

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

INDEPENDENT AUDITORS' REPORT ON  
INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2016

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

Ms. Marianne Concepcion-Teregeyo  
Secretary  
Department of Public Lands:

We have audited, 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, the financial statements of the Department of Public Lands (DPL) as of and for the year ended September 30, 2016, and the related notes to the financial statements, which collectively comprise DPL's basic financial statements, and have issued our report thereon dated January 3, 2018. Our report was qualified due to our inability to determine the propriety of due to CNMI balances or the basis for reservation of fund balances.

### **Internal Control Over Financial Reporting**

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

Our 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. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses as items 2016-001 through 2016-003 that we consider to be material weaknesses.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether DPL's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as items 2016-001 and 2016-002.

## **DPL's Responses to Findings**

DPL's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. DPL's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

## **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 result 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.

*Deloitte & Touche LLC*

January 3, 2018

DEPARTMENT OF PUBLIC LANDS  
Schedule of Findings and Responses  
Year Ended September 30, 2016

Local Noncompliance and General Ledger System

Finding No. 2016-001

Criteria: An effective system of internal control over financial reporting includes maintenance of a separate general ledger system that will record transactions and timely generate reliable and relevant financial information. Public Law 15-02 required the establishment of the DPL Operations Fund which shall be maintained by the CNMI Department of Finance (DOF) and required, 1) all revenues received by DPL be deposited in the DPL Operations Fund, and 2) all operational expenses of DPL be paid from the DPL Operations Fund.

Condition: DPL has not maintained a separate general ledger system since fiscal year 2007. Specifically:

1. Revenues received by DPL are not deposited in the DPL Operations Fund;
2. A general ledger for DPL transactions is maintained by DOF but it is not reconciled or monitored by DOF or DPL;
3. Cash transactions, received and disbursed at DPL, are summarized in cash receipt and cash disbursement journals, which are not recorded in the DOF general ledger;
4. Journal vouchers posted to DOF's general ledger by DOF personnel are not approved by DPL management;
5. The aged receivable subsidiary ledger included invalid receivables of \$186,261 as of September 30, 2016 (permit nos. C9501S, C9003S, CR9501S, T09001S, T07014S, TR0714S and TR9007S);
6. The account balances on the accounts receivable aging report for permit numbers L9104S, L9404S, L8645S, L9403S, LB8902S and T0032S does not agree with the account balances per the account ledger reports. An adjustment was proposed to correct the account balances of the accounts receivable aging report. We recommend that DPL reconcile the aging report against the account ledger reports periodically.
7. Receivables, accounts payable, accruals and unearned revenues are not reconciled in DOF's general ledger;
8. Adjustments to record DPL transactions in DOF's general ledger were recorded by DPL through proposed audit adjustments; and
9. Review and approval for journal entry 17342 for \$81,480 was not evident.

Cause: Compliance with Public Law 15-02 is not enforced. Monitoring and timely reconciliation of transactions with DOF is not performed. DPL did not implement available system controls over the financial reporting process and there is no established monitoring control procedures to determine the accuracy and completeness of disbursements processed at DOF.

Effect: DPL is in noncompliance with Public Law 15-02. DPL is unable to produce reliable and relevant financial information.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2016

Finding No. 2016-001, Continued

Recommendation: We recommend DPL comply with Public Law 15-02 and monitor and reconcile transactions with DOF in a timely manner, establish monitoring control procedures over disbursements, perform periodic reconciliations with DOF to verify the accuracy and completeness of disbursements processed, reconcile account balances maintained in the DOF general ledger and reconcile the aged receivable subsidiary ledger and exclude invalid receivables.

Prior Year Status: The lack of compliance with Public Law 15-02 and lack of reliable and relevant financial information and the inability to timely detect errors and inaccuracies was reported as a finding in the audits of DPL for fiscal years 2010 through 2015.

Auditee Response and Corrective Action Plan:

**Name of Contact Person:** Marianne Concepcion-Teregeyo, Secretary

**Corrective Action:**

Condition 1:

DPL has written to the CNMI Secretary of Finance (SOF) and the CNMI Office of the Attorney General (OAG) attempting to resolve this matter.

Conditions 2, 3, 4, 7 and 8:

The conditions pertaining to DPL and CNMI Department of Finance (DOF) accounting systems are being addressed with DOF. DPL has obtained OAG's advice regarding compliance of DPL's accounting functions with Public Law 15-02. According to OAG, compliance with Public Law 15-02 entails DOF assuming all the accounting functions of DPL and we have discussed this with SOF in the effort of transitioning. DPL is in the process of devising a transition plan that ensures an orderly transfer while simultaneously addressing reconciliation, approval and context adjustment processes.

Conditions 5 and 6:

DPL acknowledges that the account balance on the accounts receivable aging report for leases does not agree with the account balances per the account ledger reports. Our Accounting Division is investigating the cause of this imbalance.

Condition 9:

In our letter to you on September 8, 2017, we furnished copies of the transition. It was determined that the finding was due to DOF's lack of signed journal voucher. Therefore, DPL requests that this condition be removed. This finding shouldn't be a penalty to DPL as DPL has no control over DOF's entry methods.

DPL will formalize procedures with DOF for DPL to monitor and approve journal vouchers, as well as reconcile and monitor its general ledger maintained by DOF. Implementation of such procedures should prevent future like findings.

**Proposed Completion Date:** To be determined.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2016

Finding No. 2016-001, Continued

Auditor Response:

Condition 9:

Documentation provided did not evidence approval of the journal entry through initials or signature. Approval of journal vouchers is the responsibility of both DPL and DOF.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2016

Revenue/Receipts

Finding No. 2016-002

Criteria: Management is responsible to enforce its policies for leasing public lands. Long-term lease contracts and temporary permits require that the lessee, not later than forty-five (45) or thirty (30) days after the end of each calendar year of the lease or permit, submit audited financial statements and a schedule of gross receipts indicating sources and deductions. Some leases and permits require that the financial statements be audited by certified public accountants. Additional requirements include the lessee to perform an appraisal of the fair market value of the unimproved land after each succeeding five or ten-year term to determine the new annual base rental.

Condition: Tests of forty-five cash receipts for long-term lease contracts and temporary permits noted the following:

1. Audited financial statements and a schedule of gross receipts were not provided for eleven receipts related to contracts and permits requiring such documents.

<u>Lessee No.</u>	<u>Receipt No.</u>
L8646S	16-0321
LB8644S	2016-0634
LB8645S	2016-0633
L9104S	2016-0700
L8645S	16-0012
L08005S	2016-0865
L8903S	2016-0719
L9712S	16-0116
L9404S	2016-0997
LB8648S	16-0016
LB0708S	2016-0675

2. Financial statements provided for one lessee (No. LB8902S) were not audited by a certified public accountant as required by the lease.
3. Guaranteed annual rental (GAR) is based on the higher of eight percent (8%) of the property's appraised fair value or the agreed rental per the lease agreement. We noted that appraisals were not performed after the end of the appraisal period for the following lessees.

<u>Lessee No.</u>	<u>Receipt No.</u>
L07002S	16-0494
L08009T	16-1096

4. For lease no. L0708S, annual rental rates were not based on the current appraisal performed on 04/07/16.
5. For lease no. L9603S, the former annual rental rate (\$1,140) billed did not reflect the updated annual rental rate as required per the lease's rental schedule.

Cause: The cause of the above condition is the lack of monitoring procedures to determine which contracts and/or permits require financial statements or audited financial statements and appraisals and determine that rate billed agreed to rate per contract.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2016

Finding No. 2016-002, Continued

Effect: The effect of the above condition is the potential underpayment of lease revenues and collections on invalid permits and leases.

Recommendation: We recommend that management update lease contracts and permits and enforce lease provisions.

Prior Year Status: Monitoring procedures for contracts and/or permits that require financial statements or audited financial statements, a schedule of gross receipts, and the filing of authorized permits was reported as a finding in the audits of DPL for fiscal years 2010 through 2015.

Auditee Response and Corrective Action Plan:

**Name of Contact Person:** Marianne Concepcion-Teregeyo, Secretary

*Compliance Division's monitoring procedure, Accounting Division's monitoring procedure - already procured and estimated to implement Sage in FY17, Directive No. 005*

DPL is in the process of implementing an accounting software system since the original system (Peachtree) was not updated since 2002. The new system, Sage 100, will improve the ability to maintain the General Ledger System, a required system of internal control that vastly improves the integrity of our accounting processes. This implementation will clear this finding. It will streamline the current accounting processes as it will eliminate redundant manual inputting of transactions, and will improve the integrity of our financial management system and DPL's financial reporting capabilities.

Also, I implemented Directive No. 005 which will require Director of Compliance, Director of Real Estate, and Director of Accounting to conduct monthly reconciliation meetings to ensure information across divisions are consistent, up-to-date, and reliable. The goal of this directive is to rid of future findings of inconsistent accounting information.

The Compliance Division conducts annual inspections on all public land leases/Temporary Occupancy Agreements (TOA) pursuant to contract and/or TOA provisions. This methodology ensures that lessees and TOA Occupants remain in compliance by submitting requisite documents such as financial statements or audited financial statements and schedules of gross receipts. Upon site inspection, the compliance inspector makes recommendations such as compliant/non-compliant and if not remedied, the division will move to issue a Notice of Violation (NOV). The lease/TOA may be canceled should the lessee/occupant fail to cure the violation within the given deadline.

Lastly, DPL created an internal auditor position to aid in the internal review of DPL's processes; ensure compliance of established policies, procedures, and all relevant federal and local statutes and regulations; perform internal audit, review, and evaluate operations; audit accounting system; examine, investigate, and review reports, financial statements and management practices; and perform other related duties as assigned. The position will be advertised in the coming weeks by OPM and DPL will plan to interview and make a selection decision shortly after.



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Schedule of Findings and Responses, Continued  
Year Ended September 30, 2016

Finding No. 2016-002, Continued

Auditee Response and Corrective Action Plan, Continued:

**Corrective Action:**

Condition 1:

DPL acknowledges financial statements were not provided for eleven (11) receipts related to contract and permits requiring such documents. DPL reached out to all 11 lessees regarding this matter and are awaiting requested documents.

Condition 2:

DPL sent a letter notifying the lessee to submit certified financial statements.

Condition 3:

DPL issued a notice of violation to lessee no. L07002S regarding timely submission of the appraisal report which was due December 5, 2016. DPL is awaiting submission of the retrospective appraisal report to utilize in adjusting rents for the next five-year period. For future leases, DPL's regulations authorize DPL to expend security deposit amounts to enforce provisions of the agreement including obtaining appraisal reports in the event the lessee does not respond to NOV.

Condition 4:

The lessee submitted the updated appraisal late but was ultimately approved. Rents were subsequently adjusted to reflect the updated appraisal value.

Condition 5:

DPL requested an updated appraisal for lease no. L9603S.

**Proposed Completion Date:** To be determined.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2016

Receivables

Finding No. 2016-003

Criteria: Receivables should be recorded when revenues are earned and should be timely assessed for collectability. DPL policy requires a 100% allowance for receivable balances that are ninety days past due.

Condition: Lease receivables of \$990,073 were greater than ninety days past due as of September 30, 2016. No allowance was recorded for these past due accounts.

Cause: DPL does not monitor the allowance for doubtful accounts.

Effect: Lease receivables are misstated. An audit adjustment was proposed to correct this misstatement.

Recommendation: We recommend that DPL monitor the allowance for doubtful accounts.

Auditee Response and Corrective Action Plan:

**Name of Contact Person:** Marianne Concepcion-Teregeyo, Secretary

**Corrective Action:** DPL is in the process of initiating a policy on doubtful accounts. This policy will be categorized based on age of delinquency and probability of collection. The range will be from increments of 30 calendar days from 30 days to 90 days or greater. As the age of the account increases, so does the probability of non-collection. This methodology will ensure that DPL monitors doubtful accounts and eventually writes off uncollectible accounts (bad debt) as contra-revenue as required by GASB. Conditions will be included that if a customer wants to resume utilizing public land, renew an agreement or enter into a new agreement, all arrears must be paid.

**Proposed Completion Date:** To be determined.

DEPARTMENT OF PUBLIC LANDS

Unresolved Prior Year Comments  
Year Ended September 30, 2016

The status of unresolved prior year findings is discussed in the Schedule of Findings and Responses section of this report.