activities
are not financial resources and therefore are
not reported as assets in governmental funds.

| | | |
|--|---------------------|-----------------------------|
| Cost of capital assets | \$ 104,012,253 | |
| Accumulated depreciation | <u>(23,553,448)</u> | 80,458,805 |
| Capital improvement projects | | 1,051,447 |
| Accrual for unfunded retirement contribution | | (23,767,066) |
| Long-term liabilities that are not due and payable in the current period and therefore are not reported as liabilities in the Funds. Long-term liabilities at year-end pertains to: | | |
| Compensated absences | | <u>(2,537,216)</u> |
| Net position - governmental activities | | <u>\$ 50,171,249</u> |

See accompanying notes to basic financial statements.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Statements of Revenues, Expenditures, and Changes in Fund Balance
Governmental Funds
For the Year Ended September 30, 2013

| | General Fund | Federal Funds | Non-major Funds | Total |
|---|-----------------|------------------|--------------------|----------------|
| REVENUES: | | | | |
| Federal | \$ 998,140 | \$ 26,848,236 | \$ 686,305 | \$ 28,532,681 |
| Local | - | - | 620,496 | 620,496 |
| Charges for services | - | - | 385,818 | 385,818 |
| TOTAL REVENUES | 998,140 | 26,848,236 | 1,692,619 | 29,538,995 |
| EXPENDITURES: | | | | |
| Current operations: | | | | |
| Instructional programs: | | | | |
| Regular | 24,196,220 | 8,445,648 | 181,558 | 32,823,426 |
| Special | 1,563,885 | 6,643,194 | 501 | 8,207,580 |
| Co-curricular | 2,017,573 | 875,837 | 686,307 | 3,579,717 |
| Student services | 1,139,503 | 10,319,186 | 22,979 | 11,481,668 |
| Total instructional programs | 28,917,181 | 26,283,865 | 891,345 | 56,092,391 |
| Supporting services: | | | | |
| General administration | 971,691 | - | 480,478 | 1,452,169 |
| School administration | 1,762,728 | 129,965 | - | 1,892,693 |
| Individual programs | - | 434,390 | 84,962 | 519,352 |
| Other | 593,160 | - | 9,026 | 602,186 |
| Total supporting services | 3,327,579 | 564,355 | 574,466 | 4,466,400 |
| Maintenance and capital outlays | - | - | 171,382 | 171,382 |
| TOTAL EXPENDITURES | 32,244,760 | 26,848,220 | 1,637,193 | 60,730,173 |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES | (31,246,620) | 16 | 55,426 | (31,191,178) |
| OTHER FINANCING SOURCES: | | | | |
| Operating transfers-in | 30,239,861 | - | - | 30,239,861 |
| Other income | 336,016 | - | - | 336,016 |
| TOTAL OTHER FINANCING SOURCES | 30,575,877 | - | - | 30,575,877 |
| EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES | (670,743) | 16 | 55,426 | (615,301) |
| FUND BALANCE (DEFICIT), beginning of year | (5,977,438) | 984,186 | 573,832 | (4,419,420) |
| FUND BALANCE (DEFICIT), end of the year | \$ (6,648,181) | \$ 984,202 | \$ 629,258 | \$ (5,034,721) |

See accompanying notes to basic financial statements.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Reconciliation of the Governmental Funds Statements of Revenues, Expenditures
And Changes in Fund Balance with the District-wide Statement of Activities
For the Year Ended September 30, 2013

| | | |
|---|----|-----------|
| Total net changes in fund balances - governmental funds | \$ | (615,301) |
|---|----|-----------|

Amounts reported for governmental activities in the statements of activities is different because of:

| | | |
|--|--|-----------|
| Accrual for unfunded retirement contribution | | (689,157) |
|--|--|-----------|

| | | |
|--------------------------------|--|---------|
| Change in compensated absences | | 255,959 |
|--------------------------------|--|---------|

Capital outlays to purchase or build capital assets are reported in governmental funds as expenditures. However, for governmental activities, those costs are shown in the statements of net assets and allocated over their estimated useful lives as annual depreciation expense in the statements of activities. This is the amount by which capital outlays exceed depreciation in the period.

| | | |
|----------------------|--------------------|--------------------|
| Capital outlays | \$ 450,581 | |
| Depreciation expense | <u>(2,370,618)</u> | <u>(1,920,037)</u> |

| | | |
|--|----|--------------------|
| | \$ | <u>(2,968,536)</u> |
|--|----|--------------------|

See accompanying notes to basic financial statements.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Required Supplementary Information
Statement of Revenues, Expenditures
and Changes in Fund Balance - Budget and Actual
Budget and Actual (GAAP Basis) - General Fund
For the Year Ended September 30, 2013

| | General Fund | | | | Variance Favorable (Unfavorable) |
|--|-----------------------|--------------------|-----------------------|---------------------------|--|
| | Budget | | | Actual | |
| | Original | Revision | Final | | |
| EXPENDITURES: | | | | | |
| Personnel | \$ 26,751,308 | \$ - | \$ 26,751,308 | \$ 26,649,956 | \$ 101,352 |
| All other | <u>4,299,729</u> | <u>186,964</u> | <u>4,486,693</u> | <u>5,594,804</u> | <u>(1,108,111)</u> |
| Total expenditures | <u>31,051,037</u> | <u>186,964</u> | <u>31,238,001</u> | <u>32,244,760</u> | <u>(1,006,759)</u> |
| OPERATING TRANSFERS-IN | <u>31,051,037</u> | <u>186,964</u> | <u>31,238,001</u> | <u>31,238,001</u> | <u>-</u> |
| Excess of revenues and other financing sources over expenditures and other financing uses | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ (1,006,759)</u> | <u>\$ (1,006,759)</u> |
| RECONCILIATION OF BUDGET TO GAAP BASIS | | | | | |
| 2013 Budget | | | | | |
| Appropriation including Compact Impact funds and Commonwealth Worker Fund | | | | \$ 31,238,001 | |
| Other income, ASC forfeitures | | | | <u>336,016</u> | |
| Total available appropriation | | | | 31,574,017 | |
| 2012 Expenditure | | | | | |
| Actual (GAAP) | | | \$ 32,244,760 | | |
| Less 2013 accrual of unappropriated utilities | | | <u>(1,490,222)</u> | <u>30,754,538</u> | |
| Favorable variance | | | | <u>\$ 819,479</u> | |

See accompanying notes to basic financial statements.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM

(A Component Unit of the CNMI Government)

Notes to the Basic Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies

The Commonwealth of the Northern Mariana Islands (CNMI) Public School System (PSS), a component unit of the CNMI, was established as a public non-profit corporation by the CNMI Public Law No. 6-10 (The Education Act of 1988), effective October 25, 1988, and began operations on October 1, 1988.

The PSS basic financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing US GAAP for state and local governments through its pronouncements (Statements and Interpretations).

A. Reporting Entity

PSS, as the state educational agency for pre-school, elementary and secondary education programs in the CNMI, is under the direction of the CNMI Board of Education (BOE), which consists of five voting members elected at-large on a nonpartisan basis: one from Rota, one from Tinian, and three from Saipan. The Commissioner of Education, who is appointed by the Board of Education, is responsible for administering PSS in accordance with applicable laws and BOE policies.

Pursuant to CNMI Constitutional Amendment No. 38, the public education school system is guaranteed an annual budget of not less than fifteen percent (15%) of general fund revenues of the CNMI Government. This budgetary appropriation may not be reprogrammed for other purposes, and any unencumbered fund balance at the end of a fiscal year shall be available for reappropriation.

B. Basis of Presentation

District-wide Statements: The Statement of Net Position and Statement of Activities present information about PSS. These Statements include the overall financial activities of the school system. PSS operates only on governmental funds. It does not have any fiduciary and proprietary funds.

The Statement of Activities presents a comparison between direct expenses and program revenues for each function of PSS' governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Notes to the Basic Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

B. Basis of Presentation, Continued

Indirect expense allocations recorded in the funds have been reversed for the Statement of Activities. Program revenues include (a) fees and charges paid by the recipients of goods or services offered by the programs; and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues.

Fund Financial Statements: A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts, recording cash and/or other financial resources together with all related liabilities and residual equities and balances, and changes therein, which are segregated for the purpose of carrying out specific activities or attaining certain objectives in accordance with the fund's special regulations, restrictions or limitations. The fund financial statements provide information about PSS funds. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column.

PSS reports the following major governmental funds:

General Fund - Accounts for all financial resources except for those required to be accounted for in another fund. The General Fund is PSS' major operating fund.

Federal and ARRA Grants Fund - This fund accounts for activities pertaining to Federal operations grants. The primary revenue source of this fund is grant awards from various Federal agencies

Non-major Funds - Accounts for the proceeds of specific revenue sources (other than expendable trusts or major capital projects) that are legally restricted to expenditures for specified purposes. These were previously reported as Special Revenue Funds.

Specific revenues earmarked to finance particular programs and activities of the Public School System are accounted for in Non-major Funds. A summary of PSS' Non-major Funds as of September 30, 2012 follows:

Local Donations Fund - This fund accounts for activities pertaining to local donations received for specific purposes. The primary revenue source of this fund is donations from private individuals or organizations.

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(1) Summary of Significant Accounting Policies, Continued

B. Basis of Presentation, Continued

CNMI Grants Fund - This fund was established to account for projects that were appropriated without fiscal year limitation by Public Law No. 8-2.

Indirect Costs Fund - This fund, established through directive of the Commissioner of Education, accounts for indirect costs of PSS related to Federal grants.

The PSS has directed that indirect costs of the general fund expended for Federal grant activity be accounted for in a non-major fund and be used for particular programs and activities.

C. Measurement Focus and Basis of Accounting

Basis of accounting refers to the timing of recognition, that is, when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied.

District-wide Fund Financial Statements

The governmental activities in the Statement of Net Position 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. Non-exchange transactions, in which PSS gives (or receives) value without directly receiving (or giving) equal value in exchange, include grants and donations. Revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

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Notes to the Basic Financial Statements
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(1) Summary of Significant Accounting Policies, Continued

C. Measurement Focus and Basis of Accounting, Continued

Government Fund Financial Statements

The governmental funds financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when susceptible to accrual (i.e., when they become both measurable and available). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or 90 days thereafter to be used to pay liabilities of the current period. Expenditures are recorded when the related liability is incurred.

Revenues from other sources are recognized when received. Expenditures are generally recognized in the fiscal year the goods or services are received and the related fund liability is incurred. Debt service expenditures for principal interest on general long-term obligations are recognized when due unless resources have been provided for payment early in the subsequent fiscal year. Prepaid items and inventory purchases are reported as current fiscal year expenditures, rather than allocating cost to the fiscal year when items are used.

Expenditures for claims, judgments, compensated absences and employer retirement contributions are reported as the amount accrued during the fiscal year and normally would not be liquidated with expendable available financial resources. Budgetary encumbrances are not reported as expenditures.

Under the terms of federal grant award agreements, PSS funds certain programs by a combination of specific cost-reimbursement grants and general revenues. Thus, when program expenses are incurred, there are both restricted and unrestricted resources available to finance the program. Expenditures are first applied to restricted resources, when both restricted and unrestricted resources are available.

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(1) Summary of Significant Accounting Policies, Continued

D. Budgetary Data

PSS has no authority to impose taxes to generate revenue. PSS is a dependent school district, as revenue and expenditure authorizations come from the CNMI Legislature. The CNMI Legislative budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America. An annual appropriated budget is adopted by the CNMI Legislature for PSS through an Annual Appropriations Act. Budgets for non-major funds are not included in the Annual Appropriation Act. Budgets for these funds are based upon grant awards received (and are thus non-appropriated). Project-length financial plans are adopted for all capital project funds.

Pursuant to the approved policies and regulations of the Public School System, Policy 3100 outlines PSS' general budgetary procedures. A summary of the key budgetary steps and data reflected in the financial statements are as follows:

1. Program managers and principals submit their budgets to the Commissioner of Education for review and compilation by the Management Committee every October 1.
2. By the fifth working day of November, the Commissioner of Education presents the budget to the Board of Education.
3. From November 15th to December 31st, revisions are made as appropriate and as approved by the BOE.
4. By the first working day of February, the budget is presented to the CNMI Senate, House and the Office of the Governor.

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September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

E. Assets, Liabilities and Position

1. Cash and Cash Equivalents

PSS pools money from several funds to facilitate disbursements and investments to maximize investment income.

For purposes of the Statements of Net Position cash and cash equivalents are defined as cash on-hand, cash in checking and savings accounts, and short-term time certificates of deposit with a maturity date within three months of the date acquired. Time certificates of deposit with original dates greater than ninety-days are to be separately classified on the Statement of Net Position.

2. Capital Assets

Capital assets purchased or acquired with an original cost of \$5,000 or more are reported at historical cost or estimated historical cost. Contributed assets are reported at fair market value as of the date received. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred.

Depreciation expense for all assets is provided for on the straight-line basis over the following estimated useful lives:

| | |
|--------------------------------|---------------|
| Buildings | 20 - 50 years |
| Land and building improvements | 15 years |
| Vehicles | 5 years |
| Others | 3 - 5 years |

3. Compensated Absences

Vested or accumulated vacation leave that is expected to be liquidated with expendable available financial resources is reported as an expenditure and fund liability of the governmental fund that will pay it. Amounts of vested or accumulated vacation leave that are not expected to be liquidated with expendable available financial resources are reported as a non-current liability. The liability as of September 30, 2013 was \$2,537,216. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits.

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(1) Summary of Significant Accounting Policies, Continued

E. Assets, Liabilities, and Fund Equity, Continued

3. Compensated Absences, Continued

An employee cannot carry over to the following calendar year accumulated annual leave in excess of three hundred sixty (360) hours. However, any annual leave accumulated in excess of 360 hours as of the end of the calendar year can be converted to sick leave on the last day of the respective calendar year.

4. Revenues

Revenues are classified as either program or general.

Program revenues are those directly generated by a function or activity of the government entity. Revenue reported as program revenues by PSS pertains to Federal grants, local donations, charges for services and indirect costs allocation.

General revenue classification includes appropriations, interest and other income not identifiable to specific activities.

5. Net Position/Fund Balances

Net position in the district-wide financial statements are classified as investment in capital assets; investment in capital improvement projects in progress; restricted and unrestricted. Restricted net position represent constraints on resources that are either externally imposed by creditors, grantors, contributors, or the laws or regulations of Federal agencies, or imposed by law through state statute.

In the governmental fund financial statements, reservations or restrictions of fund balance represent amounts that are not appropriated, are legally segregated for a specific purpose, or are restricted by the grant agreement. Designations of fund balance represent tentative management plans that are subject to change.

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(1) Summary of Significant Accounting Policies, Continued

E. Assets, Liabilities, and Fund Equity, Continued

6. Inter-fund balances

The inter-fund balances as of September 30, 2013 pertains to unreimbursed advances between the general fund and the other funds.

PSS uses its general fund for all of its disbursements and records due from other funds in the general fund and due to other funds in the funds whose expenses the payments were made.

Funds are transferred from the non-major funds as payments to the general fund when draw downs are received from its grantors.

F. New Accounting Standards

Adopted Pronouncements

PSS adopted the following pronouncements during the fiscal year ended September 30, 2013:

GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*, which is designed to improve financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity*, and No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively.

GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements.

GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position.

Management does not believe that the implementation of these Statement does not have a material effect on the financial statements of PSS.

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(1) Summary of Significant Accounting Policies, Continued

F. New Accounting Standards, Continued

Recent Pronouncements

In March 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012. Management does not believe that the implementation of this Statement will have a material effect on the financial statements of PSS.

In April 2012, GASB issued Statement No. 66, *Technical Corrections – 2012*, which enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implantation of this statement on the financial statements of PSS.

In June 2012, GASB issued Statement No. 67, *Financial Reporting for Pension Plans*, which revises existing guidance for the financial report of most pension plans, and Statement No. 68, *Accounting and Financial Reporting for Pensions*, which establishes new financial reporting requirements for most governments that provide their employees with pension benefits. The provisions in Statement 67 are effective for financial statements for periods beginning after June 15, 2013. The provisions in Statement 68 are effective for fiscal years beginning after June 15, 2014. Management has not yet determined the effect of implementation of these statements on the financial statements of PSS.

In January 2013, GASB issued Statement No. 69, *Government Combinations and Disposals of Government Operations*, which establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term government combinations includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations. This Statement provides specific accounting and financial reporting guidance for combinations in the governmental environment. This Statement also improves the decision usefulness of financial reporting by requiring that disclosures be made by governments about combination arrangements in which they engage and for disposals of government operations. The provisions of Statement 69 are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis. Early application is encouraged. Management has not yet determined the effect of implementation of these statements on the financial statements of PSS.

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Notes to the Basic Financial Statements
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(1) Summary of Significant Accounting Policies, Continued

F. New Accounting Standards, Continued

Recent Pronouncements, Continued

In April 2013, GASB issued Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*. The requirements of this Statement will enhance comparability of financial statements among governments by requiring consistent reporting by those governments that extend nonexchange financial guarantees and by those governments that receive nonexchange financial guarantees. This Statement also will enhance the information disclosed about a government's obligations and risk exposure from extending nonexchange financial guarantees. This Statement also will augment the ability of financial statement users to assess the probability that governments will repay obligation holders by requiring disclosures about obligations that are issued with this type of financial guarantee. The provisions of Statement 70 are effective for financial statements for reporting beginning after June 15, 2013. Earlier application is encouraged. Management has not yet determined the effect of implementation of these statements on the financial statements of PSS.

G. Use of Estimates

The preparation of financial statements in accordance 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.

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(2) Reconciliation of District-wide and Fund Financial Statements

The governmental fund balance sheet includes a reconciliation between fund balance – total governmental funds and net position – governmental activities as reported in the government-wide statement of net position. The net adjustments for 2013 consist of several elements as follows:

A. Explanation of certain differences between the governmental fund and the government-wide statement of net position.

| | |
|--|----------------------|
| Capital assets used in governmental activities are not financial resources and are therefore not reported in the funds: | |
| Total capital assets on district-wide statements in governmental activities column | \$ 104,012,253 |
| Accumulated depreciation | <u>(23,553,448)</u> |
| Net capital assets | 80,458,805 |
| Capital improvement projects | 1,051,447 |
| Accrual for unfunded retirement contribution | (23,767,066) |
| Liabilities that, because they are not due and payable in the current period, do not require current resources to pay and are therefore not recorded in the fund statements: | |
| Compensated absences | <u>(2,537,216)</u> |
| Total adjustment | <u>\$ 55,205,970</u> |

B. Explanation of certain differences between the governmental fund statement of revenues, expenditures, and changes in fund balance and the district-wide statement of activities

The governmental statement of revenues, expenditures and changes in fund balances includes a reconciliation between net changes in fund balances – total governmental funds and changes in net position of governmental activities as reported in the district-wide statement of activities. The total adjustments for 2013 pertain to the following:

| | |
|---|-----------------------|
| Accrual for unfunded retirement contribution | \$ (689,157) |
| Capital outlay expenditures recorded in the Statement of Activities. | 450,581 |
| Change in compensated absences | 255,959 |
| Depreciation expense, the allocation of those assets over their useful lives, that is recorded on the Statement of Activities but not in the Fund Statements. | <u>(2,370,618)</u> |
| Total adjustments | <u>\$ (2,353,235)</u> |

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Notes to the Basic Financial Statements
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(3) Detail Notes on all Funds

Cash and Cash Equivalents

GASB Statement No. 3 previously required government entities to present deposit risks as follows:

Category 1 – Deposits that are federally insured or collateralized with securities held by PSS or its agents in PSS' name.

Category 2 – Deposits that are uninsured but are fully collateralized with securities held by the pledging financial institution's trust department or agent in PSS' name.

Category 3 - Deposits that are collateralized with securities held by the pledging institution's trust department or agent but not in PSS' name and non-collateralized deposit.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosures for deposits falling under Categories 1 and 2 but retained disclosures for deposits under Category 3 that have exposure to custodial risk. PSS does not have a deposit policy for custodial risk.

For purposes of the Statement of Net Position, cash is defined as amounts in demand deposits as well as short-term investments with a maturity date within three months from the date acquired. As of September 30, 2013 total amounts deposited with the Federal Deposit Insurance Corporation (FDIC) insured banks were \$3,068,019. From these deposits, \$500,000 is subject to coverage by FDIC, \$101,133 is deposited in a financial institution not subject to FDIC coverage with the remaining balance exceeding insurable limits. PSS requires collateralization of bank accounts, and the amounts in excess of insurable limits are collateralized by securities owned by the banks. PSS has not experienced any losses on these deposits.

Accounts Receivable

Accounts receivable are amounts due primarily from the CNMI Government and from Federal grantor agencies.

Travel Advances

The Board of Education's policy considers travel advances as loans to the traveler until proper reconciliation of approved travel expenses has been authorized. Travel advances are liquidated upon submission of required travel documents in accordance with PSS' policy.

Travel advances of \$112,823 as of September 30, 2013, included in the Statement of Net Position as part of other receivables, are reported net of an allowance for doubtful accounts of \$539,775.

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(3) Detail Notes on all Funds, Continued

Capital Assets

Capital asset activity for the year ended September 30, 2013 were as follows:

| | <u>Beginning</u> | <u>Additions</u> | <u>Restatement</u> | <u>Retirements</u> | <u>Ending</u> |
|---|----------------------|-----------------------|--------------------|--------------------|----------------------|
| Capital assets not being depreciated: | | | | | |
| Land | \$ 36,647,850 | \$ - | \$ - | \$ - | \$ 36,647,850 |
| Capital assets being depreciated: | | | | | |
| Buildings and improvements | 57,343,300 | 1,284,292 | - | - | 58,627,592 |
| Vehicles | 7,470,824 | - | - | (1,525,195) | 5,945,629 |
| Other | <u>2,045,209</u> | <u>5,645</u> | <u>740,328</u> | <u>-</u> | <u>2,791,182</u> |
| Total capital assets being depreciated | <u>66,859,333</u> | <u>1,289,937</u> | <u>740,328</u> | <u>(1,525,195)</u> | <u>67,364,403</u> |
| Less accumulated depreciation for: | | | | | |
| Buildings and improvements | 14,856,319 | 1,411,637 | - | - | 16,267,956 |
| Vehicles | 5,715,941 | 731,943 | - | (1,525,195) | 4,922,689 |
| Other | <u>1,901,750</u> | <u>227,038</u> | <u>234,015</u> | <u>-</u> | <u>2,362,803</u> |
| Total accumulated depreciation | <u>22,474,010</u> | <u>2,370,618</u> | <u>234,015</u> | <u>(1,525,195)</u> | <u>23,553,448</u> |
| Total capital assets being depreciated, net | <u>44,385,323</u> | <u>(1,080,681)</u> | <u>506,313</u> | <u>-</u> | <u>43,810,955</u> |
| Governmental activity capital assets, net | <u>\$ 81,033,173</u> | <u>\$ (1,080,681)</u> | <u>\$ 506,313</u> | <u>\$ -</u> | <u>\$ 80,458,805</u> |

Capital Improvements Projects in Progress and Related Commitments

Construction in progress and related commitments for the years ended September 30, 2013 are as follows:

| | <u>Beginning</u> | <u>Additions</u> | <u>Retirements</u> | <u>Ending</u> |
|--------------------------|------------------|------------------|--------------------|---------------|
| Construction in Progress | \$ 1,890,803 | \$ 444,936 | \$ (1,284,292) | \$ 1,051,447 |

| | <u>Construction In-progress</u> | <u>Commitment</u> |
|----------------|-------------------------------------|-------------------|
| PSS Facilities | \$ 1,051,477 | \$ 21,039 |

Depreciation expense directly identified to specific functions is charged as a direct expense and depreciation of assets that essentially serves all functions is charged as unallocated depreciation.

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(3) Detail Notes on all Funds, Continued

Retirement Plan

PSS contributes to the Northern Mariana Islands Retirement Fund's (the Fund) defined benefit plan (DB Plan) and defined contribution plan (DC Plan), a cost sharing, and multi-employer plan (the Plan) established and administered by the Fund. The Fund issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the Northern Mariana Islands Retirement Fund, P.O. Box 501247, Saipan, MP, 96950-1247.

GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*, requires employers to record other postemployment benefits (OPEB) expense for their contractually required contributions to the OPEB plan. Except as described in the paragraphs below, PSS has complied with GASB Statement No. 45 by recording OPEB expense based on the statutorily determined contribution rate of the Fund. It is the understanding of the management of PSS that the statutorily determined contribution rate of the Fund incorporates both the pension liability and OPEB liability. GASB Statement No. 45 also requires detailed disclosure of information related to the OPEB plan and the management of PSS was unable to obtain this information from the Fund financial report. The management of PSS is unable to obtain the required disclosures and is of the opinion that such information must be obtained from the Fund. It is the position of the management of PSS that the Fund is solely responsible for disclosure of OPEB information.

Defined Benefit Plan (DB Plan)

The DB Plan provides retirement, disability, security and other benefits to employees of the CNMI Government and CNMI agencies, instrumentalities and public corporations and their spouses and dependents. Benefits are based on the average annual salary of the beneficiary over the term of credited service. Public Law No. 6-17, the Northern Mariana Islands Retirement Fund (NMIRF) Act of 1988, is the authority under which benefit provisions are established. Public Law No. 6-17 was subsequently amended by Public Law Nos. 6-41, 8-24, 8-30, 8-31, 8-39, 9-25, 9-45, 10-8, 10-19, 11-9, 11-95, 13-60, 15-14, 15-70, 15-126, 16-2, 16-36, 17-82 and 18-02.

DB Plan members are required to contribute 6.5% and 9% of their annual covered salary for Class I and Class II members, respectively. On June 14, 2007, Public Law No. 15-70 was enacted to amend the NMIRF Act to improve the DB Plan's fiscal solvency. Public Law No. 15-70 provides for increasing employee contributions to the DB Plan by 1% per year beginning in fiscal year 2008 until reaching 10.5% for Class I members and 11% for Class II members. The actuarially determined contribution rate for the fiscal year ended September 30, 2010 is 72.7215% of covered payroll based on an actuarial valuation as of October 1, 2010 issued in October 2012. The established statutory rate at September 30, 2012 through April 31, 2013 was 60.8686% and 72.7215% thereafter, of covered payroll.

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(3) Detail Notes on all Funds, Continued

Retirement Plan, Continued

PSS contribution to the Fund is at accrued 30% of covered payroll. This is based on a Court Order, requiring the CNMI government and its autonomous agencies to remit contributions to the Fund.

Defined Contribution Plan (DC Plan)

On June 16, 2006, Public Law No. 15-13 was enacted which created the DC Plan, a multiemployer pension plan and is the single retirement program for all employees whose first time CNMI government employment commences on or after January 1, 2007. Each member of the DC Plan is required to contribute to the member's individual account an amount equal to 10% of the member's compensation. PSS is required to contribute to each member's individual account an amount equal to 4% of the member's compensation. The DC Plan by its nature is fully funded on a current basis from employer and member contributions. Members of the DC Plan, who have completed five years of government service, have a vested balance of 100% of both member and employer contribution plus any earnings thereon. With the passage of Public Law 17-82 in September 11, 2011, the membership to the DC Plan became voluntary.

PSS' contributions to the Fund for the years ended September 30, 2013, 2012 and 2011 were \$2,520,886, \$2,358,633 and \$4,255,235, respectively.

Pursuant to Public Law No. 6-41, codified in 1CMC § 8362, any employer who fails to pay or remit contributions as required by this section shall pay a penalty of 10% per month or part thereof for which the contribution remains unpaid, up to a maximum penalty of 25% of the unpaid contribution.

The amount payable to the Retirement fund recognized by PSS totaled to \$23,767,066 as of September 30, 2013. However, the amount due from PSS based on actuarially determined rate including interest amounted to \$39,854,170. Pursuant to the Court Order, PSS only recognized a liability based on the percentage the court ordered PSS to remit to the Fund. PSS believes that the difference of \$16,087,104 is due from the CNMI central government and not from PSS.

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(3) Detail Notes on all Funds, Continued

Medical and Life Insurance Benefits

In addition to providing pension benefits, the CNMI Government also ensures that employees are provided with medical and life insurance benefits. The CNMI Government created the Group Health and Life Insurance Trust Fund ("Trust Fund"), held in trust and administered by the Northern Mariana Islands Retirement Fund (NMIRF). PSS contributes to the Group Health and Life Insurance program. This is open to active employees who work at least 20 hours per week and to retired CNMI Government employees who retire as a result of length of service, disability or age, as well as their dependents. Life insurance coverage is to be provided by a private carrier. Contributions from employees and employers are based on rates as determined by NMIRF Board of Trustees. Employee deductions are made through payroll withholdings.

Federal Grants

Federal grants and assistance awards from various Federal agencies made on the basis of entitlement periods are recorded as revenue when entitlement occurs. Federal reimbursement-type grants are recorded as revenues when the related expenditures or expenses are incurred.

Related Party Transactions

The CNMI Government appropriated \$30,239,861 for PSS' operational use for the fiscal year ended September 30, 2013. Receivables from CNMI Government under the general fund as of September 30, 2013 amounted to \$1,487,371. This was subsequently collected as of December 2014.

At September 30, 2013, amounts payable for utilities expense to the Commonwealth Utilities Corporation (CUC) which is included in accounts payable and accrued expenses in the accompanying Statement of Net Position amounted to \$4,975,781, excluding penalties amounting to \$1,052,027. During the year ended September 30, 2013, total utilities expense to CUC amounted to \$3,826,072.

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Notes to the Basic Financial Statements
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(3) Detail Notes on all Funds, Continued

Non-current Liabilities

Changes in non-current liabilities presented in the Statement of Net Position are as follows:

| | Balance <u>9/30/12</u> | <u>Increase</u> | <u>Decrease</u> | Balance <u>9/30/13</u> | Due in <u>1 Year</u> | <u>Noncurrent</u> |
|----------------------------------|---------------------------|---------------------|-----------------------|---------------------------|-------------------------|----------------------|
| Retirement contributions payable | <u>\$ 23,077,909</u> | <u>\$ 2,520,886</u> | <u>\$ (1,831,729)</u> | <u>\$ 23,767,066</u> | <u>\$ -</u> | <u>\$ 23,767,066</u> |
| Compensated absences | <u>\$ 2,793,175</u> | <u>\$ 1,016,885</u> | <u>\$ (1,272,844)</u> | <u>\$ 2,537,216</u> | <u>\$ 1,141,747</u> | <u>\$ 1,395,469</u> |

PSS uses its general funds to liquidate its accrued compensated absences and to pay for prior year retirement contributions of retiring employees. Management is unable to determine the current portion of the retirement contributions payable since payments are only requested from CNMI Treasurer upon actual retirement.

(4) Deferred Inflows and Deferred Outflows of Resources

In addition to assets, the Statement of Net Position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position or fund balance that applies to a future period(s) and thus, will not be recognized as an outflow of resources (expense/expenditure) until then. PSS does not have any deferred outflows of resources as of September 30, 2013

In addition to liabilities, the Statement of Net Position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position or fund balance that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. As of September 30, 2013, PSS only has one type of deferred inflows of resources arising from grants received with restrictions.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Notes to the Basic Financial Statements
September 30, 2013

(5) Contingencies

CNMI Contributions

A substantial amount of PSS's funding is provided by appropriations from the CNMI Government. PSS is guaranteed an annual budget of not less than fifteen percent (15%) of general revenues of the CNMI Government. The future of PSS is contingent on its ability to continue to obtain CNMI appropriations.

Financial and Compliance Audits

PSS administers significant financial assistance from the Federal Government in the form of grants and entitlements. Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable Federal regulations, including expenditure of resources for eligible purposes. Substantially, all grants are subject to either the Single Audit Act or to financial and compliance audits by the grantor agencies of the Federal Government or their designees.

Disallowances and sanctions as a result of these audits may become liabilities of PSS and the general fund would be liable for the return of such funds. Questioned costs as of September 30, 2013 totaled \$76,584. No liability, which may arise from the ultimate outcome of this matter, has been provided for in the accompanying financial statements.

Lawsuits and Claims

PSS is involved in various legal actions and possible claims arising principally from claims of former employees. The eventual outcome of these matters cannot be reasonably predicted by management and, accordingly, no provisions for any liabilities or potential losses that may result from settlement of these claims have been recorded in the accompanying financial statements.

On July 26, 2012, the CNMI Department of Finance, Division of Revenue and Taxation issued a Final Notice of Intent to Levy and Notice of Right to a Hearing to PSS related to its unpaid withholding taxes for the calendar year ended December 31, 2011. The total unpaid withholding taxes were subsequently paid; however, PSS did not recognize any liability for the assessed penalties and interest amounting to approximately \$1.3 million.

Also, PSS did not recognize as liability the assessed late payment penalty from CUC amounting to \$569,371 as of September 30, 2013.

Sick Leave

It is the policy of PSS to record expenditures for sick leave when the leave is actually taken. Sick leave is compensated time for absence during working hours arising from employee illness or injury. The estimated accumulated sick leave at September 30, 2013 is approximately \$5 million.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM

(A Component Unit of the CNMI Government)

Notes to the Basic Financial Statements
September 30, 2013

(6) Commitments

The accrual basis of accounting provides that expenses include only amounts associated with goods and services received and liabilities include only the unpaid amounts associated with such expenses. Accordingly, \$1,139,159 of outstanding purchase orders and purchase commitments are not reported in the financial statements as of September 30, 2013.

(7) Risk Management

The CNMI government is a self-insured entity. The CNMI government has limited its general liability to individuals to \$100,000 by statute. For this reason, the government does not maintain any insurance on its buildings, or on its employees. At some future date, PSS may insure some of its assets, as an autonomous agency, it is not required to follow the CNMI Government's self-insurance policy. PSS has not experienced any losses for the year ended September 30, 2013.

PSS does require performance bonds on all its building projects financed by the CNMI and Federal Governments.

(8) Economic Dependency

PSS receives a substantial amount of its support from Federal and local governments. In fiscal year ending September 30, 2013, 50% and 47% of total revenues were received from local appropriations and federal grants, respectively. A significant reduction in the level of this support, if this were to occur, may have an adverse effect on PSS' programs and activities.

(9) Fair Value of Financial Instruments

PSS financial instruments are cash and cash equivalents, receivables from CNMI Government and Federal agencies, and payables. The recorded values of these financial instruments approximate their fair values based on their short-term nature.

(10) Restatement

During fiscal year PSS 2013, PSS conducted a physical count of its capital assets and as a result of the reconciliation of the recorded values and capital assets and the physical count, PSS restated net position by \$506,313. See Capital Asset disclosure on page 36.

(11) Subsequent Events

PSS has evaluated subsequent events from October 1, 2013 through May 15, 2014, the date of financial statements were available to be issued. PSS did not note any subsequent events requiring disclosure or adjustment to the accompanying financial statements.

PUBLIC SCHOOL SYSTEM

SUPPLEMENTAL INFORMATION

Year Ended September 30, 2013

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Combining Balance Sheets
Non-major Funds
For the Year Ended September 30, 2013

| | Local CIP Fund ⁽¹⁾ | ARRA Fund (25000) | GOB Fund (30000) | Indirect Cost Fund (40000) | Donation and Other Revenue Fund (42000) | Other Federal Fund (60000) | JROTC Army Fund (65000) | Federal Program Income Fund (66000) | Total Non-major Funds |
|---|-------------------------------------|-------------------------|------------------------|-------------------------------------|--|-------------------------------------|----------------------------------|--|-----------------------------|
| <u>ASSETS</u> | | | | | | | | | |
| Current Assets: | | | | | | | | | |
| Due from (to) other funds | \$ 351,507 | \$ 400,513 | \$ 1,238,278 | \$ 149,668 | \$ (779,137) | \$ 176,668 | \$ 638,778 | \$ (218,941) | \$ 1,957,334 |
| TOTAL ASSETS | <u>351,507</u> | <u>400,513</u> | <u>1,238,278</u> | <u>149,668</u> | <u>(779,137)</u> | <u>176,668</u> | <u>638,778</u> | <u>(218,941)</u> | <u>1,957,334</u> |
| <u>LIABILITIES AND FUND BALANCES</u> | | | | | | | | | |
| Liabilities: | | | | | | | | | |
| Accounts payable and accrued expenses | - | - | 150,588 | (6,716) | 906 | 12,532 | 544 | 1,020 | 158,874 |
| Unearned revenues | <u>409,954</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>6,373</u> | <u>677,761</u> | <u>75,114</u> | <u>1,169,202</u> |
| Total liabilities | <u>409,954</u> | <u>-</u> | <u>150,588</u> | <u>(6,716)</u> | <u>906</u> | <u>18,905</u> | <u>678,305</u> | <u>76,134</u> | <u>1,328,076</u> |
| Fund Balances: | | | | | | | | | |
| Unreserved | <u>(58,447)</u> | <u>400,513</u> | <u>1,087,690</u> | <u>156,384</u> | <u>(780,043)</u> | <u>157,763</u> | <u>(39,527)</u> | <u>(295,075)</u> | <u>629,258</u> |
| Total fund balances | <u>\$ (58,447)</u> | <u>\$ 400,513</u> | <u>\$ 1,087,690</u> | <u>\$ 156,384</u> | <u>\$ (780,043)</u> | <u>\$ 157,763</u> | <u>\$ (39,527)</u> | <u>\$ (295,075)</u> | <u>\$ 629,258</u> |

(1) Fund codes 17000, 18000 and 19000

See accompanying notes to basic financial statements.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Combining Statements of Revenues, Expenditures, and Changes in Fund Balance
Non-major Funds
For the Year Ended September 30, 2013

| | Local CIP Fund(1) | ARRA Fund (25000) | GOB Fund (30000) | Indirect Cost Fund (40000) | Other Revenue Fund (42000) | Federal Fund (60000) | Army Fund (65000) | Program Income Fund (66000) | Total Non-major Funds |
|--|-------------------------|-------------------------|------------------------|----------------------------------|----------------------------------|----------------------------|-------------------------|-----------------------------------|-----------------------------|
| REVENUES: | | | | | | | | | |
| Federal | \$ - | \$ - | \$ - | \$ - | \$ - | \$ 137,468 | \$ 548,837 | \$ - | \$ 686,305 |
| Local | 241,955 | - | - | - | 378,541 | - | - | - | 620,496 |
| Charges for services | - | - | - | 338,610 | - | - | - | 47,208 | 385,818 |
| TOTAL REVENUES | 241,955 | - | - | 338,610 | 378,541 | 137,468 | 548,837 | 47,208 | 1,692,619 |
| EXPENDITURES: | | | | | | | | | |
| Current operations: | | | | | | | | | |
| Instructional programs: | | | | | | | | | |
| Regular | - | - | - | - | 181,558 | - | - | - | 181,558 |
| Special | - | - | - | - | - | - | - | 501 | 501 |
| Co-curricular | - | - | - | - | - | 137,471 | 548,836 | - | 686,307 |
| Student services | - | - | - | - | - | - | - | 22,979 | 22,979 |
| Total instructional programs | - | - | - | - | 181,558 | 137,471 | 548,836 | 23,480 | 891,345 |
| Supporting services: | | | | | | | | | |
| General administration | - | - | - | 443,719 | 36,759 | - | - | - | 480,478 |
| Individual programs | - | - | - | - | 61,233 | - | - | 23,729 | 84,962 |
| Other | 9,026 | - | - | - | - | - | - | - | 9,026 |
| Total supporting services | 9,026 | - | - | 443,719 | 97,992 | - | - | 23,729 | 574,466 |
| Maintenance and capital outlays | 149,843 | - | 21,539 | - | - | - | - | - | 171,382 |
| TOTAL EXPENDITURES | 158,869 | - | 21,539 | 443,719 | 279,550 | 137,471 | 548,836 | 47,209 | 1,637,193 |
| OVER EXPENDITURES | 83,086 | - | (21,539) | (105,109) | 98,991 | (3) | 1 | (1) | 55,426 |
| FUND BALANCE (DEFICIT), beginning of year | (141,533) | 400,513 | 1,109,229 | 261,493 | (879,034) | 157,766 | (39,528) | (295,074) | 573,832 |
| FUND BALANCE (DEFICIT), end of the year | \$ (58,447) | \$ 400,513 | \$ 1,087,690 | \$ 156,384 | \$ (780,043) | \$ 157,763 | \$ (39,527) | \$ (295,075) | \$ 629,258 |

(1) Fund codes 17000, 18000 and 19000

See accompanying notes to basic financial statements.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDSPUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Schedule of Expenditures/Expense (By Natural Classification)
Year Ended September 30, 2013

| | General Fund | Federal Fund | Non-Major Funds | Total Expenditures | Conversion | Total Expenses |
|-------------------------------------|----------------------|----------------------|---------------------|-----------------------|--------------|-------------------|
| Salaries and wages | \$ 22,490,501 | \$ 7,365,701 | \$ 570,800 | \$ 30,427,002 | \$ (255,959) | \$ 30,171,043 |
| Professional services | 223,175 | 11,678,499 | 29,061 | 11,930,735 | | 11,930,735 |
| Employee benefits | 4,159,455 | 1,333,833 | 100,640 | 5,593,928 | 689,157 | 6,283,085 |
| Utilities | 3,738,772 | 67,096 | 20,206 | 3,826,074 | | 3,826,074 |
| Depreciation | - | - | - | - | 2,370,618 | 2,370,618 |
| Travel | 110,500 | 1,468,494 | 398,735 | 1,977,729 | | 1,977,729 |
| Rental | 126,919 | 1,106,546 | 37,506 | 1,270,971 | | 1,270,971 |
| Controlled Assets | 56,913 | 1,071,874 | 26,773 | 1,155,560 | (5,645) | 1,149,915 |
| Books and instruction materials | 4,647 | 910,846 | 14,221 | 929,714 | | 929,714 |
| Supplies and materials | 123,290 | 630,536 | 91,798 | 845,624 | | 845,624 |
| Repairs and maintenance | 209,227 | 164,485 | 192,689 | 566,401 | | 566,401 |
| Communications | 238,081 | 170,626 | 16,663 | 425,370 | | 425,370 |
| Fuel and lubrications | 257,720 | 57,043 | 14,563 | 329,326 | | 329,326 |
| Indirect Costs | - | 289,107 | - | 289,107 | | 289,107 |
| Cleaning Services | 161,310 | 33,669 | 14,269 | 209,248 | | 209,248 |
| Security services | 168,183 | 9,060 | 29,258 | 206,501 | | 206,501 |
| Miscellaneous | 40,903 | 143,757 | 11,613 | 196,273 | | 196,273 |
| Printing and photocopying | 16,566 | 119,618 | 1,770 | 137,954 | | 137,954 |
| Licenses and fees | 18,211 | 86,642 | 6,413 | 111,266 | | 111,266 |
| Dues and subscriptions | 21,421 | 47,611 | 15,033 | 84,065 | | 84,065 |
| Advertising | 4,029 | 70,400 | 8,076 | 82,505 | | 82,505 |
| Food Items | 27,643 | 10,040 | 25,172 | 62,855 | | 62,855 |
| Recruitment and repatriation | 11,292 | 6,989 | 5,987 | 24,268 | | 24,268 |
| Freight and handling | 10,157 | 5,748 | 5,947 | 21,852 | | 21,852 |
| Insurance | 20,969 | - | - | 20,969 | | 20,969 |
| Bank charges | 4,876 | - | - | 4,876 | | 4,876 |
| Total expenditures (page 21) | \$ 32,244,760 | \$ 26,848,220 | \$ 1,637,193 | \$ 60,730,173 | | |

Total expenses (page 19) \$ 63,528,344

See accompanying notes to basic financial statements.

PUBLIC SCHOOL SYSTEM

**REPORTS ON INTERNAL CONTROL
AND COMPLIANCE**

Year Ended September 30, 2013



CERTIFIED PUBLIC ACCOUNTANT

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**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**

To the State Board of Education of the
Commonwealth of the Northern Mariana Islands
Public School System

I have audited, in accordance with the 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, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Commonwealth of the Northern Mariana Islands Public School System as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise PSS' basic financial statements and have issued my report thereon dated May 15, 2014.

Internal Control Over Financial Reporting

In planning and performing my audit of the financial statements, I considered PSS' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing my opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of PSS' internal control. Accordingly, I do not express an opinion on the effectiveness of PSS' internal control.

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. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

My consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during my audit I did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. I did identify certain deficiencies in

internal control, described in the accompanying schedule of findings and questioned costs as Findings 13-01 through 13-04 that I consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether PSS' financial statements are free from material misstatement, I 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 my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as Finding 13-01.

PSS' Response to Findings

PSS' response to the findings identified in my audit is described in the accompanying schedule of findings and questioned costs. PSS' response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, I express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.


Saipan, Commonwealth of the Northern Mariana Islands
May 15, 2014



CERTIFIED PUBLIC ACCOUNTANT

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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM
AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133**

To the State Board of Education of the
Commonwealth of the Northern Mariana Islands
Public School System

Report on Compliance for Each Major Federal Program

I have audited Commonwealth of the Northern Mariana Islands Public School System's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have direct and material effect on each of PSS' major federal programs for the year ended September 30, 2013. PSS' major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

My responsibility is to express an opinion on compliance for each of PSS' major federal programs based on my audit of the types of compliance requirements referred to above. I conducted my 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 I 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 PSS' compliance with those requirements and performing such other procedures as I considered necessary in the circumstances.

I believe that my audit provides a reasonable basis for my opinion on compliance for each major federal program. However, my audit does not provide a legal determination of PSS' compliance.

Basis for Qualified Opinion on CFDA 10.550 National School Lunch Program, CFDA 84.403 Consolidated Grant to the Outlying Areas, CFDA 84.027 Special Education Grants to States and CFDA 93.600 Head Start

As described in the accompanying schedule of findings and questioned costs, PSS did not comply with requirements regarding CFDA Nos. 10.500, 84.403, 84,027 and 93.600 as described in Finding Nos. 13-05, 13-06 and 13-09 for Allowed Costs/Cost Principles; CFDA Nos. 10.500, 84.403 and 84,027 as described in Finding Nos. 13-07 and 13-08 for Procurement and Suspension and Debarment and CFDA 93.600 as described in Finding Nos. 13-10 for eligibility. Compliance with such requirements is necessary, in my opinion, for PSS to comply with the requirements applicable to that program.

Qualified Opinion on CFDA 10.550 National School Lunch Program, CFDA 84.403 Consolidated Grant to the Outlying Areas, CFDA 84.027 Special Education Grants to States and CFDA 93.600 Head Start

In my opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, PSS, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on CFDA 10.550 National School Lunch Program, CFDA 84.403 Consolidated Grant to the Outlying Areas, CFDA 84.027 Special Education Grants to States and CFDA 93.600 Head Start for the year ended September 30, 2013.

Report on Internal Control Over Compliance

Management of PSS, is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing my audit of compliance, I considered PSS internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program 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, I do not express an opinion on the effectiveness of PSS' internal control over compliance.

A *deficiency in 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 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. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

My 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 material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during my audit I did not identify any deficiencies

in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. I did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as Findings 13-03, 13-04 and 13-08 that I consider to be significant deficiencies. PSS' response to the internal control over compliance findings identified in my audit is described in the accompanying schedule of findings and questioned costs. PSS' response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, I express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

J. Scott Magliari & Company

Saipan, Commonwealth of the Northern Mariana Islands
May 15, 2014

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
(A Component Unit of the CNMI Government)

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2013

| <u>Federal Grantor/Program Title</u> | <u>CFDA Number</u> | <u>Expenditures</u> |
|--|--------------------|----------------------|
| <u>U.S. Department of Agriculture</u> | | |
| Direct Program: | | |
| National School Lunch Program | 10.555 | \$ 10,098,315 |
| Total U.S. Department of Agriculture | | <u>10,098,315</u> |
| <u>U.S. Department of Commerce</u> | | |
| Direct Program: | | |
| Public Telecommunications Facilities Planning and Construction | 11.550 | 129,965 |
| Total U.S. Department of Commerce | | <u>129,965</u> |
| <u>U.S. Department of Defense</u> | | |
| Direct Program: | | |
| Army JROTC | 12.Unknown | 548,836 |
| Total U.S. Department of Defense | | <u>548,836</u> |
| <u>U.S. Department of Education</u> | | |
| Direct Program: | | |
| Consolidated Grants to the Outlying Areas | 84.403 | 8,445,282 |
| Special Education - Grants to States (IDEA, Part B) Territories and Freely Associated States Education Grant Program | 84.027 | 4,276,102 |
| Special Education - Grants for Infants and Families Striving Readers | 84.256 | 796,769 |
| Common core | 84.181 | 518,435 |
| | 84.371 | 79,068 |
| | 84.unknown | 371 |
| Total U.S. Department of Education | | <u>14,116,027</u> |
| <u>U.S. Department of Transportation</u> | | |
| Direct Program: | | |
| Formula Grants for Other Than Urbanized Areas | 20.509 | 268,082 |
| Total U.S. Department of Transportation | | <u>268,082</u> |
| Sub-total carried forward | | <u>\$ 25,161,225</u> |

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

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
(A Component Unit of the CNMI Government)

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2013

| <u>Federal Grantor/Program Title</u> | <u>CFDA Number</u> | <u>Expenditures</u> |
|---|--------------------|-----------------------------|
| Sub-total brought forward | | \$ 25,161,225 |
| <u>U.S. Department of Health and Human Services</u> | | |
| Direct Programs: | | |
| Head Start | 93.600 | 1,848,654 |
| Personality Responsibility Education | 93.092 | 103,849 |
| Cooperative Agreements to Support Comprehensive School Health Programs to Prevent the Spread of HIV and Other Important Health Problems | 93.938 | <u>89,139</u> |
| Subtotal Direct Programs | | 2,041,642 |
| Pass-Through the Government of the CNMI: | | |
| Child Care | 93.575 | <u>137,471</u> |
| Total U.S. Department of Health and Human Services | | <u>2,179,113</u> |
| <u>Corporation for National and Community Service</u> | | |
| Direct Program: | | |
| AmeriCorps | 94.006 | <u>241,403</u> |
| Total Corporation for National and Community Service | | <u>241,403</u> |
| <u>U.S. Department of the Interior</u> | | |
| Passed-through the CNMI Government | | |
| Compact impact | 15.875 | <u>498,140</u> |
| Total U.S. Department of the Interior | | <u>498,140</u> |
| <u>U.S. Department of Homeland Security</u> | | |
| Passed-through the CNMI Government | | |
| Commonwealth Worker Fund | 97.unknown | <u>500,000</u> |
| Total U.S. Department of Homeland Security | | <u>500,000</u> |
| Total expenditures | | <u>\$ 28,579,881</u> |
| Reconciliation: | | |
| Expenditures Federal Fund | | \$ 26,848,220 |
| Expenditures included in nonmajor funds | | 686,305 |
| Expenditures included in General Fund | | 998,140 |
| Program income | | <u>47,216</u> |
| Total expenditures | | <u>\$ 28,579,881</u> |

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

COMMONWEALTH OF THE NORTHERN MARIANA ISLAND
PUBLIC SCHOOL SYSTEM
(A Component Unit of the CNMI Government)

Notes to the Schedule of Expenditures of Federal Awards
Year Ended September 30, 2013

(1) Scope of Review

The Public School System (PSS) was established as a public non-profit corporation by the Commonwealth of the Northern Mariana Islands (CNMI) Public Law No. 6-10, effective October 25, 1988 and began operations on October 1, 1988. All significant operations of PSS 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 PSS' cognizant agency for 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

PSS negotiated an indirect cost plan with the U.S. Department of Education for fiscal year 2012. The approved rates are as follows:

| | |
|-----------------|-------|
| Restricted rate | 4.30% |
|-----------------|-------|

The restricted rate is applicable only to U.S. Department of Education programs and is based on total direct costs, less capital expenditures and pass-through funds. Pass-through funds are normally defined as major subcontracts, payments to participants, stipends to eligible recipients and subgrants, all of which normally require minimal administrative effort.

PSS has an unrestricted indirect cost rate that is applicable to all programs except for the U.S. Department of Education programs and is based on total direct salaries and wages, including fringe benefits. The provisional rate is as follows:

| | |
|--------------|-------|
| Unrestricted | 2.04% |
|--------------|-------|

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM

(A Component Unit of the CNMI Government)

Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued: Unmodified

Internal control over financial reporting:

- Material weakness(es) identified? yes no
- Significant deficiency(ies) identified that are not considered to be material weaknesses? yes none reported

Noncompliance material to financial statements noted? yes no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? yes no
- Significant deficiency(ies) identified that are not considered to be material weaknesses? yes none reported

Type of auditor's report issued on compliance: Modified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133? yes no

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**
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Schedule of Findings and Questioned Costs
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SECTION I – SUMMARY OF AUDITOR’S RESULTS, Continued

Federal Awards

Identification of major programs:

| <u>CFDA Number</u> | <u>Description</u> | <u>Federal Expenditures</u> |
|------------------------|---|---------------------------------|
| 10.550 | National School Lunch Program | \$ 10,098,315 |
| 84.403 | Consolidated Grant to the Outlying Areas | 8,445,282 |
| 84.027 | Special Education Grants to States | 4,276,102 |
| 93.600 | Head Start | <u>1,848,654</u> |
| | Total Federal Expenditures–Major Programs | <u>\$ 24,668,353</u> |
| | Percentage of total awards tested | 86% |

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

\$ 857,396

3% of the total awards expended

Auditee qualified as low-risk auditee

 yes X no

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-01, Use of Restricted Cash

Criteria:

In June 1997, CNMI House Joint Resolution No. 10-36 authorized PSS to issue general obligation bonds for a total value not to exceed \$15,685,000. These bonds were used to leverage an equal amount of federal capital improvement project funds to finance school construction projects and will be repaid by the CNMI Government through appropriation of liquid fuel taxes per Public Law No. 11-14. The liability relating to these bonds is recorded by the CNMI Government. In August 2008, Public Law No. 16-10 appropriated funds available at the closure of the Indenture Trust Agreement to fund critical classroom repairs, renovations and the paving of school parking areas at public schools with the Commissioner of Education as expenditure authority.

Condition:

PSS accounts for bond proceeds in the Capital Projects Fund (Fund 30000). At September 30, 2013, adjusted net position of Fund 30000 amounted to \$1,087,689 and accounts payable balance of \$150,589. Fund 30000's cash is held in the restricted bank account recorded in the General Fund, hence Fund 30000 has a interfund receivable of \$1,238,278 as of September 30, 2013.

The restricted account balance as of September 30, 2013 was \$96,302 which is \$1,141,976 less than audited required balance.

Cause:

Due to financial difficulties, PSS used the restricted funds for expenditures not allowed by Public Law No. 16-10.

Effect:

PSS is noncompliance with Public Law 16-10.

Recommendation:

PSS should return the restricted funds used for expenditures not allowed under Public Law 16-10 and ensure that future disbursements from this account comply with its restrictions.

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-01, Use of Restricted Cash, continued

Auditee Response:

Contact Person - Mr. George Palican
Completion Date - September 30, 2014

Due to the Central Government's partial withholding of FY2012 and FY2011 appropriated funds from prior years and the extended delay in settlement of the Maintenance of Effort (MOE) agreement, PSS received prior Board approval to utilize these restricted funds, as a last resort to address urgent financial needs. PSS fully intends to repay these borrowed funds through the execution of a payment plan.

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Schedule of Findings and Questioned Costs
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SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-02, Accrual and Timely reconciliation of CNMI Appropriations

Criteria:

Governmental Fund revenues should be recognized in the accounting period they become susceptible to accrual – that is, when they become *measurable* and *available* to finance expenditure for the fiscal period.

The related receivables should be reconciled to sub-ledger balances and assessed for collectability on a timely basis.

Conditions:

As of September 30, 2013, the general ledger balance of PSS Appropriations receivable was \$4,579,269. This was the September 30, 2012 audited balance.

1. PSS did not properly accrue the appropriations allotments.

From CNMI Government confirmation:

| | |
|--|------------------------|
| Allotment for PSS operations and Board of Education | \$ 30,239,859.76 |
| Commonwealth Workers Fund | 500,000.00 |
| Compact Impact Fund | <u>498,140.00</u> |
| Total | 31,237,999.76 |
| Revenues recognized by PSS | \$ 34,329,899.59 |
| Collections of prior year | |
| Receivable recognized as current | <u>(4,572,363.32)</u> |
| Unrecorded allotments | <u>\$ 1,480,463.49</u> |

2. PSS did not record CNMI transfers to the proper account. Collection of previously accrued appropriation should be posted as reduction to appropriations receivable and not as current period income.

| | |
|--|--------------------------|
| Appropriations receivable as confirmed by the CNMI Department of Finance | \$ 1,480,463.50 |
| Appropriations receivable per PSS general ledger | <u>4,579,269.49</u> |
| Difference | <u>\$ (3,098,805.99)</u> |
| Difference accounted for as: | |
| Collection from prior years recorded as current revenue | \$ 4,572,363.32 |
| Unrecorded appropriations | (1,480,463.49) |
| Difference in 2012 appropriations receivable ending balance against CNMI Government recognized payable | <u>6,906.16</u> |
| | <u>\$ 3,098,805.99</u> |

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-02, Accrual and Timely reconciliation of CNMI Appropriations, Continued

Cause:

PSS did not record a journal entry to recognize appropriation revenue and corresponding receivable upon advise from the CNMI government of the total appropriation. Furthermore, all cash receipts entries for allotment received are recorded as current revenue, without regard to the fiscal year's appropriation such allotment pertains.

Effect:

The effect of the above condition is the misstatement of receivable balances. However, this was corrected by proposed audit adjustments and to agree the account balance to the amount confirmed by the CNMI Department of Finance confirmation.

Furthermore, financial decisions made when financial information is misstated or otherwise in error, could result in negative or unplanned outcomes.

Recommendation:

PSS should use the Public Law for the Appropriation and Budget Authority Act, which is passed annually to serve as the basis for the recognition of appropriation revenue and related receivable.

Furthermore, PSS should ensure that collections are recorded as reduction to receivable.

Auditee Response:

Contact Person - Mr. George Palican
Completion Date - June 30, 2014

PSS concurs with the findings and beginning FY 2014, PSS will record appropriations revenue and receivable based on the Appropriation and Budget Authority Act and record collections as reductions to the receivable from the CNMI Government.

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-03, Travel Advances

Criteria:

Travel advances should be properly monitored to and sub-ledger balances should be reconciled to the general ledger.

Furthermore travel advances and liquidation should be pursuant to PSS travel and Commuting Regulations.

Conditions:

1. The following were noted during the audit of outstanding travel advances as of September 30, 2013:
 - a. Total outstanding travel advances as of September 30, 2013 amounted to \$652,598. An analysis of the aging of open travel advances shows that \$287,797 were over one year.
 - b. For 41 travelers, the travel advance and the liquidation were posted on separate accounts, and although the travelers have already liquidated their travel advances the general ledger where the advances were posted still reflects a receivable amount and the general ledger where the liquidation were posted shows an amount due to the traveler.

2. The following were noted during the test of PSS compliance with the travel and commuting policies:
 - a. PSS commuting policy is silent as to:
 - who is authorized to approve the Commute forms.
 - the Commute forms submission deadline and required supporting documents.
 - b. PSS commuting policy states that all official commutes shall be initiated and authorized with an approved Commute Form. I noted that the official Commute Form has no form date. Furthermore, the approvers usually do not put dates beside their signatures. The absence of these dates makes it difficult to validate whether the actual travel really happened after the approval. Current practice makes it possible to fill out the commute form after the fact.
 - c. PSS policy on commute states that per diem rates cover all traveler expenses except airline transportation. However, I noted that during liquidation, gas purchase receipts are reimbursed when the traveler is allowed car rental.

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SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-03, Travel Advances, continued

Cause:

- 1a. The documents supporting the liquidation of travel advance prior to 1999 cannot be located, hence the travel advance were left open.
- 1b. PSS uses four general ledger accounts to record travel advances. Some travelers have travel balances in two or more general ledger accounts, hence application of liquidation at time are posted to the wrong general ledger.
2. Weakness in the design of the PSS commuting policy.

Effect:

1. Although there is not material misstatement since these past due accounts have been provided 100% allowance since 2002. The traveler ledger balance may be overstated for travel advance actually liquidated but were not recorded due to missing documentation.
2. The weakness in the design of the internal controls over commuting provides opportunity for abuse and misuse of the commuting expenses.

Furthermore, fraud and abuse might exist and not be detected on a timely manner.

Recommendation:

1. PSS should review travel advances beyond the normal statute of limitation for write-off. PSS should also send regular statements to travelers with outstanding advances to remind them to liquidate the open travel advances. Pursuant to PSS regulation, PSS should recover unliquidated travel advances in form of salary deductions.
2. PSS should review its commuting policy to ensure that it is effectively designed and implemented.

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Year Ended September 30, 2013

SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-03, Travel Advances, Continued

Auditee Response:

Contact Person - Mr. George Palican
Completion Date - September 30, 2014

1. The write-off old travel balances in the Travel Account 1235 totaling \$287,797 that were transferred back in 1998 and 1999 from the old Wang system to the current JDE system has been approved write-off by the Commissioner and the Board of Education. This write-off will be offset against the allowance recorded in prior audits. This write-off will be processed by in FY 2014.

As travel liquidations are reconciled and processed, travelers with credit balances will be paid to clear these credit balances. On-going efforts will continue to properly reconcile the travel advance and liquidation.

2. PSS policy will be review and revised by September 30, 2014.

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-04, Human Resources

Criteria:

Personnel records should have all the required documents pursuant to PSS regulation § 60-30.1-910.

Condition:

1. Based on Results of testing of personnel records the following were noted:
 - a. For 31 or 34% of 90 personnel records selected to testing, there were no current contracts on file.
 - b. For 19 or 21% of 90 personnel records selected to testing, the contracts were signed more than 30 days after the effective dates.
 - c. For 36 or 40% of 90 personnel records selected to testing, there were no current medical certificates.
 - d. For 11 or 12% of the personnel records selected for testing, a letter of recommendation for renewal was not on file.

Cause:

PSS did not adhere to policies and procedures for the maintenance of Human Resources record.

Effect:

PSS is not in compliance with its regulations and there could be misstatements of payroll expenses. Fraud could exist and not be detected.

Recommendations:

PSS should ensure that all the required documents all the required documents pursuant to PSS regulation §60-30.1-190.

All employment contracts and personnel action forms should be timely signed by the employee, filed and maintained.

Employment contracts should be updated in a timely manner.

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION II – FINANCIAL STATEMENT FINDINGS

Finding No. 13-04, Human Resources

Auditee Response:

Contact Person - Ms. Coreen Palacios
Completion Date - August 31, 2014

The Human Resource Office (HRO) has begun the implementation of corrective steps to ensure that all PSS employees have valid contracts. The JDE system has been updated to include contract expiration dates and next review dates. All schools and programs have been given a directive to provide the required documents for renewals on January 2013. During February 2013, HRO issued a memo on contract renewal regulations and standard operating procedures. The impact of this improvements will affect contracts beginning SY 2014.

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Schedule of Findings and Questioned Costs
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SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-05 – Allowed Costs/Cost Principles - Compensation - Compliance with Human Resources Policies and Procedures.

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|--|--|-----------------------------|
| 84.403, 84.027, 93.600 and 10.550 | <p><u>Criteria:</u></p> <p>Pursuant to OMB Circular A-21, Cost Principles for Educational Institutions, compensation for personal services covers all amounts paid currently or accrued by the institution for services of employees rendered during the period of performance under sponsored agreements. Such amounts include salaries, wages, and fringe benefits. These costs are allowable to the extent that the total compensation to individual employees conforms to the established policies of the institution, consistently applied, and provided that the charges for work performed directly on sponsored agreements and for other work allocable as F&A costs are determined and supported as provided below.</p> | \$ - |

Context:

Selected 10% of employees funded under each of the major Federal Programs for compliance with compensation and Human Resources policies.

Conditions:

(1) The following employees were found to have no current contract on file:

(a) *Consolidated Grants (84.403) - 2 or 25% of 8 employees.*

| <u>Employee No.</u> | <u>Remarks</u> |
|-------------------------|---------------------------------------|
| 12744 | Contract expired on Sept 1, 2012 |
| 2515 | Last contract on file expired in 2007 |

(b) *Special Education (84.027) - 1 or 10% of 10 employees.*

| <u>Employee No.</u> | <u>Remarks</u> |
|-------------------------|---------------------------------------|
| 11460 | Last contract on file expired in 2010 |

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SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-05 – Allowed Costs/Cost Principles - Compensation - Compliance with Human Resources Policies and Procedures, Continued

| | | |
|-----------------|-------------------------------|-----------------------------|
| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|-----------------|-------------------------------|-----------------------------|

Conditions, Continued:

(2) *The contract for the following employees were signed more 30 days after their effectivity dates:* \$ -

(a) *Head Start (93.600) - 2 or 40% of 5 employees.*

| <u>Employee Number</u> | <u>Effectivity</u> | <u>Contract Date</u> | <u>No. of Days Late</u> |
|----------------------------|--------------------|--------------------------|-----------------------------|
| 13720 | 03/29/12 | 01/31/13 | 308 |
| 2077 | 08/01/13 | 12/06/13 | 127 |

(b) *Consolidated Grants (84.403) - 4 or 50% of 8 employees.*

| <u>Employee Number</u> | <u>Effectivity</u> | <u>Contract Date</u> | <u>No. of Days Late</u> |
|----------------------------|--------------------|--------------------------|-----------------------------|
| 2122 | 11/04/12 | 05/09/13 | 186 |
| 2986 | 07/31/12 | 05/09/13 | 282 |
| 5889 | 08/01/12 | 10/26/12 | 86 |
| 6116 | 08/01/12 | 05/09/13 | 281 |

(c) *Food and Nutrition (10.550) - 1 or 50% of 2 employees.*

| <u>Employee Number</u> | <u>Effectivity</u> | <u>Contract Date</u> | <u>No. of Days Late</u> |
|----------------------------|--------------------|--------------------------|-----------------------------|
| 2258 | 08/06/13 | 12/18/13 | 134 |

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SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-05 – Allowed Costs/Cost Principles - Compensation - Compliance with Human Resources Policies and Procedures, Continued

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> | | | | | | | | | | | | | | | | | | | | | | | | |
|----------------------------|--|-----------------------------|-----------------------------|--------------------------|-----------------------------|------|----------|----------|-----|------|----------|----------|----|-------|----------|----------|-----|-------|----------|----------|-----|------|----------|----------|-----|--|
| | (d) <i>Special Education (84.027) - 5 or 50% of 10 employees.</i> | \$ - | | | | | | | | | | | | | | | | | | | | | | | | |
| | <table border="0" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: left;"><u>Employee Number</u></th> <th style="text-align: left;"><u>Effectivity</u></th> <th style="text-align: left;"><u>Contract Date</u></th> <th style="text-align: left;"><u>No. of Days Late</u></th> </tr> </thead> <tbody> <tr> <td>2647</td> <td>08/01/12</td> <td>02/11/13</td> <td>194</td> </tr> <tr> <td>2814</td> <td>08/01/12</td> <td>10/26/12</td> <td>86</td> </tr> <tr> <td>12588</td> <td>09/02/11</td> <td>06/29/12</td> <td>301</td> </tr> <tr> <td>13480</td> <td>01/14/12</td> <td>04/30/12</td> <td>107</td> </tr> <tr> <td>6456</td> <td>02/01/12</td> <td>04/29/13</td> <td>453</td> </tr> </tbody> </table> | <u>Employee Number</u> | <u>Effectivity</u> | <u>Contract Date</u> | <u>No. of Days Late</u> | 2647 | 08/01/12 | 02/11/13 | 194 | 2814 | 08/01/12 | 10/26/12 | 86 | 12588 | 09/02/11 | 06/29/12 | 301 | 13480 | 01/14/12 | 04/30/12 | 107 | 6456 | 02/01/12 | 04/29/13 | 453 | |
| <u>Employee Number</u> | <u>Effectivity</u> | <u>Contract Date</u> | <u>No. of Days Late</u> | | | | | | | | | | | | | | | | | | | | | | | |
| 2647 | 08/01/12 | 02/11/13 | 194 | | | | | | | | | | | | | | | | | | | | | | | |
| 2814 | 08/01/12 | 10/26/12 | 86 | | | | | | | | | | | | | | | | | | | | | | | |
| 12588 | 09/02/11 | 06/29/12 | 301 | | | | | | | | | | | | | | | | | | | | | | | |
| 13480 | 01/14/12 | 04/30/12 | 107 | | | | | | | | | | | | | | | | | | | | | | | |
| 6456 | 02/01/12 | 04/29/13 | 453 | | | | | | | | | | | | | | | | | | | | | | | |

(3) *Head Start (93.600)* The job vacancy announcement, application form, applicant evaluation and assessment were not on file for one Head Start employee (Employee No. 14047). I am unable to determine through documentation that the recruitment was a result of full and open competition.

Cause:

PSS did not adhere to policies and procedures for the maintenance of Human Resources record pursuant to PSS regulation § 60-30.1-910.

Effect:

PSS is not in compliance with its regulations and there could be misstatements of payroll expenses. Fraud could exist and not be timely detected.

Recommendations:

PSS should ensure that all the required documents pursuant to PSS regulation §60-30.1-190.

All employment contracts and personnel action forms should be timely signed by the employee, filed and maintained.

Employment contracts should be updated in a timely manner.

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SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-05 – Allowed Costs/Cost Principles - Compensation - Compliance
with Human Resources Policies and Procedures, Continued

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|-----------------|-------------------------------|-----------------------------|
|-----------------|-------------------------------|-----------------------------|

Auditee Response:

\$ -

The Human Resource Office (HRO) has begun the implementation of corrective steps to ensure that all PSS employees have valid contracts. The JDE system has been updated to include contract expiration dates and next review dates. All schools and programs have been given a directive to provide the required documents for renewals on January 2013. During February 2013, HRO issued a memo on contract renewal regulations and standard operating procedures. The impact of this improvements will affect contracts beginning school year 2014.

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SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-06 – Allowed Costs/Cost Principles - Compensation - Time Cards

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|-----------------|--|-----------------------------|
| | <u>Criteria:</u> | \$ - |
| 84.403 | <p>Pursuant to OMB Circular A-21, Cost Principles for Educational Institutions, J(10)(c)(2)(c), to confirm that the distribution of activity represents a reasonable estimate of the work performed by the employee during the period, the reports will be signed by the employee, principal investigator, or responsible official(s) using suitable means of verification that the work was performed.</p> <p><u>Context:</u></p> <p>Randomly selected three pay period for testing, using the employees selected for the test of employment contracts.</p> <p><u>Conditions:</u></p> <p>(1) <i>Consolidated Grants (84.403)</i>. The actual hours worked reported on the timesheet summary for employee no 5263 for pay period ending December 15, 2012, cannot be verified because the time cards of the following employees have incomplete time in/out information:</p> <p>2) The sick leave form attached to Employee No. 2515 for pay period ending December 15, 2012 was for November 19 to November 30, 2012.</p> | |

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SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-06 – Allowed Costs/Cost Principles - Compensation - Time
Cards, Continued

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|-----------------|--|-----------------------------|
| | <p><u>Cause:</u></p> <p>PSS did not adhere to its policies and procedures for timekeeping.</p> <p><u>Effect:</u></p> <p>PSS is not in compliance with its regulations. Fraud could exist and not be timely detected.</p> <p><u>Recommendation:</u></p> <p>PSS should ensure that all hours paid can be verifiable pursuant to OMB Circular A-21. All time cards should be properly filled up and filed with the timesheet summary.</p> <p><u>Auditee Response:</u></p> <p>Payroll Staff closely monitors each bi-weekly submission of payroll timecards and related documents as part of its on-going Corrective Audit Action Plans. Timekeepers are emailed by Payroll Staff to correct any discrepancies and email copies are sent to keep School and Program Leaders updated in regards to payroll documentation discrepancies requiring correction. Funding is sought to obtain a computerized Timekeeping, Leave and Attendance (TLA) system that is linked to the JDE modules for HRO and Payroll to replace the manual timecard system.</p> | <p>\$ -</p> |

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Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-07 – Procurement and Suspension and Debarment – Public Notice and Bidding Time

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|---------------------------------|---|-----------------------------|
| 84.027, 10.550 and 84.403 | <p><u>Criteria:</u></p> <p>Pursuant to OMB Circular A-110, subpart C.43, All procurement transactions shall be conducted in a manner to provide, to the maximum extent practical, open and free competition.</p> <p>Pursuant to §60-40-205 (b) and (c) and §60-40-225 (b) and (c) of the Public School System Procurement Rules and Regulations,</p> <p>Public Notice - Adequate public notice of the invitation for bids shall be given a reasonable time prior to the date set forth for the opening of bids. Publication of notice in a newspaper of general circulation in the Commonwealth once in each week over a period of thirty calendar days shall be deemed to be adequate notice.</p> <p>Bidding Time - A bidding time of at least thirty calendar days shall be provided, unless the Chief of Procurement and Supply determines a shorter period is reasonable and necessary.</p> | \$ - |

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SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-07 – Procurement and Suspension and Debarment – Public Notice and Bidding Time, Continued

| | | |
|-----------------|-------------------------------|-----------------------------|
| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
| | <u>Condition:</u> | \$ - |

The following Invitation for Bids (IFB) and Request for Proposal (RFP) have and have been published for less than once a week over thirty calendar days and have bidding time of less than thirty calendar days.

Special Education

| | <u>Publication of Public Notice</u> | | | | <u>Bid Due Date</u> | <u>Bidding Time</u> |
|------------|-------------------------------------|------------|------------|------------|-------------------------|-------------------------|
| | <u>1st</u> | <u>2nd</u> | <u>3rd</u> | <u>4th</u> | | |
| RFP 12-042 | 09/28/12 | 10/05/12 | 10/12/12 | none | 10/23/12 | 25 |
| IFB 13-007 | 10/31/12 | 11/07/12 | none | none | 11/21/12 | 21 |

Food and Nutrition

| | <u>Publication of Public Notice</u> | | | | <u>Bid Due Date</u> | <u>Bidding Time</u> |
|------------|-------------------------------------|------------|------------|------------|-------------------------|-------------------------|
| | <u>1st</u> | <u>2nd</u> | <u>3rd</u> | <u>4th</u> | | |
| RFP 12-040 | 10/04/12 | 10/11/12 | none | none | 11/02/12 | 29 |

Consolidated Grants

| | <u>Publication of Public Notice</u> | | | | <u>Bid Due Date</u> | <u>Bidding Time</u> |
|------------|-------------------------------------|------------|------------|------------|-------------------------|-------------------------|
| | <u>1st</u> | <u>2nd</u> | <u>3rd</u> | <u>4th</u> | | |
| RFP 13-015 | 02/21/13 | 02/28/13 | 03/07/13 | none | 03/20/13 | 27 |

Only RFP 12-040 was accompanied by a written determination from the Chief of Procurement that a shorter period is reasonable and necessary.

Cause:

PSS Procurement and Supply Office construed the approval of the Chief of Procurement and Supply on the fewer dates of the publications of the public notice as his determination that the shorter period is reasonable and necessary.

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-07 – Procurement and Suspension and Debarment - Public Notice
and Bidding Time, Continued

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|-----------------|-------------------------------|-----------------------------|
|-----------------|-------------------------------|-----------------------------|

Effect:

\$ -

PSS is not in compliance with the provisions of its procurement rules and regulations in relations to public notice and bidding time for procurement requiring competitive sealed bidding.

There is no questioned cost presented for these conditions as documentations were provided, except for RFP 13-015, to evidence that a sufficient number of vendors were able to respond and the most responsive bidder was selected.

Recommendation:

PSS should ensure compliance with its procurement rules and regulations. If a determination is made by the Chief of Procurement and Supply that a shorter period of bidding is reasonable and necessary, such determination should be properly documented and retained in the Invitation for Bid files.

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-08 – Procurement and Suspension and Debarment – Change Order

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|-----------------|-------------------------------|-----------------------------|
| 84.403 | <u>Criteria:</u> | \$ - |

On December 28, 2010, PSS Procurement Officer aligned the change order regulation for PSS with the CNMI Central Government procedure.

CNMI Procurement Regulations § 70-30.3-410 (b) states that before adding significant new work to existing contracts, the agency shall thoroughly assess whether or not it would be more prudent to seek competition.

Context:

Randomly selected disbursements for compliance with procurement regulations.

Condition:

Contract No. 111617-OC awarded to provide professional development training for PSS Teachers with original contract amount of \$284,760 had the following change orders:

| Change Order No. | Scope | Amount | Percent of Change to Original Contract |
|------------------------|---|-------------------|--|
| 1 | To add work entitled "High Performance with High Reliability". | \$ 18,300 | 6% |
| 2 | To revive and extend the Original Contract to add sessions from October 2012 through June 30, 2013 for additional participants for the Classroom Instructions that works with Technology. | 75,000 | 26% |
| 3 | To add work entitled "Balance Leadership Sustainability Project Objectives" from April 2013 through August 12, 2013. | 50,000 | 18% |
| 4 | To add evaluation instrument license. | <u>22,450</u> | <u>8%</u> |
| | | <u>\$ 165,750</u> | <u>58%</u> |

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
PUBLIC SCHOOL SYSTEM**

(A Component Unit of the CNMI Government)

Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-08 – Procurement and Suspension and Debarment – Change Order,
Continued

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|-----------------|-------------------------------|-----------------------------|
| | <u>Condition, Continued:</u> | \$ - |

The original contract and the change orders were funded by the following federal programs:

| | | |
|-----------------|------------|-------------|
| Original Amount | \$ 284,760 | CFDA 15.875 |
| Change Order 1 | 18,300 | CFDA 84.403 |
| Change Order 2 | 75,000 | CFDA 84.256 |
| Change Order 3 | 50,000 | CFDA 84.256 |
| Change Order 4 | 22,450 | CFDA 84.403 |

Documentation that an assessment was performed to determine whether or not it would be more prudent to seek competition was not on file.

Cause:

Except for construction contracts, PSS Procurement regulations does not have specific provision for change orders, hence management have utilized change orders to facilitate procurement of services related to an existing contract.

Effect:

PSS is unable to determine whether or not it would be more prudent to seek competition. These change orders may have limited PSS ability for open and free competition.

Recommendation:

PSS should document a more comprehensive change order policy to ensure that internal controls are in place to prevent fraud and abuse.

Auditee Response:

PSS will review its procurement policy to ensure that internal controls are in place for change orders.

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-09 – Allowed Cost/Cost Principles - Travel

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|----------------------|--|-----------------------------|
| 84.027 and 93.600 | <u>Criteria:</u> Pursuant to PSS Travel Regulation §60-20-720 (d)(5), Travel routes other than what was authorized shall be allowed if it can be established as necessary and will not incur additional expense to the PSS and if the trip is related to official business to be performed by the traveler. | \$ - |

Condition:

1. *Special Education (84.027)*

For 5 or 38% of 13 Government Transportation Request (GTR) tested, the traveler changed route and the documentation that the change in route is necessary and related to the official business is not on file.

| Document Number | GTR No. | TA No. | Itinerary | Change in Route | Ticket Cost |
|--------------------|------------|-----------|--|--|-----------------|
| 210578 | 12400 | 114742 | GRT Saipan/Long Beach CA Return 04/26/13 05/05/13 | | |
| | | | ACTUAL Saipan/Long Beach CA Return 04/24/13 05/08/13 | 5 extra days in San Diego, CA | \$ 1,790 |
| 211124 | 12474 | 114562 | GRT Saipan/Charlotte, NC Return 05/04/13 05/12/13 | | |
| | | | ACTUAL Saipan/Charlotte, NC Return 05/01/13 05/14/13 | 5 extra days in Atlanta, GA | 2,581 |
| 212909 | 12684 | 115421 | GRT Saipan/Allentown, PA Return 06/22/13 07/01/13 | 2 extra days in Sacramento, CA | |
| | | | ACTUAL Saipan/Allentown, PA Return 06/19/13 07/05/13 | 4 extra days in San Diego, CA | 2,540 |
| 214475 | 12943 | 115873 | GRT Saipan/Washington Return 07/28/13 08/02/13 | | |
| | | | ACTUAL Saipan/Washington Return 07/28/13 08/10/13 | 8 extra days in Chattanooga, TN | 2,500 |
| 214478 | 12946 | 115872 | GRT Saipan/Washington Return 07/28/13 08/02/13 | 13 extra days in San Francisco and Santa Ana, CA | 2,500 |
| | | | ACTUAL Saipan/Washington Return 07/28/13 08/15/13 | | |
| | | | | | <u>\$11,911</u> |

2. *Head Start (93.600)*

For 1 or 9% of 11 GTRs tested, the traveler changed route and the documentation that the change in route is necessary and related to the official business is not on file.

| Document Number | GTR No. | TA No. | Itinerary | Change in Route | Ticket Cost |
|--------------------|------------|-----------|--|----------------------|----------------|
| 210600 | 12255 | 114347 | GRT Saipan/Guam Return 03/31/13 04/03/13 | | |
| | | | ACTUAL Saipan/Guam/Rota Return 03/31/13 04/08/13 | 5 extra days in Rota | \$ 285 |

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-09 – Allowed Cost/Cost Principles - Travel

| <u>CFDA No.</u> | <u>Findings/Noncompliance</u> | <u>Questioned Costs</u> |
|-----------------|---|-----------------------------|
| | <p><u>Cause:</u></p> <p>The changes in the itinerary were often made by the traveler directly with the travel agent. PSS will only become aware of these changes upon receipt of the invoice. Often times, when the invoice amounts agree with the GTR amounts, the detailed itineraries are overlooked as amounts either agrees or are within the allowed amount.</p> <p><u>Effect:</u></p> <p>Although no additional costs were incurred by PSS, the changes in the route is still not in compliance with PSS Travel regulations.</p> <p><u>Recommendation:</u></p> <p>The PSS GRT form has a notice stating there are penalties for "Private" use. PSS should enforce penalties to travel agents that accommodate changes in routes that are not covered by approved GRT as this may be construed as private use.</p> <p><u>Auditee Response:</u></p> <p>Contact Person - Mr. George Palican Completion Date - September 30, 2014</p> <p>Travel regulations will be revised to allow for no-cost changes in travel itineraries as long as there are no additional costs for PSS.</p> | \$ - |

**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
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(A Component Unit of the CNMI Government)

Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-10 – Head Start - Eligibility - Health Certificate

| <u>CFDA No.</u> | Findings/Noncompliance | <u>Questioned Costs</u> |
|-----------------|------------------------|-----------------------------|
| 93.600 | <u>Criteria:</u> | \$ - |

Pursuant to Head Start policies § 60-60-404,

The use of immunizations is recommended to prevent young children from becoming seriously ill or dying from once common and feared childhood diseases. The recommended immunization schedule begins during infancy and, with the exception of boosters, is completed during early childhood.

(a) CNMI Public Law 6-10 § 1163 states that "If the child has not received all of the required immunization, the parents shall be notified immediately that they are required to initiate all required immunization for their child within two weeks after the date of such notice...failure to comply shall be grounds for suspension of the child from school until immunization standards have been met."

(b) Pursuant to CNMI law, every parent of a child shall, at the time of first enrollment of the child in any Commonwealth public or non-public school and for each subsequent school year, irrespective of grade level, provide the school of attendance with proof that the child has received vision and hearing tests and all of the immunizations required by the Department of Public Health. Every parent/guardian of a child whose health records show incomplete tests and immunizations shall be immediately notified of the test or immunization deficiency.

(c) Parents are required to initiate all required examinations, tests and immunizations for their child within two weeks after the date of such notice. Except as provided in 3 CMC § 1164, failure to comply shall be grounds for suspension of the child from school until the examination, testing or immunization standards have been met.

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-10 – Head Start - Eligibility - Health Certificate

| | | |
|-----------------|---|-----------------------------|
| <u>CFDA No.</u> | Findings/Noncompliance | <u>Questioned Costs</u> |
| | <u>Condition:</u> | \$ - |
| | 9 or 10% of 90 student selected for testing do not have the updated health certification on file. | |

| <u>Center</u> | <u>Date of Birth</u> | <u>Last Certification on File</u> |
|--|----------------------|-----------------------------------|
| Chalan Kanoa Center - CK/A-PM | 03/15/08 | None on file |
| Chalan Kanoa Center - CK/B-AM | 01/21/08 | 02/07/11 |
| Chalan Kanoa Center - CK/B-AM | 11/26/07 | 05/17/12 |
| Chalan Kanoa Center - CK/B-PM | 11/07/07 | none on file |
| Chalan Kanoa Center - CK/C-AM | 10/21/07 | 07/13/11 |
| Chalan Kanoa Center - CK/D-AM | 09/27/07 | 04/06/11 |
| Joaquina M. Rabauliman Center - JMR/B-AM | 09/10/07 | 04/04/11 |
| Joaquina M. Rabauliman Center - JMR/B-AM | 10/14/08 | 12/23/11 |
| Oleai Center - Oleai/A-PM | 09/07/07 | 07/12/11 |

The review of the immunization records of these students shows that all students, except one, are current with the required immunization. However, the certification section of the immunization records are not properly certified. Some are not signed, not dated or the name of the certifying individual is not indicated.

Cause:

The responsibility to obtain proof that the child has received vision and hearing tests and all of the immunizations required by the Department of Public Health lies with the parents. PSS Head Start informs the parents of children with expiring health certification to obtain an updated certification to comply with the CNMI laws. However, most parents are not able to obtain the "Blue Card" (Health Certification) because of the fee. PSS Head Start considers the students in compliance with the health certifications for as long as they are current with their immunizations. Since no immunization is required for age 5, most of the returning Head Start students fail to obtain the Blue Card.

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Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

SECTION III – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 13-10 – Head Start - Eligibility - Health Certificate

| <u>CFDA No.</u> | Findings/Noncompliance | <u>Questioned Costs</u> |
|-----------------|------------------------|-----------------------------|
|-----------------|------------------------|-----------------------------|

Effect:

\$ -

The Head Start program is not in compliance with regulations.

Recommendation:

PSS Head Start should considered amending the Memorandum of Agreement with the Commonwealth Healthcare Corporation to include the Health certification of Head Start students in lieu of the individual certification.

Auditee Response:

The Head Start Administrator will review and redesign their medical certification and immunization form to address multiple dating of certification.

The Head Start Administrator will also coordinate with the Commonwealth Healthcare Corporation to amend the existing Memorandum of Agreement to include the Health certification of all Head Start students in lieu of the individual certification.



COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS

STATE BOARD OF EDUCATION
PUBLIC SCHOOL SYSTEM
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SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

A. FINANCIAL STATEMENT FINDINGS

| Reference No. | Findings | Status |
|---------------|--|--|
| 12-01 | Bank Reconciliation | Resolved. |
| 12-02 | Purchase/Disbursements | Resolved. |
| 12-03 | Use of Restricted Cash | Not Corrected. Similar condition noted in Finding No. 13-01. |
| 12-04 | Accrual and timely reconciliation of CNMI Appropriations | Not Corrected. Similar condition noted in Finding No. 13-02. |
| 12-05 | Accrual and timely reconciliation of Payables and Related Expenses | Resolved. |
| 12-06 | Capital Assets | Resolved. |
| 12-07 | Travel Advances | Not Corrected. Similar condition noted in Finding No. 13-03. |
| 12-08 | Human Resources and Payroll | Not Corrected. Similar condition noted in Finding No. 13-04. |

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**COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS
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Schedule of Prior Year Audit Findings
Year Ended September 30, 2013

| Reference No. | Findings | Status |
|----------------------|-----------------|--|
| 12-09 | Tax Compliance | On-going. PSS is in the process of reconciling with the U.S. Internal Revenue Services |

B. FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

| | | |
|-------|--|--|
| 12-10 | Procurement and Suspension and Debarment – Sole Source Justification | Resolved. Corrective actions were taken. |
| 12-11 | Procurement and Suspension and Debarment – | Resolved. Corrective actions were taken. |
| 12-12 | Procurement and Suspension and Debarment – After-the-Justification | Resolved. Corrective actions were taken. |
| 12-13 | Procurement and Suspension and Debarment – Public Notice and Bidding Time | Not corrected. Similar condition noted in Finding No. 13-07. |
| 12-14 | Allowable Costs/Cost Principles – | Resolved. Corrective actions were taken. |
| 12-15 | Davis-Bacon Act – | Resolved. Corrective actions were taken. |
| 12-16 | Allowable Costs/Cost Principles - Travel – | Not corrected. condition noted in Finding No. 13-09. |
| 12-17 | Equipment and Real Property Management – | Resolved. Corrective actions were taken. |

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Summary of Unresolved Questioned Costs
Year Ended September 30, 2013

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, 2013:

| | |
|---|--------------------|
| Questioned costs as previously reported | \$ 779,924 |
| Questioned costs resolved during the year ended September 30, 2013 | (703,340) |
| Questioned costs of fiscal year 2013 Single Audit | <u> -</u> |
| Unresolved questioned costs at September 30, 2013 | <u>\$ 76,584</u> |