

OPA REPORT  
LT-00-02

Office of the Public Auditor  
Commonwealth of the Northern Mariana Islands

Audit of the Department of Finance's  
Double Payments of 1995 Corporate Tax Rebates to  
Eleven Taxpayers in Fiscal Year 1997



Letter Report  
LT-00-02



# Office of the Public Auditor

Commonwealth of the Northern Mariana Islands

World Wide Web Site: <http://opacnmi.com>  
2nd Floor J. E. Tenorio Building, Chalan Pale Arnold  
Gualo Rai, Saipan, MP 96950

Mailing Address:  
P.O. Box 1399  
Saipan, MP 96950  
E-mail Address:  
[mail@opacnmi.com](mailto:mail@opacnmi.com)  
Phone: (670) 234-6481  
Fax: (670) 234-7812

March 14, 2000

Ms. Lucy DLG. Nielsen  
Secretary, Department of Finance  
P.O. Box 5234 CHRB  
Saipan, MP 96950

Dear Ms. Nielsen:

**Subject: Final Letter Report on the Audit of the Department of Finance's Double Payments of 1995 Corporate Tax Rebates to Eleven Taxpayers in Fiscal Year 1997 (Report No. LT-00-02)**

This report presents the results of our audit of the Department of Finance's (DOF) double payments of 1995 corporate tax rebates to eleven taxpayers in fiscal year (FY) 1997. The objectives of the audit were to determine whether (1) DOF processed payments of corporate tax rebates in accordance with its established control procedures, and these procedures were adequate to ensure that only valid obligations were processed for payment; and (2) CNMI accounting records were adjusted accordingly to correct the accounting errors brought about by the double payments.

Our audit showed that DOF did not perform the established control procedure for processing complaints of nonreceipt of corporate tax rebate payments. Specifically, the Accounts Payable Section did not verify whether previous payments had already been made, resulting in double payments of 1995 corporate tax rebates to eleven taxpayers in FY 1997 amounting to \$469,798. We also found that the established controls were inadequate. No control procedure was in place in the DOF financial management system to detect duplicate presentations of the Division of Revenue and Taxation (DRT) payment voucher listing(s) of corporate tax rebate(s), and thus the likelihood of duplicate payments in the future is not minimized.

Our audit also showed that although FY 1997 operating accounts were still open when DOF discovered the double payments (*i.e.*, the FY 1997 audit was completed in October 1998 while DOF had knowledge of the double payments in November 1997), DOF failed to accrue receivables from the eleven corporate taxpayers and correct the overstatement of rebate tax expense at the end of FY 1997. These omissions caused the FY 1997 assets, income, and ending fund balance (and thus the FY 1998 beginning fund balance) to be understated by \$469,798. DOF's recording of the collection of the double payments in FY 1998 as revenues caused FY 1998 income to be overstated.

We recommended that the Secretary of Finance (1) require the DOF-Accounts Payable Section of the Division of Finance and Accounting to strictly comply with its established control procedures for processing complaints about nonreceipt of corporate tax rebate payments, in particular verifying if previous payment has been made before processing a new payment; (2) develop and implement control procedures in its financial management system which will recognize and flag potential duplicate processing of corporate tax rebate payments; and (3) ensure that prompt and proper adjustments to the CNMI accounting records are made for the affected fiscal year(s) in case any other double payment is found.

In her letter response dated January 27, 2000 (**Appendix B**), the Secretary of Finance addressed Recommendations 1 and 2 by stating that a new tax system is currently being developed to give DOF the capability to automate processing of the corporate rebate tax returns. Because the annual returns will be entered and processed through the tax system, the rebate computations and preparation of rebate checks will be part of the automated process. Since the payment data are stored, the system will automatically flag a warning if a rebate check has already been issued to a particular corporation for a specific tax year. This process will ensure the detection of duplicate processings of a return and potential double payment of a tax rebate. The new tax system is expected to be completed by the summer of year 2000. DOF anticipates processing the 1999 tax returns using the new system.

Based on the response we received from the Secretary, we consider Recommendations 1 and 2 resolved and Recommendation 3 closed. We agree that the alternative course of action cited by the Secretary in addressing Recommendations 1 and 2 is a reasonable course of action. The additional information or action required to close the recommendations is presented in **Appendix C**.

## **BACKGROUND**

While conducting verification procedures at the CNMI Treasury (in connection with another audit), the auditor noticed a folder with a list and correspondence from the former Acting Secretary of Finance pertaining to double payment of corporate tax rebates. An inquiry revealed that eleven corporate taxpayers were paid twice for their 1995 tax rebates because the complaint by one unpaid taxpayer was mistaken as claims for all twelve taxpayers in the DRT payment voucher listing faxed by the DOF-Secretary's Office to the DOF-Accounts Payable Section. Because one of the taxpayers informed DOF of the double payment, DOF discovered and was able to recover all overpayments. However, because of the substantial amount of the overpayments and the risk of recurrence if the cause is not addressed and corrected, OPA decided to investigate the circumstances surrounding the double payments.

## **OBJECTIVES, SCOPE AND METHODOLOGY**

The objectives of the audit were to determine whether (1) DOF processed payments of corporate tax rebates in accordance with its established control procedures, and these procedures were adequate to ensure that only valid obligations were processed for payment; and (2) CNMI accounting records were adjusted accordingly to correct the accounting errors brought about by the double payments. To accomplish our objectives, we examined payment and accounting records, evaluated the controls over processing payments of corporate tax rebates, and interviewed officials and employees of the CNMI Treasury, DOF-Accounts Payable Section, DRT, and Secretary's Office.

We performed our audit at the CNMI Treasury, DOF-Accounts Payable Section, and DRT offices in Saipan from October to November 1998. The audit was made, where applicable, in accordance with Government Auditing Standards issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures as were considered necessary in the circumstances.

## **FINDINGS AND RECOMMENDATIONS**

### **A. Failure to Verify Prior Payments Resulted in \$469,798 Double Payments**

DOF established policies and procedures for processing corporate tax rebates and complaints of nonreceipt of corporate tax rebate payments. For complaints, one of the control procedures is for the DOF- Accounts Payable Section to verify if prior payments have been processed. Our audit showed, however, that DOF did not perform the established control procedure for processing complaints of nonreceipt of corporate tax rebate payments. Specifically, the Accounts Payable Section did not verify whether previous payments had already been made, resulting in double payments of 1995 corporate tax rebates to eleven taxpayers in FY 1997 amounting to \$469,798. In September 1997, DOF-Finance and Accounting Division received thru fax the *September 1996* memorandum from the DRT Director requesting the processing of payments, together with the supporting DRT payment voucher listing summarizing the tax rebates due to twelve corporate taxpayers whose rebate checks had already been processed and issued a year earlier, in September 1996. The former Accounts Payable supervisor did not verify payees' records to ascertain if payments had been previously processed, and if checks had been issued and had cleared the bank. Consequently, on September 30, 1997, DOF again processed tax rebates for twelve corporate taxpayers even though eleven of them had already received checks in September 1996. OPA knew that when the double payments occurred, DOF was in a transition period because of a change to a new computerized financial management system; nevertheless, there should be no excuse for not performing the control procedure to verify prior payments. We also found that the established controls were inadequate. No control procedure was in place in the DOF financial management system to detect duplicate presentations of the DRT payment voucher listing(s) of corporate tax rebate(s), and thus the likelihood of duplicate payments in the future is not minimized. It should be noted that the double payments might not have been discovered if one of the eleven corporate taxpayers had not informed DOF of the double payments.

### *Proper Authorization and Verification Procedures*

Adequate authorization and verification procedures are very basic steps in the system of internal control required to be maintained by any financial organization. These procedures include checking whether transactions are authorized and valid.

DOF has existing policies and procedures on processing corporate tax rebates and complaints about nonreceipt of those rebate payments. Corporate tax returns are processed manually at DRT and rebate payments are processed at DOF-Accounts Payable Section through the regular accounts payable system. DRT prepares a memorandum (a cover letter addressed to the Director of Finance and Accounting thru the Secretary of Finance requesting payment) together with the DRT payment voucher listing<sup>1</sup>. Upon receipt of the memorandum and the DRT payment voucher listing from the Secretary's Office, the Accounts Payable Section of the Division of Finance and Accounting prepares the Accounts Payable Voucher (APV) for each taxpayer on the DRT payment voucher listing. Based on the processed APV, the CNMI Treasury processes and prints the checks and mails them directly to the corporate taxpayers.

For a complaint about non-receipt of a corporate tax rebate payment, the DRT Compliance branch initially acts on it by assisting the taxpayer in documenting the complaint in a form established by DRT for this purpose. The Compliance Branch initiates the review process by determining whether a DRT payment voucher listing has been prepared and submitted to the DOF-Finance and Accounting Division. If a DRT payment voucher listing has been prepared, an inquiry to the DOF-Accounts Payable Section is made to determine if payment was processed. The DOF financial management system is used by DOF managers or staff to inquire about the history of payments to any payee. If a rebate check has been processed and issued, the corporate taxpayer is informed as to the disposition of the check. If the taxpayer still complains of not having received the check, DRT requests the CNMI Treasury to determine the status of the check. If the check is still outstanding, a stop payment order is placed on it. Then, the check is cancelled and a replacement check is issued. If the check has cleared, the corporate taxpayer is informed as to the status of the check.

### *Review of Prior Payments Not Made*

Our audit showed that DOF did not perform the established control procedure for processing complaints about nonreceipt of corporate tax rebate payments. Specifically, the Accounts Payable Section did not verify whether previous payments had already been made, resulting in double payments of 1995 corporate tax rebates to eleven taxpayers in FY 1997 amounting to \$469,798.

In September 1997, the DRT-Compliance Branch received a complaint that a corporate taxpayer (a Japanese bank) had not received its tax rebate for year 1995. According to the DRT Compliance Branch manager, after determining that a DRT payment voucher listing had been prepared in

---

<sup>1</sup> The DRT payment voucher listing serves as the Accounts Payable Section's basis for processing payments. It lists the tax rebate due to each corporate taxpayer, showing the following details for each corporate taxpayer: tax identification number, name and address, type of return, document locator number of the tax return, date filed, date required to be paid, amount, and remarks, if any. There is no minimum or maximum limit as to the number of taxpayers the DRT payment voucher listing may contain.

September 1996, she requested the former Acting Secretary of Finance to determine the status of the tax rebate check that was supposed to have been issued to the corporation in 1996.

OPA learned that the corporate taxpayer who complained was one of the twelve taxpayers who were issued manually prepared tax rebate checks in September 1996. Check payments were processed based on DRT payment voucher listing no. 013-96 which showed the corporate names of the twelve taxpayers and their rebate amounts totaling \$750,926.46 (see **Appendix A**). The DRT Director's memorandum dated September 13, 1996, together with this DRT payment voucher listing, directed the processing of tax rebate payments to the twelve corporate taxpayers. Except for one (check number 457866 amounting to \$281,128 payable to the Japanese bank), all rebate checks "cleared" and were charged against the CNMI's bank account between September and November 1996<sup>2</sup>.

On September 22, 1997, a copy of the same memorandum and DRT payment voucher listing no. 013-96 was sent by fax by the former Acting Secretary of Finance (at DOF Dandan office) to DOF-Finance and Accounting, Accounts Payable Section (on Capitol Hill). There were no other written instructions but according to the former Acting Secretary of Finance, she verbally instructed the former Accounts Payable Supervisor to check on previous payments to the twelve taxpayers. When interviewed, the former Accounts Payable Supervisor could not recall any verbal instructions from the former Acting Secretary of Finance. She could only recall receiving a faxed copy of the memorandum and the DRT payment voucher listing no. 013-96, and her understanding of the situation was that a second set of rebate checks needed to be processed. She admitted that no verification procedures were conducted to determine whether the obligations created by the DRT payment voucher listing had been paid. Consequently, twelve rebate checks totaling \$750,926 were again processed and printed, and mailed to the taxpayers. However, since only the tax rebate payable to the Japanese bank amounting to \$281,128 should have been processed, the transactions resulted in double payments to eleven taxpayers totaling \$469,798 (see **Appendix A** for details).

We also found that the established controls were inadequate. No control procedure was in place in the DOF financial management system to detect duplicate presentations of the DRT payment voucher listing(s) of corporate tax rebate(s), and thus the likelihood of duplicate payments in the future is not minimized. The JD Edwards financial management system has the capability to recognize and flag potential duplicate payments through the invoice number. If a duplicate invoice number is entered, the system warns the end user of a possible duplicate entry. Corporate tax rebates, however, are not supported by invoice. Nevertheless, DOF should have developed a control system of assigning a unique invoice number to each corporate taxpayer in the DRT payment voucher listing when processing payment (e.g., use the DRT payment voucher listing no. and 01 for the first taxpayer, then DRT payment voucher listing no. and 02 for the second taxpayer, and so on). Through this method, if the same DRT payment voucher listing already processed is again received from the Secretary's Office or from any other sources, the same invoice number will be entered and the system will warn the end user of the possible duplicate processing of a corporate tax rebate.

---

<sup>2</sup> Although CNMI Treasury records showed that check number 457866 was mailed to the payee, the check remains missing and unaccounted for to date.

## B. CNMI Accounting Records not Adjusted to Correct Accounting Errors Due to Double Payments

Accounting errors made in the course of a year and discovered by the government's accounting staff, its internal auditors, or its external auditors when the operating accounts have not been closed should be rectified by correcting the affected year(s) accounts. Our audit showed, however, that although FY 1997 operating accounts were still open when DOF discovered the double payments (*i.e.*, the FY 1997 audit was completed in October 1998 while DOF had knowledge of the double payments in November 1997), DOF failed to accrue receivables from the eleven corporate taxpayers and correct the overstatement of rebate tax expense at the end of FY 1997. These omissions caused the FY 1997 assets, income, and ending fund balance (and thus the FY 1998 beginning fund balance) to be understated by \$469,798. DOF's recording of the collection of the double payments in FY 1998 as revenues caused FY 1998 income to be overstated.

### *Correction of Errors*

Many types of accounting errors may be made in the course of a year and discovered by the government's accounting staff, its internal auditors, or its external auditors. The effects of errors on the accounts of the current year and/or prior year financial statements must be analyzed to determine the correcting entry required:

- *Errors that affect only the current year accounts* may be rectified by correcting the current year accounts, assuming that they have not been closed, and therefore do not require restatement of the beginning fund balance.
- *Errors that affect prior year financial statements* may require restatement of the beginning fund balance since the prior year accounts were closed at the end of the prior year, and may require corrections of related current year accounts. Prior year errors must be corrected if material (*i.e.*, when the financial statements for the current year will be misstated). Likewise, prior year statements should be corrected if they are issued again, alone, or with the current year financial statements.

### *Failure to Adjust DOF Books in FY 1997*

Our audit also showed that although FY 1997 operating accounts were still open when DOF discovered the double payments (*i.e.*, the FY 1997 audit was completed in October 1998 while DOF had knowledge of the double payments in November 1997), DOF failed to accrue receivables from the eleven corporate taxpayers and correct the overstatement of rebate tax expense at the end of FY 1997.

In November 1997, one of the taxpayers informed DOF of the double payment. DOF reviewed the matter and ordered the bank to stop payment on the tax rebate checks which were determined

to be double payments<sup>3</sup>. During that time, FY 1997 books were still open. The external auditors completed field work of the audit in October 1998. DOF should have made the following entries:

|                          |         |
|--------------------------|---------|
| Receivables .....        | 469,798 |
| Rebate Tax Expense ..... | 469,798 |

To accrue the receivables from the eleven corporate taxpayers and to correct the overstatement of rebate tax expense at the end of FY 1997.

If reversing entries are used, the above adjusting entry should have been reversed at the beginning of FY 1998, as follows.

|                          |         |
|--------------------------|---------|
| Rebate Tax Expense ..... | 469,798 |
| Receivables .....        | 469,798 |

To reverse prior year-end accrual adjusting entry at the beginning of the current fiscal year.

Then, as FY 1998 cash receipts for collection of double payments are routinely credited to rebate tax expense (or revenues), the amounts applicable to FY 1997 would be automatically deducted from FY 1998 rebate tax expense (or revenues).

Had the double payments been discovered after FY 1997 books were closed, DOF should have made the following correcting entry.

|   |     |
|---|-----|
| Rebate Tax Expense or Revenues (depending what was credited upon collection of double payments) . . . | xxx |
| Prior Year Error Correction .....   | xxx |

To correct prior year overstatement of rebate tax expense and current year overstatement of net income.

DOF's failure to make the adjusting entry in FY 1997 caused the FY 1997 assets, income, and ending fund balance (and thus, FY 1998 beginning fund balance) to be understated by \$469,798. DOF's recording of collection of double payments in FY 1998<sup>4</sup> as revenues caused FY 1998 income to be overstated.

### ***Conclusion and Recommendations***

DOF should strictly comply with its established control procedures for processing complaints about nonreceipt of corporate tax rebate payments, in particular verifying if previous payment has been made before processing a new payment. DOF-Accounts Payable Section erroneously processed the tax rebates of the eleven taxpayers totaling \$469,798 when they accepted the faxed duplicate DRT payment voucher listing no. 013-96 as the basis for processing payments and did

---

<sup>3</sup> All except the two corporate taxpayers had already cashed the duplicate payment checks before the stop payment order date. Although a stop payment order was made, one of the two corporate taxpayers was still able to cash the check after the stop payment order date.

<sup>4</sup> Only ten out of the eleven duplicate payments were recouped totaling \$380,621. These were credited to FY 1998 general fund revenues, rebate tax expense, or rebate trust fund accounts. The other taxpayer received a check for \$89,177 but did not cash it. The check became stale and was added back to the general fund cash balance at the end of FY 1998 (together with all other stale checks), as part of DOF's year-end reconciliation procedures.



not perform verification procedures. Only the voluntary act of one taxpayer in informing DOF of the double payment alerted DOF to the mistake and required DRT to make a total recovery. In addition, no control procedure was in place in the DOF financial management system to detect duplicate presentations of the DRT payment voucher listing(s) of corporate tax rebate(s), and thus the likelihood of duplicate payments in the future is not minimized. Also, CNMI accounting records should be adjusted accordingly to correct accounting errors due to double payments in order to have accurate financial information.

Accordingly, we recommend<sup>5</sup> that the Secretary of Finance:

1. Require the DOF-Accounts Payable Section of the Division of Finance and Accounting to strictly comply with its established control procedure for processing complaints about nonreceipt of corporate tax rebate payments, in particular verifying if previous payment has been made before processing a new payment;
2. Develop and implement control procedures in its financial management system which will recognize and flag potential duplicate processing of corporate tax rebate payments; and
3. Ensure that prompt and proper adjustments to the CNMI accounting records are made for the affected fiscal year(s) in case any other double payment is found.

#### *Secretary of Finance's Response*

In her letter response dated January 27, 2000 (**Appendix B**), the Secretary of Finance addressed Recommendations 1 and 2 by stating that a new tax system is currently being developed to give DOF the capability to automate processing of the corporate rebate tax returns. Because the annual returns will be entered and processed through the tax system, the rebate computations and preparation of rebate checks will be part of the automated process. Since the payment data are stored, the system will automatically flag a warning if a rebate check has already been issued to a particular corporation for a specific tax year. This process will ensure the detection of duplicate processings of a return and potential double payment of a tax rebate. The new tax system is expected to be completed by the summer of year 2000. DOF anticipates processing the 1999 tax returns using the new system.

#### *OPA Comments*

Based on the response we received from the Secretary, we consider Recommendations 1 and 2 resolved and Recommendation 3 closed because of the following:

Recommendations 1 and 2 - We agree that the alternative course of action cited by the Secretary in addressing the recommendations is a reasonable course of action.

---

<sup>5</sup> The original recommendations have been revised and rearranged for clarity. Some of the responses of the Secretary of Finance to the original recommendations were determined to be significant in developing findings, and thus were included in the findings section of the final version of the report.

Recommendation 3 - The recommendation in the draft report was changed to an advice for prompt and proper adjustments of affected accounts in case error occurs in the future, and in the audit recommendations tracking status, Recommendation 3 will be considered closed.


FY 1997 and 1998 CNMI books of accounts were already closed and audited. Since the amount of the adjustment was below the materiality level set in the FY 1998 financial audit, OPA will not pursue the restatement of FY 1998 general fund revenue (decrease) and general fund beginning balance (increase). The compensating recording errors in FY 1997 and FY 1998 resulted in the correct general fund ending balance in FY 1998. From an analytical point, however, the comparative statements of revenues for FY 1998 and FY 1999 will not show an accurate matching of both years revenues. The FY 1998 revenue will be overstated by \$469,798 because that account was already deducted from the general fund beginning balance. We will let DOF determine how the comparative revenue amounts will be presented in the FY 1999 and FY 1998 audited financial statements.

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

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

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

Sincerely,

  
Leo L. LaMotte  
Public Auditor, CNMI

cc: Governor  
Lt. Governor  
Twelfth CNMI Legislature (27 copies)  
Attorney General (temporary)  
Special Assistant for Management and Budget  
Press Secretary  
Press

SCHEDULE OF CORPORATE TAXPAYERS WHOSE REBATES WERE PROCESSED AND PAID TWICE

| Corporate Taxpayers               | FIRST PAYMENT - FY 1996 |           |   |                     | SECOND PAYMENT - FY 1997 |           |                     |                     | Date of Stop Payment Order | Date Collected |
|-----------------------------------|-------------------------|-----------|---|---------------------|--------------------------|-----------|---------------------|---------------------|----------------------------|----------------|
|                                   | Check Date              | Check No. | Amount of Check   | Date Cleared        | Check Date               | Check No. | Amount of Check     | Date Cleared        |                            |                |
| 1. EMC2 Electrical                | 09/19/96                | 456920    | \$2,000.00  | 10/03/96            | 09/30/97                 | 8008      | \$2,000.00          | 10/20/97            | 11/21/97                   | 02/10/98       |
| 2. FPA Pacific Corp.              | 09/19/96                | 456923    | 1,387.00  | 09/26/96            | 09/30/97                 | 8015      | 1,387.00            | 02/11/98            | 11/21/97                   | 02/10/98       |
| 3. Hotel Nikko Saipan             | 09/30/96                | 457854    | 190,000.00  | 10/07/96            | 09/30/97                 | 8035      | 190,000.00          | 10/08/97            | 11/21/97                   | 02/13/98       |
| 4. Kambara Kisen Co.              | 09/19/96                | 456937    | 2,885.40  | 10/31/96            | 09/30/97                 | 8062      | 2,885.40            | 11/07/97            | 11/21/97                   | 02/09/98       |
| 5. Mammy House, Inc.              | 09/30/96                | 457857    | 10,000.00   | 10/15/96            | 09/30/97                 | 8068      | 10,000.00           | 10/09/97            | 11/21/97                   | 01/28/98       |
| 6. Microl Corp.                   | 09/30/96                | 457858    | 62,754.38   | 10/04/96            | 09/30/97                 | 8072      | 62,754.38*          | 10/03/97            | 11/21/97                   | 01/23/98       |
| 7. Pantrac Trading                | 09/30/96                | 457860    | 100,497.76  | 10/17/96            | 09/30/97                 | 8094      | 100,497.76          | 10/24/97            | 11/21/97                   | 12/05/97       |
| 8. S.H.A. Project, Inc.           | 09/19/96                | 456969    | 466.00  | 10/07/96            | 09/30/97                 | 8100      | 466.00              | 10/15/97            | 11/21/97                   | 01/27/98       |
| 9. Industrial Bank of Japan, Ltd. | 09/30/96                | 457866    | 281,128.00  | Missing/Outstanding | 09/30/97                 | 8039      | 281,128.00          | 12/23/97            | none                       | not applicable |
| 10. The Sakura Bank, Ltd.         | 09/30/96                | 457867    | 89,177.12   | 10/24/96            | 09/30/97                 | 8119      | 89,177.12           | Missing/Outstanding | 11/21/97                   | not applicable |
| 11. Tsuneishi Research & Dev't.   | 09/19/96                | 456978    | 1,012.50  | 11/12/96            | 09/30/97                 | 8144      | 1,012.50            | 11/07/97            | 11/21/97                   | 02/09/98       |
| 12. Tsuneishi Shipbuilding Co.    | 09/19/96                | 456979    | 9,618.30  | 10/28/96            | 09/30/97                 | 8145      | 9,618.30            | 11/07/97            | 11/21/97                   | 02/09/98       |
| <b>TOTAL CHECKS PROCESSED</b>     |                         |           | <b>\$750,926.46</b>   |                     |                          |           | <b>\$750,926.46</b> |                     |                            |                |
|                                   |                         |           | Less: Replacement check amount - to replace check no. 457866 (see no. 9 under FIRST PAYMENT - FY 1996 above) which did not clear the bank |                     |                          |           | 281,128.00          |                     |                            |                |
| <b>Total Double Payments</b>      |                         |           |   |                     |                          |           | <b>\$469,798.46</b> |                     |                            |                |

\* The actual amount on the second payment check was \$67,554.38. However, only \$62,754.38 pertained to duplicate rebate payment.



Office of the Secretary  
Department of Finance

P.O. Box 5234 CHR B SAIPAN, MP 96950

TEL: (670) 664-1100 FAX: (670) 664-1115

January 27, 2000

SFL2000-118

Mr. Leo L. LaMotte  
Public Auditor, CNMI  
Office of the Public Auditor  
The Commonwealth of the Northern  
Mariana Islands  
P.O. Box 501399  
Saipan, MP 96950-1399



Dear Mr. LaMotte:

**SUBJECT: Draft Letter Report on the Audit of Double Payments of 1995 Corporate Tax Rebates to Eleven Taxpayers**

I am providing the Department of Finance's response to the draft letter report on the Audit of Double Payments of 1995 Corporate Rebates to Eleven Taxpayers.

I wish to emphasize that the Department of Finance had taken immediate steps to recover the double payments of the corporate rebates to the taxpayers. Nine to eleven months before your office conducted the audit, we had already fully recovered the payments as a result of our immediate action. The circumstances surrounding the double payments were unusual because the Department of Finance was in the process of converting to a new financial management system, which may have contributed to the confusion on what steps were needed to be taken to resolve the problem. Due to the length of time it took to release the draft report, we may not be able to make the recommended adjustments because the accounting periods have been closed and the adjustments should have been taken care of in our year end adjustment procedures. Some of the concerns over double payments currently exist because the corporate tax returns are processed manually and rebate checks are issued through the regular accounts payable system. A new tax system is currently in the development stage where the processing of the corporate tax returns will be automated, similar to the processing of the individual tax returns. The project is anticipated to be complete by summer of this year and we will be able to process the corporate tax returns for tax year 1999 on the new system.

Our specific responses to your audit findings are as follows:

1. Obtain written suggestions from the personnel of DOF Accounts Payable Section, the Division of Treasury, DRT, and the Secretary's Office on how to improve communication and coordination, and what internal control policies and procedures should be adopted to avoid double payments.

The Department of Finance has existing policies and procedures on processing claims or complaints of nonpayment for both regular vendor payments and tax rebates. The procedures for claims of nonpayment of corporate rebates will change once the new tax system is completed

*OPA Note:* The memorandum explaining the usage of accounts relative to the NMTIT Rebate Trust Fund is no longer attached to the report.

Public Auditor, CNMI  
01/27/2000  
Page 2

Currently, corporate rebates are processed manually. The Division of Revenue and Taxation prepares a payment voucher and submits a memorandum requesting for payment to the Director of Finance and Accounting, with the concurrence of the Secretary of Finance. The Accounts Payable Section of the Division of Finance and Accounting prepares a payment voucher based on the information provided in the memorandum from the Director of Revenue and Taxation. The CNMI Treasury cuts the check and mails it directly to the taxpayer. Because the corporate tax rebates go through the regular accounts payable system, a separate check register for corporate rebate checks is not produced for the Division of Revenue and Taxation. Consequently the only way that Revenue and Taxation can verify if a corporate rebate check has been processed is to inquire with the CNMI Treasury.

The new tax system, which is currently in the development phase and expected to be completed by summer of this year, will give us the capability to automate the processing of the corporate rebate tax returns. Because the annual returns will be entered and processed through the tax system, the amount of the rebate will be automatically calculated and a rebate check will be generated. Since the whole process will be computerized, the system will automatically flag if a rebate check has already been issued to a particular corporation for a specific tax year. This process will allow for the detection of duplicate processing of a return, and potential double payment of a tax rebate. We anticipate processing the 1999 tax returns on the new system.

The Compliance Branch of the Division of Revenue and Taxation receives complaints of nonpayment of rebates. For corporate rebates, the Compliance Branch will initiate the review process to determine the status of the taxpayer's corporate return, including a review of whether or not a voucher has been prepared and submitted to the Division of Finance and Accounting for payment. If a voucher was prepared, an inquiry will be made to the Accounts Payable Section if the voucher has been received and processed for payment. If it had been processed and a check issued, then the taxpayer is informed as to the disposition of the check (the date the check was cut and mailed to the taxpayer's address). If the check was cut but remains outstanding, then the Director of Revenue and Taxation will request the CNMI Treasury to process a request for stop payment to the Bank and request for a replacement check to be reissued to the taxpayer.

2. Provide a list of the specific internal control features in the new JD Edwards financial management and DRT computerized systems that will prevent or easily allow the detection of double payments.

The JD Edwards financial management system has the capability to recognize and flag potential duplicate payments through the invoice number. If a duplicate invoice number is entered for payment, the system warns the end user of a possible duplicate entry. Non-invoice transactions are more difficult to trace because it will require consistency in the way those transactions are entered into the accounts payable system.

The DRT computerized system on the other hand, will not allow duplicate entry of tax returns for a given tax year which will minimize the likelihood of duplicate payment of tax rebates. We will

provide you with the specifications of the internal control feature of the new tax system once the development phase is completed.

3. Instruct DOE Finance and Accounting Division to adjust and reclassify the following (See Appendix B for the proposed adjusting and reclassifying entries):

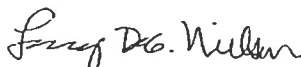
Public Auditor, CNMI  
01/27/2000  
Page 3

The recommended adjustments to prior years could be done if fiscal years 1997 and 1998 were still open. Due to the length of time it took to issue this report, we are not able to make those adjustments because these years have already been closed and audited. Adjustments a), b), c) and d) were accounted for in the year end adjustment procedures for those fiscal years. One of our year end procedures is to transfer the Rebate Trust Fund balance for the prior tax year that had not been paid out as rebates at the end of the fiscal year, and is not considered a rebate liability, to General Fund revenue. The double payment recoveries posted as revenues reduced the revenue amount transferred into the General Fund since it was already recorded in the General Fund. State dated checks are added back to the general fund cash balance at the end of the fiscal year as part of our year end reconciliation procedures.

4. Provide training to cashiers in using the right accounts and in dealing with unusual transactions:  
We concur with the recommendation. A copy of a memorandum explaining the usage of accounts relative to the NMITT Rebate Trust Fund is enclosed for your reference. We will consider developing a manual of the usage of revenue accounts for the cash collection points for their reference guide.

Please let us know if you have any questions on our responses.

Sincerely,



LUCY D.G. NIELSEN  
Secretary of Finance

Attachments (2)

cc: Director of Revenue and Taxation  
Acting Director of Finance and Accounting  
CNMI Treasurer

**AUDIT OF THE DEPARTMENT OF FINANCE'S  
DOUBLE PAYMENTS OF 1995 CORPORATE TAX REBATES TO  
ELEVEN TAXPAYERS IN FISCAL YEAR 1997**

**STATUS OF RECOMMENDATIONS**

| Recommendations  | Agency to Act | Status   | Agency Response/<br>Action Required  |
|--|---------------|----------|--|
| 1. Require the DOF-Accounts Payable Section of the Division of Finance and Accounting to strictly comply with its established control procedure for processing complaints of nonreceipt of corporate tax rebate payments, in particular verifying if previous payment has been made before processing a new payment; | DOF           | Resolved | <p>The Secretary of Finance addressed Recommendations 1 and 2 by stating that a new tax system is currently being developed to give DOF the capability to automate processing of the corporate rebate tax returns. Because the annual returns will be entered and processed through the tax system, the rebate computations and preparation of rebate checks will be part of the automated process. Since the payment data are stored, the system will automatically flag a warning if a rebate check has already been issued to a particular corporation for a specific tax year. This process will ensure the detection of duplicate processings of a return and potential double payment of a tax rebate. The new tax system is expected to be completed by the summer of year 2000. DOF anticipates processing the 1999 tax returns using the new system.</p> <p><i>Further Action Needed</i></p> <p>Recommendations 1 and 2 - Provide OPA copies of the specifications for the internal control feature of the new tax system (once the development phase is completed) that will prevent or easily allow the detection of double payments. Discuss how DOF will handle the processing of the following cases and the control procedures available under the new tax system: (1) an amendment to the original corporate tax return that was successfully processed in the system and a check has been processed and issued; (2) a request for manual rebate check because the corporate tax return is pending in the system (due to data entry error, reporting error, incomplete information or support on tax return, etc.); and (3) a replacement check because the original check issued was missing.</p> |
| 2. Develop and implement control procedures in its financial management system which will recognize and flag potential duplicate processing of corporate tax rebate payments; and  | DOF           | Resolved |  |
| 3. Ensure that prompt and proper adjustments to the CNMI accounting records are made for the affected fiscal year(s) in case any other double payment is found.  | DOF           | Closed   |  |

