

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, 2012

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*

Mr. Pedro A. Tenorio
Secretary
Department of Public Lands:

We have audited the financial statements of the Department of Public Lands (DPL) as of and for the year ended September 30, 2012, and have issued our report thereon dated December 13, 2013. We conducted our 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.

Internal Control Over Financial Reporting

Management of DPL is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered DPL's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of DPL's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of DPL's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Responses (pages 3 through 7), we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

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. We consider the deficiencies described in the Schedule of Findings and Responses as items 2012-01 through 2012-04 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether DPL's financial statements are free of 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 that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as items 2012-02 through 2012-04.

We noted certain matters that we reported to management of DPL in a separate letter dated December 13, 2013.

DPL's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. We did not audit DPL's responses and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLC

December 13, 2013

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses
Year Ended September 30, 2012

Purchases/Disbursements

Finding No. 2012-01

Criteria: An effective system of internal control provides for policies and procedures that require expenses to be recorded in the period incurred.

Condition: Tests of thirty-seven nonpayroll expenditures aggregating \$200,335 and nine subsequent disbursements totaling \$75,682 noted the following:

1. Three nonpayroll expenses (document PV nos. 1073292, 1061627 and 1007446) totaling \$24,500 relate to services incurred in a prior fiscal year but recorded as expenses of the current fiscal year. Management did not consider the amount sufficiently material to the financial statements to warrant an adjustment.
2. Two subsequent disbursements (document PV nos. 1103250 and 1111153) totaling \$11,672 were fiscal year 2012 expenses but were not accrued at September 30, 2012. This condition was corrected through a proposed audit adjustment.

Cause: The cause of the above condition is the lack of monitoring procedures over cash disbursements.

Effect: The effect of the above condition is potential misstated liabilities.

Recommendation: We recommend DPL strengthen controls over processing, recording and monitoring disbursements.

Prior Year Status: The lack of monitoring procedures in place for cash disbursements was reported as a finding in the audit of DPL for fiscal year 2010.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Ms. Evelyn J. Sablan, Finance Manager

Corrective Action: DPL will ensure that expenses are recorded within the proper fiscal year and monitor all accruals.

Proposed Completion Date: Closing date of the audit report.

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Schedule of Findings and Responses, Continued
Year Ended September 30, 2012

Revenue/Receipts

Finding No. 2012-02

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 required documents include submitting an annual statement that includes names of stockholders and number of shares owned and reporting on public benefits and training programs being offered to the local workforce.

Condition: Tests of seventy-five cash receipts noted thirteen, or 23%, pertaining to long-term lease contracts and temporary permits that require the lessee to submit financial statements audited by accountants or by certified public accountants and to submit a schedule of gross receipts; however, such audited financial statements or schedule of gross receipts were incomplete or were not in file. The lessee and cash receipt numbers are the following:

<u>Lessee No.</u>	<u>Receipt No.</u>
L0901S	765
L0901S	906
TP0316S	635
T0921S	132
T0603S	393
L0711S	883
L07001T	124
L0901S	721
T0310S	392
L0901S	358
T12032T	2371
L0901S	32
L08001S	529

Two (permit # A080247 and cash receipt # 2312; permit # A0730R and cash receipt # 3395) did not have a valid and authorized permit on file. The last approved permit was in 2008 for permit # A080247 and 2010 for permit # A0730R.

One lease (L07001S) required the lessee to perform an appraisal of the fair market value of the unimproved land after each succeeding five-year term to determine the new annual base rental. The first five-year term ended for the period from 12/26/06 - 3/31/07 to 12/26/11 - 03/31/12, with no appraisal performed. The lessee continues to make payments at the same base rental amount.

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 a schedule of gross receipts, and the lack of valid and authorized permits and required appraisals on file.

Effect: The effect of the above condition is the potential loss of revenues when contracts and/or permits are up for renewal and lease amounts are to be determined.

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Schedule of Findings and Responses, Continued
Year Ended September 30, 2012

Finding No. 2012-02, Continued

Recommendation: We recommend that management endeavor to update the lease contracts and permits and propose a standard threshold which would differentiate those lessees to be audited by certified public accountants from those by regular accountants, or by none at all.

Prior Year Status: The lack of monitoring procedures in place to determine which contracts and/or permits require financial statements or audited financial statements was reported as a finding in the audit of DPL for fiscal year 2010.

Auditee Response and Corrective Action Plan:

Name of Contact Persons: Ms. Evelyn J. Sablan, Finance Manager and Ms. Rachel Roque, Real Estate Division

Corrective Action: DPL will ensure that permittees and lessees comply with the submission of financial statements and BGR, including the renewal of agreements, in a timely manner.

Proposed Completion Date: Closing date of the audit report.

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Schedule of Findings and Responses, Continued
Year Ended September 30, 2012

General Ledger System

Finding No. 2012-03

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.

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

- Pursuant to Public Law 15-02, effective October 1, 2007, disbursement of DPL expenses, including land compensation claims, was centralized at the CNMI Department of Finance (DOF). DPL reimburses DOF for expenses paid on behalf of DPL;
- A general ledger for DPL transactions is maintained by DOF but it is not reconciled or monitored by DOF or DPL;
- 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; and
- Journal vouchers posted to the DOF general ledger by DOF personnel are not approved by DPL management or evidenced as being reviewed by DOF management.

Adjustments to record DPL transactions within the DOF general ledger were recorded by DPL, through proposed audit adjustments.

Cause: The cause of the above condition is the lack of monitoring and timely reconciliation of transactions with DOF, the failure to implement available system controls over the financial reporting process and the lack of established monitoring control procedures to determine the accuracy and completeness of disbursements processed at DOF.

Effect: The effect of the above condition is the lack of reliable and relevant financial information and the inability to timely detect errors and inaccuracies.

Recommendation: We recommend DPL 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 and approve all journal vouchers posted to the general ledger maintained by DOF.

Prior Year Status: The lack of reliable and relevant financial information and the inability to timely detect errors and inaccuracies was reported as a finding in the audit of DPL for fiscal year 2010.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Ms. Evelyn J. Sablan, Finance Manager

Corrective Action: DPL is working with DOF in reconciling accounts payable, payroll disbursements and other journal entries recorded by DOF to determine errors.

Proposed Completion Date: Closing date of the audit report.

DEPARTMENT OF PUBLIC LANDS

Schedule of Findings and Responses, Continued
Year Ended September 30, 2012

Local Noncompliance

Finding No. 2012-04

Criteria: The CNMI Constitution requires that all revenues received by DPL in excess of the amount necessary to meet reasonable expenses of administration and management, land surveying, homestead development, and any other expenses reasonably necessary for the accomplishment of its functions, must be transferred to the Marianas Public Land Trust (MPLT).

Public Law 15-02 required the establishment of the DPL Operations Fund which shall be maintained by 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.

Conditions: DPL has not obtained concurrence from MPLT regarding its method for determining amounts owed. DPL has also not determined the basis of the \$2,000,000 reservation of fund balance at September 30, 2012.

DPL does not deposit revenues received into the DPL Operations Fund.

Not all operational expenses of DPL are paid from the DPL Operations Fund. Specifically, during the year ended September 30, 2012, DPL paid \$690,898 directly to the Northern Mariana Islands Retirement Fund. The payments may have duplicated payments by DOF and DPL has recorded the payments as fully reserved receivables.

Cause: The cause of the above condition is the lack of agreement with MPLT and policies and procedures to determine restricted fund balance and the lack of compliance with Public Law 15-02.

Effect: The effect of the above condition is potential noncompliance with DPL's constitutional mandate to transfer net revenues received to MPLT and with Public Law 15-02.

Recommendation: We recommend that DPL obtain a legal determination on the merits of transfers to MPLT and comply with Public Law 15-02.

Prior Year Status: The lack of agreement with MPLT and policies and procedures to determine restricted fund balance was reported as a finding in the audit of DPL for fiscal year 2010.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Ms. Evelyn J. Sablan, Finance Manager

Corrective Action: DPL will comply with its constitutional mandate to remit net operation proceeds to MPLT.

Proposed Completion Date: Closing date of the audit report.

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Unresolved Prior Year Comments
Year Ended September 30, 2012

The status of unresolved prior year findings is discussed in the Schedule of Findings and Responses section of this report (pages 3 through 7).