



Office of the Public Auditor

Commonwealth of the Northern Mariana Islands

World Wide Web Site: <http://opacnmi.com>

1236 Yap Drive

Capitol Hill, Saipan, MP 96950

Mailing Address:
P.O. Box 501399
Saipan, MP 96950

E-mail Address:
mail@opacnmi.com

Phone: (670) 322-6481
Fax: (670) 322-7812

August 26, 2004

Honorable Juan N. Babauta
Governor
Office of the Governor
Caller Box 10007
Saipan, MP 96950

Dear Governor Babauta:

Enclosed please find a copy of the audited Financial Statements for the CNMI Government for the Fiscal Year Ending September 30, 2002. The audited Financial Statements, representing the consolidated report or "Single Audit" of all government operations, were prepared by the accounting firm of Deloitte Touche Tohmatsu under contract with the Office of the Public Auditor (OPA).

OPA has reviewed the report and has prepared an **Executive Summary** that addresses the primary sections of the audit, including the Audit Opinion, Selected Financial Data, Notes to the Financial Statements and the Auditor's Report on Internal Control and Compliance. OPA's new Financial Audit Unit (Unit) will be responsible for reviewing and generating executive summaries for all future financial audits.

The Unit will also be tasked with coordinating and monitoring all of the CNMI's financial audits in order that OPA may more effectively "*conduct or supervise all audits required for or sought by a Commonwealth Agency*" pursuant to 1 CMC § 7821. As the Federal Government has placed increased emphasis on the timely submission of financial audits and resolution of audit findings and, further, as such timely submission and resolution of audit findings are among primary criteria used to determine future allocation of Covenant 702 CIP assistance, OPA believes the Unit can assist the CNMI meet such requirements.

As reflected in the Executive Summary for the audited year, the CNMI Government has shown continued improvement in its financial reporting and accountability. Overall, the Auditor's Opinion was improved and the noted errors (Audit Findings) reflected a decrease compared to the prior year. Based upon the responses received and the future follow-through by the various agencies, OPA anticipates that the accountability of the CNMI's funds will continue to improve.

As shown in the Executive Summary, during four of the past six fiscal years, from Fiscal Year 1997 through Fiscal Year 2002, the CNMI Government incurred expenditures in excess of its revenue collections. It has been reported that Fiscal Year 2003 will also reflect a deficit.

While it is acknowledged that this six year period represents the most volatile financial period in recent history, OPA is gravely concerned about the continued increase in the CNMI Government's accumulated deficit and the impact it could have on the government's continuing ability to maintain the current level of operations, programs and services.

On the matter of accountability, OPA strongly believes that preparation of separate financial statements for the Commonwealth Health Center (CHC) could lead to improved efficiency for the health center. Presently, neither the CHC nor the Department of Public Health (DPH), of which the CHC is a division, has a separate financial or accounting presentation. In Fiscal Year 2001, the CHC recorded an allowance for uncollectible accounts in the amount of \$73,734,827. This increased dramatically in Fiscal Year 2002 to \$99,802,496. This one year write-off in excess of \$26 million underscores the need for better accountability. The DPH department-wide incurred General Fund expenditures in excess of \$43 million in Fiscal Year 2002, representing the largest departmental operational outlay in the CNMI Government. As such, the lack of separate and audited financial statements for DPH and CHC reduces the accountability of a significant portion of the General Fund.

While there are costs involved in developing a separate accounting presentation for CHC, OPA believes that the benefits derivable would significantly outweigh the costs. This would additionally have the effect of providing specific financial information to management and policymakers. In discussing this matter with the independent auditor, Deloitte Touche Tohmatsu, it was determined that legislative direction would be needed. OPA would welcome the opportunity to discuss this matter with the Administration and the Legislature.

Other items of concern include:

- Repayment of existing general obligation bonds will require increased funding, reducing the funds available to other programs. For Fiscal Year 2002, bond repayment totaled \$5,841,000. This will increase to \$8,084,000 for Fiscal Year 2003 and will again increase for the repayment of the \$40,000,000 Land Compensation Bond funded in Fiscal Year 2004.
- Pension liabilities are unfunded by \$488,693,000. While these are "contingent" in nature, at some future time at least a portion of the unfunded liability will need to be funded. Recent legislative action was taken to address this concern subsequent to the end of the audited fiscal year. It is unknown at this time, however, what impact such legislation will have on the liability.
- An estimated \$24,000,000 in medical claims are unpaid. This amount as a contingency to the Government Health Insurance Program is guaranteed by the General Fund. Again, it

- is unknown what portion of this liability, if any, will need to be paid by the General Fund.
As reported in the Internal Control and Compliance report, a weakness exists in the proper reporting of accounts receivables. Specifically (Finding # 2002-02), Federal Grant Receivables may be misstated, which could lead to an increase in recorded expenditures which in turn would lead to an increase in the deficit.

While these matters are troubling, the enclosed Fiscal Year 2002 audited Financial Statements reflect an improvement in the CNMI Government's overall reporting of financial information and accountability of its financial resources. OPA commends the Department of Finance and the various offices and agencies for their diligence and contributions toward improvements in government accountability.

Very truly yours,

A handwritten signature in blue ink, appearing to read "MS Sablan", written in a cursive style.

Michael S. Sablan, CPA
Public Auditor

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