
Office of the Public Auditor

Department of Public Lands Management of Land Leases and Temporary Permits



**OPA Report No.
AR-18-01**

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Results in Brief

By law, the Department of Public Lands (DPL) has stewardship of public lands in the Commonwealth of the Northern Mariana Islands (CNMI). The 15th Legislature gave this responsibility to DPL when it enacted Public Law 15-2 (the Public Land Use Act of 2006 or Act) due to prior problems with the management of CNMI public lands. The Act sought to establish additional controls to ensure the administration of public lands complied with the Commonwealth Constitution.

Ten years after the law's enactment, on January 28, 2016, DPL adopted regulations pertaining to leases and temporary occupancy of public lands. Further amendments followed on May 28, 2017 and November 28, 2017. Although DPL has belatedly adopted needed regulations, it has delayed full implementation. The independent auditors' report on financial statements as well as compliance and internal control recommend that DPL review and actively monitor its implementation of regulations within all divisions.

Our audit found that DPL did not have sufficient internal controls in place to effectively manage public land leases and permits. Specifically, DPL did not:

- adopt an updated comprehensive land use plan;
- timely renew leases and temporary permits;
- closely monitor compliance with lease and permit agreements;
- produce billing records, accurately assess fees, and keep reliable records;
- effectively communicate with the Rota and Tinian district offices; and
- adopt standard operating procedures for the management of public land leases and permits.

OPA commends DPL for its effort towards updating the CNMI Comprehensive Land Use Plan (Plan) after a 12-year delay. The updated Plan will serve as both a physical and a policy-based blueprint to manage future development and related stewardship of public lands in the CNMI. A draft Plan was developed in February 2018 and is expected to be completed by August 2018.

We found, however, that without the necessary controls in place and the periodic review of those controls, the CNMI risks potential loss of revenue, improper or unauthorized use of public lands, and noncompliance with laws and regulations.

Introduction

Objective

The objective of the audit is to determine if the Department of Public Lands (DPL) has developed sufficient internal controls to provide reasonable assurance that public land leases are properly managed in accordance with applicable laws and regulations. Please see *APPENDIX 1* for the scope and methodology of our audit.

Background

Public Law (PL) 15-2 (the Public Lands Act of 2006 or Act) established DPL, formerly known as the Marianas Public Lands Corporation, on February 22, 2006. It required the Governor, with the advice and consent of the Senate, to appoint a Secretary to oversee DPL. In addition to giving DPL responsibility over public lands, the Act also required DPL to create and implement a homesteading program, establish commercial leasing and permitting of public lands, settle land claims, and designate public land parcels to other government agencies for the fulfillment of public purposes.

To perform these duties, DPL has seven divisions and two district offices: Administration Division, Finance and Accounting Division, Compliance Division, Homestead Division, Land Claims Division, Planning Division, Real Estate Division, Rota District Office, and Tinian District Office. Of the seven divisions, the Real Estate Division, in coordination with the Compliance Division, Finance and Accounting Division, and the district offices in Rota and Tinian, need to generate income for its operations, maintenance, and administration of all public lands through public land leases and permits.

The Act mandates that DPL shall strictly enforce all terms of every lease and all requirements imposed as a condition of legislative approval of leases or lease extensions. Moreover, the Act requires DPL to develop policies, procedures, and controls related to public lands, some of which would ensure the assessment of rental payments, submission of required financial documents, and the regular appraisal of all public lands leased for commercial purposes. The Act establishes that any public property to be leased for commercial purposes would undergo a public proposal notice process to provide all interested persons with the opportunity to submit proposals. In addition, the Act requires that rental income from public land had to be based on the appraised fair market value, although DPL could negotiate rent based upon current economic conditions.

The Commonwealth Constitution requires DPL to receive all revenues from public lands and retain the amount necessary to cover reasonable costs of administration, management, land surveying, homestead development, and other expenses necessary to carry out its mission. After such operating expenses are withdrawn, the annual net revenues shall be transferred to the Marianas Public Land Trust to be invested. Land leases represent the largest percentage of net revenues that DPL receives, contributing to 76 percent of DPL's overall revenue. See *EXHIBIT A* and *B* for further details.

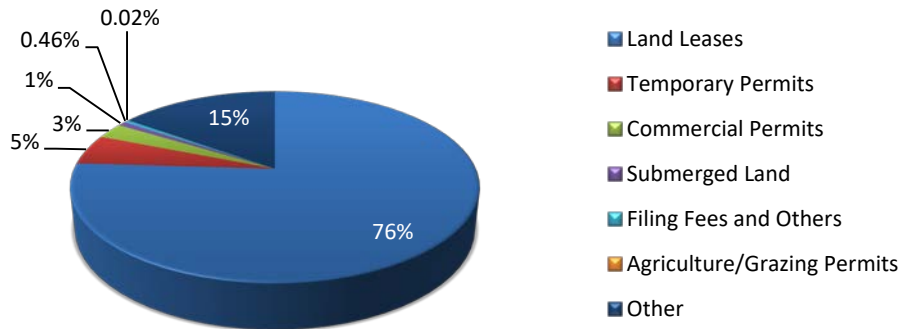
EXHIBIT A

Revenues	2016	2015
Land Leases	\$6,191,351	\$5,297,364
Temporary Permits	416,657	328,639
Commercial Permits	215,902	101,861
Submerged Land	59,511	60,000
Filing Fees and Others	37,634	58,408
Agriculture/Grazing Permits	1,825	7,870
Other	1,229,200	14,686
	\$8,152,080	\$5,868,828
Bad debt	(990,076)	(392,640)
Net revenues	<u>\$7,162,004</u>	<u>\$5,476,188</u>

Source: Financial Statements and Independent Auditors' Report for Year Ended 9/30/2016 and 2015.

EXHIBIT B

**Revenues
for Year Ended 9/30/2016**



Source: Financial Statements and Independent Auditors' Report for Year Ended 9/30/16

Since its inception in 2006 until 2016, DPL had not developed regulations to manage public land leases and temporary permits. On January 28, 2016, DPL adopted rules and regulations which govern the leasing and temporary occupancy of public lands whether by permit, lease, or temporary authorization. Under these regulations, commercial use of public lands cannot be authorized or permitted without a valid lease, temporary occupancy agreement, permit, or concession agreement. The regulations also require that lease rental payments in subsequent years would not be lower than in previous years despite possibly lower market values. The regulations pertaining to leases and temporary permits have been subsequently amended on May and November 2017. See *EXHIBIT C* for additional details regarding the current fees.

EXHIBIT C

	Application Processing Fees	Basic Rent	Additional Rent
Lease	\$5,000 or 0.5% of the estimated value of the property	At least 5% of the fair market value, appraised every 5 years	At the most 3% of BGR
Agricultural/Grazing Permit	\$225 (livestock) \$250 (farming)	\$25 per hectare annually	
Parking Permit	\$ 50	Annually <u>Commercial Purposes:</u> \$10 per sq. m (primary) \$6 per sq. m (secondary) \$2 per sq. m (tertiary) <u>Non-Commercial/Non-Profit Purposes (All Zones):</u> \$2 per sq. m	
Signboard Permit	\$ 50	<u>Commercial Purposes:</u> \$600 Annually (primary) \$350 Annually (secondary) \$250 Annually (tertiary) <u>Non-Commercial/Non-Profit Purposes (All Zones):</u> \$250 Annually \$50 Monthly	
Roadside Vendor Permit	\$ 50	\$250 per month	1% of BGR
Maintenance Permit	\$100 (Commercial) \$ 20 (Residential)	2% of the fair market value annually (Commercial)	
Commercial Motion/Still Filming or Photography Permit	\$ 50	\$250 per day \$500 per day (Managaha)	
Still/Portrait Photography (Not for commercial reproduction)	\$ 50	\$1,000 annually	
Staging Permit	\$ 50	8% of the fair market value annually	
Quarry Permit	\$ 50	\$12,000 annually (shall increase by 5% in each subsequent year)	\$3.00 per cubic yard (royalty) plus 0.50% of BGR
Encroachment Permit	\$ 50	<u>Commercial Purposes:</u> 8% of the fair market value or 3% of BGR annually <u>Residential Purposes:</u> 8% of fair market value annually	
Concession Permit	\$ 75	\$250 per month	3% of BGR
Underground Telecommunication Cables	\$ 50	5% per year of 50% of the average market value annually	
Telecommunication Tower	\$ 50	8% of the estimated fair market value annually	

Source: Department of Public Lands, Regulations

Findings

Our audit found that the Department of Public Lands (DPL) did not develop sufficient internal controls to provide reasonable assurance that public land leases are managed in accordance with applicable laws and regulations. Specifically, DPL did not:

1. Adopt an updated comprehensive land use plan as required by law;
2. Renew lease agreements and temporary permits in a timely manner;
3. Closely monitor compliance with lease agreements and permits;
4. Prepare billings, accurately assess fees and keep reliable accounting records;
5. Effectively communicate with the Tinian and Rota district offices; and
6. Adopt standard operating procedures for the management of public land leases and permits.

Previous audits conducted by the Office of the Public Auditor (OPA), including those conducted by the independent auditor, have reported inadequate monitoring and enforcement of lease provisions and permit agreements. OPA's prior audit on quarry leases reported on DPL's inability to collect substantial amounts of lease rental and related interest amounting to an estimated \$4.7 million from 1990 to 1995 (see *APPENDIX 2* for more details on prior audits). Furthermore, in DPL's audited financial statements for fiscal year 2016, cumulative receivables amounted to approximately \$18.9 million, however, a net receivable amount of only approximately \$1.5 million was determined to be collectible. This represents an accumulated bad debt loss of about \$17.4 million.

DPL has made some progress implementing regulations pertaining to public land leases and temporary occupancy agreements (TOA's or permits) in early 2016 and subsequent amendments in 2017. Nevertheless, DPL cannot achieve its objectives or its Constitutional and legal mandates without implementing an effective internal control system.

A Comprehensive Land Use Plan Was Not Adopted

Article XI section 5(f) of the Commonwealth Constitution mandates DPL to adopt a comprehensive land use plan with respect to public lands including prioritizing uses and amending the plan as appropriate. The Public Lands Act of 2006 (Act), requires DPL to adopt and promulgate a comprehensive land use plan in February 2007. In addition, the law requires the plan be updated every five years beginning in 2012, and again in 2017, and so on.

The Act outlined numerous objectives of the plan, summarized as follows: (1) to coordinate the public land use and development with the plans, programs, and requirements of other government agencies; and (2) to identify all public lands and prioritize their use for homestead development, revenue generation, rights-of-way, and areas that require special attention due to the presence of critical resources or hazardous materials.

Similarly, DPL's mission statement, reiterates this Constitutional and statutory mandate:

The mission of the Department of Public Lands (DPL), as trustees for public lands in the Commonwealth, is to *develop and adopt a strategic land use plan* that promotes cultural and economic growth for the benefit of our present and future generations. The plan provides for the efficient and effective services in the management, use, disposition and development of public lands for the economic and social betterment of the Commonwealth.

The CNMI has changed drastically since the 1980s, due in part to the influx of foreign investors and an increasing desire to use land for commercial growth. In keeping with the Commonwealth Constitution and DPL's mission, proper planning is critical to avoid under or over use of resources, thereby developing public lands to maximize public benefit.

OPA found that DPL did not adopt a comprehensive land use plan in 2007 and missed subsequent updates in 2012 and 2017 as required by law. Instead of proceeding with the updates, DPL relied on an outdated existing plan adopted in 1989, thus impeding DPL's ability to maximize the use and development of public lands and avoid potential revenue loss.

On May 2017, the House of Representatives introduced House Bill 20-81 to restrict DPL from executing future public land leases until it adopted a plan. Although this bill remains in the House, had it been passed into law it could have affected potential revenue generation on future land leases. Revenue loss means fewer funds available for operations including homestead development and investment for the indigenous population through the Marianas Public Land Trust.

DPL's failure to develop a strategic management plan ensuring compliance with legal requirements and DPL's mission led to a 12-year delay in adopting a land use plan. Also contributing to the delay, the Legislature failed to hold officials accountable and provide the funding necessary to achieve DPL's fiduciary responsibilities.

Despite the 12-year delay, however, OPA commends current DPL management for awarding the contract on August 11, 2017 to update the plan for Rota, Tinian, Saipan, and the Northern Islands. The updated plan will serve as both a physical and policy-based blueprint to manage the future development of public lands in the CNMI. The project is divided into four phases with a final completion date of August 2018.

OPA recommends:

DPL adopt and implement a comprehensive land use plan.

Leases and Temporary Permit Renewals Were Untimely

Timely renewal of public land leases and temporary permits is a critical practice especially after adopting new regulations establishing rental fees, penalties, and holdover charges. As evident in the leases and permits reviewed, the new regulations require that lessees and permittees submit renewal requests *two years* prior to lease expiration and *two months* prior to permit expiration, allowing for adequate time to process before holdover status begins.

OPA found that leases and permits were not renewed timely. DPL’s records show that out of 80 leases and 240 temporary permits, 13 leases and 169 permits expired as of March 31, 2017.

Leases

The number of expired leases make up about 16 percent of the 80 total leases. The status of each expired lease as of January 2018 is as follows: (see *EXHIBIT D* for details)

- 2 were approved by the Legislature;
- 3 are pending approval by the Legislature and;
- 8 are under negotiation and have not been submitted to the Legislature.

Of the eight leases that have not been forwarded to the Legislature, two have been expired since 2011, one since 2012, four since 2014, and one since 2016. Once these leases have expired, they continued to be paid for on a month-to-month basis. Review of 12 of 13 total expired lease agreements show that a holdover fee was not stipulated, and therefore DPL did not collect these additional revenues. The regulations adopted in 2016 now require a holdover fee of 150 percent of the latest basic rent.

EXHIBIT D

Lease	Term (Yrs.)	Expiration	Time Lapse as of 3/31/17	Request for Legislature approval
Approved by the Legislature on January 5, 2018				
L89-03S	25	01/17/2014	3 yrs., 2 mos.	10/16/2017
L90-10S	25	12/31/2015	1 yrs., 3 mos.	08/31/2016
Submitted to the Legislature for approval				
L90-15S	25	05/31/2015	1 yrs., 10 mos.	12/01/2017
L90-14S	25	08/31/2015	1 yrs., 7 mos.	12/01/2017
L90-16S	25	08/31/2015	1 yrs., 7 mos.	12/01/2017
Under Negotiation between DPL and Lessee				
L86-10S	25	08/08/2011	5 yrs., 7 mos.	
L86-27S	25	10/31/2011	5 yrs., 5 mos.	
L86-09S	25	02/03/2012	5 yrs., 1 mo.	
L89-02S	25	01/17/2014	3 yrs., 2 mos.	
L89-01S	25	01/17/2014	3 yrs., 2 mos.	
L91-04S	25	11/31/2014	2 yrs., 4 mos.	
L90-06S	25	12/31/2014	2 yrs., 3 mos.	
L07-001S	10	12/25/2016	0 yrs., 3 mos.	

Source: Department of Public Lands

Temporary Permits

The number of expired temporary permits (169) as of March 2017 make up about 70 percent of the 240 total permits. Out of our sample of 22 temporary permits, we noted that 14 temporary permits (or 64 percent) had expired and not been renewed at the time of our review.

Among the agriculture and grazing permits (AGP’s), as well as the beach concessions selected for review, all 10 samples had expired. DPL staff informed OPA that DPL has not renewed AGP’s, due to controversies that arose from the adoption of new regulations surrounding the fees and insurance requirements and DPL’s anticipation of amendments in 2017. However, our sample testing showed that DPL had not renewed AGP’s for many years prior to the adoption of new regulations in January 2016. For example, one permit (A94-01R), expired in 2009, and two permits (06-03S, A06-03T) expired in 2012.

In one particular AGP-related case, OPA found no documents supporting public land use authorization. In January 2014, DPL received an application to take over a deceased relative’s AGP lot located on Tinian, but an authorizing permit was never issued even though DPL assigned a permit number (A14-003T) to the applicant, which it included in the listing of active permits.

We calculated the average time it took DPL to execute renewals, finding anywhere from four to 24 months from the time it received the renewal request. However, some AGP’s and beach concessions required even longer processing time. As a result, permit renewals cover periods with a break in term coverage. For example, if a renewal was not issued for a certain period of time, term coverage is backdated to cover the missed period of term coverage caused by the lengthy renewal time. See details in *EXHIBIT E*.

EXHIBIT E

Permit no.	Term Start	Term End	Execution Date
05-51S	5/1/2015	4/30/2016	4/10/2015
Renewal	5/1/2016	4/30/2018	8/25/2017
11-029S	4/1/2015	3/31/2016	3/19/2015
Renewal	4/1/2016	3/31/2018	8/11/2017

Source: Department of Public Lands

As for beach concessions, another form of temporary permit, OPA found that all 13 were expired, including two that OPA reviewed. The oldest of these permits expired in 2011. During an interview, DPL staff informed OPA of a moratorium placed on beach concessions at around that time, and a task force was developed to discuss designating one area for all beach concessions. DPL informed OPA that the task force has not been active and the moratorium has never been lifted.



Exhibit F. Beach Concession

DPL provided numerous reasons to OPA for the untimely renewal of leases or permits. According to DPL, renewal processing takes longer than expected due to: (1) untimely submission of documents by the lessee or permittee, (2) delays on the part of DPL, (3) anticipated amendments to the regulations due to public concerns, and (4) delays on the part of the Legislature.

Although these reasons are valid, DPL also has no written guidelines to clearly establish responsibilities and coordination among the divisions renewing leases and permits. OPA was informed that the Real Estate Division (RED) will not initiate a renewal unless the Compliance Division forwards the files. OPA also found letters indicating conditional approval from the Compliance Division and stating that a draft permit would be prepared by RED. In these instances, however, OPA did not find renewal permits in the files.

In addition, no consequences are imposed on a lessee or permittee for failure to comply with renewal requirements. DPL, (see finding 3), does not rigorously enforce lease and permit provisions requiring specific documents to be submitted.

Allowing a lease to extend beyond the initial 25-year term, by defaulting to a month-to-month lease arrangement could potentially be seen as offending the Commonwealth Constitution. For example, the public land lease that expired in 2011 continued month-to-month for an additional seven years without the scrutiny and statutorily required approval of the Legislature. However, once a lease's extension is approved by the Legislature, the 15-year term is reduced by the number of years past the lease's expiration. In addition, because most permits were expired before adoption of new regulations and renewals, DPL has delayed implementation of the new regulations.

DPL may not be able to control the delays in the Legislature, however it can influence how employees, management, lessees, and permittees respond to those delays.

OPA recommends:

DPL develop written guidelines that establish clear lines of responsibility and coordination among the divisions for the execution of timely lease and permit renewals. Furthermore, the Secretary or the designee should monitor these functions and hold employees accountable for their work.

Compliance with Lease Agreements and Permits Were Not Closely Monitored

DPL's Compliance Division plays a major role in DPL's overall operation with responsibility to stringently enforce and monitor lease and permit compliance as required by 1 CMC § 2808(a). In addition, DPL's regulations, specifically NMIAC §§ 145-70-101(b) and 202(a)(4) also provides that DPL shall periodically monitor compliance with leases and permits. Furthermore, the requirements set forth in the lease and permit agreements, mandate DPL to monitor the submission of required documents. These include financial statements, appraisal reports, business gross receipts, and insurance coverage—all necessary for the assessment of rent and asset protection. DPL's default provision in its lease agreements also state that a lessee shall automatically be in default for failure to cure such breaches within 30 days and after written notice from DPL. Moreover, DPL's permit agreements state that a permittee shall automatically be in violation if the permittee fails to cure a violation within 15 days after written notice from DPL; also all rights under such an agreement may be terminated.

OPA's review of four lease samples revealed that:

- Only one appraisal report (L09-04S) was submitted in a timely manner. One lessee (L08-009T) did not submit its latest report when due in October 2013. One lessee's (L90-03R) appraisal report could not be located in DPL's files, even though references made to it were noted on another reviewed document, which prevented OPA from determining its timely submission. Finally, one lessee's (L11-03S) appraisal report was submitted four months late and review by the in-house appraiser was not completed until eight months later.
- For the three leases required to submit business gross receipt (BGR) forms and financial statements, we found that BGR documents were complete for one lessee (L11-03S). However, we did not find complete records for one lessee (L90-03R), and forms were not current for one lessee (L09-04S).
- Financial statements are required to be submitted annually. We could not locate the 2015 and 2016 financial statements for three lessees (L90-03R, L09-04S, L11-03S). After OPA's January 25, 2018 inquiry with the Finance and Accounting Division (F&A) staff, OPA received financial statements for two lessees (L09-04S-dated April 5, 2017 but unstamped with DPL's stamp of receipt; and L11-03S-submitted January 30, 2018 stamped with DPL's date of receipt). DPL informed OPA that the third lessee had not responded to their request.

Furthermore, OPA's review of 14 temporary permit samples (12 other permits, two beach concessions) revealed that:

- During the time of our review in October and November 2017, four of the 14 permittees (05-51S, 16-031S, 02-21S, and 12-032T) were not current with their BGR documents and nine of the 14 permittees had not submitted their up-to-date liability insurance policy.

Likewise, the independent auditors reported the lack of monitoring procedures as a repeated finding on internal control and compliance for fiscal years (FY) 2010 to 2016. In FY 2016, their sample testing of 45 cash receipts for long-term lease contracts and temporary permits revealed that: (1) audited financial statements and a schedule of gross receipts listing sources and deductions were not provided for 11 lessees as required by the contracts and permits; (2) one lessee submitted its financial statements, but was not audited by a certified public accountant as required by the lease agreement; and (3) appraisals were not performed for two lessees, although required by the lease agreement.

During our analysis of F&A's processes, OPA identified a promissory note for a former lessee's tenant (sub-lessee) who did not vacate public land after their lease expired. OPA conducted a follow-up interview and found that DPL discovered the sub-lessee's presence on public land only by chance. DPL staff stated that its division does not have the time or resources to conduct inspections of unleased lands. As such, instances like the example are on an as-seen basis.

OPA was informed that DPL assigned uniform expiration dates for each permit category and that inspections were conducted once per year. However, OPA noted during its review of 14 temporary permits that the Compliance Division did not conduct an inspection for six permittees in 2014 and 2015, four permittees in 2016, and eight permittees in 2017. For AGP's, two of the

eight were not inspected within the last three years. If inspections are not conducted every year, annual renewals required by regulations may be difficult to implement.

In addition, close-out inspections are not performed to ensure that lessees/permittees are compliant with terms and conditions of their agreements, applicable laws, and regulations. It is important to note that the Rota District Office incorporated a close-out inspection as part of the office's processes to address this issue and provided OPA with the close-out inspection report for review. The staff found that it was necessary to conduct close-out inspections upon termination of the Agreements to ensure lessees/permittees are in full compliance.

DPL currently does not have a monitoring system to ensure that required documents are submitted when due, and not merely when inspections are scheduled. Untimely submission of, or complete failure to submit, required appraisals and financial documents may result in potential loss of revenue. This is an ongoing concern because these financial documents dictate the annual base rent and additional rent for lessees and permittees. During our review in October 2017, one lessee did not submit its appraisal report when due in October 2013 and therefore the new rental rate could not be assessed by DPL.

During our interview, DPL claimed that it collects back rentals once an overdue appraisal report is submitted. However, the collection of back rentals could potentially become difficult if the dollar amount is significant. To illustrate, the independent auditors reported that in FY 2016, DPL's receivable amounted to about \$18.9 million, and of this total, DPL expects to collect about \$1.5 million (or 7 percent) in net receivables. This indicates that historically, collections have been problematic, with a history-to-date allowance for bad debt of \$17.4 million or 93 percent considered uncollectable.

OPA recommends:

DPL develop a tracking system to monitor the submission of required documents when due and adopt policies and procedures to ensure lessee's/permittee's compliance with the terms and conditions of its agreement, applicable laws and regulations.

Billing Records Were Not Produced; Fees Were Not Accurately Assessed; Records Were Unreliable

To ensure that an entity collects the correct fees as stipulated in the lease and permit agreements, accurately billing and assessing fees is a good practice. The following are examples of the fees assessed and collected by DPL: (1) application processing fee (APF), (2) basic annual rent, (3) additional rent (in most agreements, additional rent applies if a percentage of BGR is greater than the basic rent), (4) penalty fee, and (5) holdover fee. Also, keeping reliable accounting records help management make sound decisions and project future revenues.

Regular billings are not a standard practice at DPL, and instead DPL relies on the lessee or permittee to submit their payments on time.

Our review of 22 temporary permits found that DPL did not consistently assess and/or collect the following fees from permittees: (1) APF, (2) basic annual rent, (3) additional rent (BGR), and (4) holdover. See *EXHIBIT G* for permittees whose fees were not consistently assessed.

EXHIBIT G

Permit No.	Type of Permit	Application Processing Fee	Annual Rent	Additional Rent (BGRT)	Holdover Fee
06-03T	Agriculture & Grazing	✓			
06-03S	Agriculture & Grazing	✓			
A08-005S	Agriculture & Grazing	✓	✓		
12-008T	Agriculture & Grazing	✓	✓		
A11-017S	Agriculture & Grazing		✓		
02-21S	Beach Concession	✓		✓	✓
12-032T	Beach Concession	✓		✓	✓
16-031S	Concession	✓		✓	✓
02-12S	Container Storage	✓			
05-51S	Encroachment			✓	
08-050R	Encroachment				✓
10-26S	Maintenance				✓
05-51S	Parking				✓
09-08S	Parking				✓
04-05S	Roadside Vendor			✓	✓

Source: Department of Public Lands

In one of our lease samples, the lessee's (L11-03S) additional rent was computed at a lower amount because BGR taxes were excluded from the gross revenue amount. In another example, a permittee (07-22T) computed royalty fees at \$2.00 per cubic yard despite the rate of \$1.75 as stipulated in its agreement with DPL. Accounting records showed that DPL relied on the amounts paid by the lessee without thoroughly reviewing their rental computation. OPA's computation showed a credit balance of about \$2,250.



Exhibit H: Quarry

Furthermore, DPL maintains two sets of ledgers one in the Peachtree accounting software and one in Microsoft Excel. OPA was informed that DPL uses Peachtree to record all revenues, and Microsoft Excel is used only to compute adjustments and related penalties. Once the new amount is computed in Microsoft Excel, the adjusting entry then is recorded in Peachtree. However, in one of the samples (TP 02-12S) reviewed in March 2017, DPL's accounts receivable report as of March 2017 showed that the permittee did not have an accounts receivable (AR) balance. OPA later found a letter placing the permittee on holdover status. OPA discussed the holdover status with DPL staff discovering it was an oversight on their part and that a billing would be prepared. A review of the permittees account ledger revealed that DPL amended the original entries recorded from July 2015 through March 2017, as opposed to recording the adjustment dated at the time the computation was done. This is not considered a proper accounting entry and affects the prior year's audited figures.

Rental amounts and other related fees payable under all lease/permit agreements are not consistently assessed accurately or collected in a timely manner. This hinders DPL's ability to produce reliable financial information and improve its collection efforts. This also means that the other DPL divisions do not have reliable information with which to determine the lessee's/permittee's compliance.

For our sample selection, OPA calculated forgone revenue amounting to approximately \$18,000. Forgone revenues would have been substantially higher had OPA sampled the entire population.

These errors occurred because (1) there are no written policies and procedures governing the assessment and collection of rental payments; (2) staff lack the proper accounting education, necessary training, and supervision; (3) staff are not familiar with the terms and conditions of the agreements; and (4) DPL does not have a reliable accounting system.

OPA recommends:

DPL (1) review and monitor all leases and permits to ensure that fees are properly assessed; (2) develop and implement written policies and procedures governing the assessment and collection of rental payments; (3) assist and provide adequate training for accounting staff; and (4) utilize a reliable accounting software to eliminate redundant tasks and process transactions efficiently.

Communication with the Tinian and Rota District Offices was Ineffective

Effective communication is vital for any organization to meet its intended goals. The *Standards for Internal Controls in the Federal Government* (Standards), issued by the Government Accountability Office, state that effective information and communication are vital for an entity to achieve its objectives. This means that management should communicate quality information down and across reporting lines to enable its staff to perform key roles in achieving objectives, addressing the risks, and supporting internal controls.

The Saipan office stated that it works collaboratively with district offices on matters relating to the initiation and execution of TOA's for public lands located in their respective islands. However, the district offices indicate that they have not received clear guidelines. In addition, pertinent information that may assist the district offices to do their jobs more effectively was not made available to them.

Samples tested from the district offices show that, although draft TOA's were forwarded to the Saipan office, the status of those drafts were not communicated. In one example, a permittee (A14-003T) submitted an application for an AGP in 2014. Upon receipt, the Tinian office forwarded the draft to the Saipan office, but never received an update. Because such drafts are not finalized, permittees were allowed to operate on public land without a renewal permit, or in the case cited, a permit. OPA site visits confirmed that the property was still being used despite the absence of a permit agreement. The Rota office had a similar concern. Our review of Rota's records showed that AGP applications were submitted and forwarded to the Saipan office. However, when applicants received no status confirmation after several follow-up attempts, some opted to withdraw them.

In addition to the lack of internal communication, copies of approved long-term leases and TOA's are not consistently provided or communicated to the district offices for reference. Among our sampled lessees, OPA did not find an appraisal report for lessee "L08-009T" in files maintained by the Saipan office, which told us that the missing appraisal report may have been submitted and filed with the Tinian office. During our visit to Tinian, however, we found that the staff had no knowledge of the lease and, therefore, had no records pertaining to that lease and had not conducted any inspections to determine lessee compliance. Further, OPA received no file for permittee "08-050R" having been advised that the permittee's file might be maintained by Rota office. We did locate the file in Rota, but found it to be incomplete.

The Standards also require management to evaluate internal and external data sources for reliability, including obtaining data on a timely basis to aid in effective monitoring. In DPL's case, management failed to disseminate the master list of all leased/permitted public lands to the district offices, restricting significant responsibilities such as required inspections, as in the example of Lease No. L08-009T. In addition, the Saipan office did not have an updated listing of AGP's on Rota and Tinian. The district office staff confirmed during our visit that only at OPA's request did the Saipan office communicate with their district offices, who in turn created a list to give to OPA. In another example, OPA inquired about the status of AGP's on Tinian, specifically, those in the leaseback area. The Tinian District Office staff stated that the leaseback agreement had expired in July 2016, making the office hesitate to collect payment from permittees until clear directions come from the Saipan office on how to proceed with TOA processing, fees, and AGP in the leaseback area.

DPL does not effectively communicate expectations and information regarding public land leases with its divisions and district offices. The lack of communication and lack of written guidelines and procedures have resulted in poor policy implementation and execution, leaving room for potential abuse and misuse of public lands.



Exhibit I: Agriculture & Grazing

OPA recommends:

DPL should (1) consistently communicate and monitor the operation in Tinian and Rota to ensure that public land leases are being monitored for compliance; and (2) establish and implement written procedures that guide coordination between its offices and clearly delineate responsibility for maintaining adequate land lease records.

Standard Operating Procedures Were Not Adopted

Standard operating procedures (SOPs) ensure that an entity achieves its mission through efficiency, quality output, and uniformity of performance, while reducing miscommunication and noncompliance with laws and regulations. As a best practice, the Standards state that "management documents in policies the internal control responsibilities of the organization."

Furthermore, 1 CMC § 2808(c) of the Commonwealth code requires that DPL develop administrative policies, procedures, and controls related to public land.

While DPL staff have mentioned the existence of SOPs adopted by the former entity Marianas Public Land Authority (MPLA), only the Compliance Division provided OPA with a copy of its SOPs. However, we found these SOPs to be outdated. They neither reflect nor support DPL’s current processes. MPLA’s and DPL’s current structure is not the same. Their structures are derived from different laws and regulations. The Standards also state that “management [should] periodically review policies, procedures, and related control activities for continued relevance and effectiveness in achieving the entity’s objectives or addressing related risks.” Having a set of policies and procedures in place is necessary to mitigate risk, for example in the previously mentioned sub-lessee, where we found inadequate review of rental computations, missing required documents, and other items.

An interview with the F&A staff illustrates the importance of SOPs. OPA came across a promissory note for a former lessee’s tenant (sub-lessee) operating on public land without authorization. The Compliance Division staff mentioned that the discovery was made by chance. This example highlights the need to reassess policies and procedures to include closeout inspections ensuring that lessees or sub-lessees vacate public land when a lease or permit is terminated. The Rota office has initiated its own closeout procedures finding it necessary to ensure that lessees/permittees comply with their agreements, as well as applicable laws and regulations.

DPL staff interviewed by OPA have recognized the need to update policies and procedures to reflect current practices and regulations. OPA noted that DPL had started updating their SOPs. This project is ongoing.

Exhibit J: Auto Repair Services



Interview with DPL staff confirmed the absence of procedures for monitoring the submission of financial documents and the assessment of fees, despite these procedures being required by the law. F&A relies on the Compliance Division for the submission of required documents.

1 CMC § 2808(c)(8) also requires that “[p]rocedures are established for the regular appraisal of all public lands leased for commercial purposes, which ensure that the fair market value basis for computation of minimum annual rental payments for any given lease is updated no less frequently than every five years.” Despite DPL’s current regulations, NMIAC § 145-70-301, referencing appraisals, the regulations remain insufficient to ensure that appraisals are submitted within the required time.

Because management did not update or create written procedures to guide staff, DPL has not been able to ensure that public land leases are being managed in accordance with applicable laws and regulations. Outdated SOPs hinder DPL’s ability to work efficiently.

OPA recommends:

DPL should adequately develop and adopt administrative policies and update its SOPs to ensure accountability, compliance with laws and regulations, guidance for decision-making, and streamline its internal processes.

Conclusion and Recommendations

DPL has proven through the years that it has not effectively managed public land leases and temporary permits. Despite efforts to adopt regulations, DPL will continue to face challenges managing the CNMI's public lands without an updated comprehensive land use plan, proper management review, effective communication, and consistent implementation of standard operating procedures. DPL management also needs to take a more active role in overseeing, reviewing, and updating its internal control system regulating leases and temporary permits while also communicating quality information internally and externally to improve efficacy and mitigate related risks.

In addition to the recommendations presented below, OPA would like to stress the importance of continuously monitoring the internal control system and updating as deemed necessary to ensure that DPL achieves its mission and accomplishes its goals and objectives.

Recommendation Summary

We recommend that DPL:

1. Adopt a comprehensive land use plan as required by law.
2. The Secretary or the designee should monitor all functions and hold employees accountable for their work.
3. Adequately develop and adopt administrative policies and update SOPs to ensure:
 - a. clear lines of responsibility and coordination among the divisions and district offices to ensure the timely execution of leases and permits, maintenance of adequate land lease records;
 - b. leases and permits are reviewed and monitored for compliance;
 - c. rental fees are timely billed, assessed, and collected;
 - d. pertinent information is communicated to the district offices to carry out DPL's mission and comply with laws and regulations.
4. Develop a tracking system to monitor the submission of required documents and consistently review, maintain, and update the master list to accurately track all active public land leases and permits.
5. Assist and provide adequate training for accounting staff; and utilize a reliable accounting software to eliminate redundant tasks and process transactions efficiently.

Summary of Responses

Please see *APPENDIX 3* for OPA's response and *APPENDIX 4* for DPL's detailed response.

Appendix 1. Scope and Methodology

The scope of our audit covered Saipan, Rota, and Tinian leases and temporary permits, as well as, the revenues assessed and collected from October 1, 2014 through March 31, 2017. In addition, when necessary, OPA reviewed documents outside the intended scope. To achieve our objective, we performed the following:

- Gained an understanding of:
 - Laws and regulations, policies and procedures applicable to DPL’s public land leases and short-term permits such as
 - Public Law 15-2, “The Public Lands Act of 2006”;
 - 1 CMC § 2801 *et. seq.*; and
 - NMIAC Title 145, Chapter 70.
- Interviewed staff and conducted a walk-through of DPL’s processes and internal control procedures in the following divisions and district offices:
 - Administrative Division;
 - Real Estate Division;
 - Compliance Division;
 - Finance and Accounting Division;
 - Planning Division;
 - Rota District Office; and
 - Tinian District Office.
- Reviewed controls currently in place to ensure that:
 - Public land leases were executed in a timely manner;
 - All terms and conditions of leases and permits were enforced;
 - All leases and permits were accounted for and have complete files;
 - All rental fees were assessed and checked for accuracy; and
 - Lease payments were collected in a timely manner.
- Randomly selected four leases, 14 Temporary Occupancy Agreements, and eight Agricultural/Grazing Permit. A total of 26 short and long-term leases were reviewed and tested for completeness, compliance, and accuracy, as well as timeliness of payments and collection.
- Summarized audit results.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Appendix 2. Prior Audit Coverage

Independent Auditors' Report

The Independent Auditors' Report on Internal Control and on Compliance for years ended September 30, 2010 through September 30, 2016 identified weaknesses in internal control and on compliance, where DPL did not enforce its policies for leasing public lands.

Office of the Public Auditor, CNMI

Audit Report No. AR-00-04

OPA's prior audit of DPL's collection of rentals on land leases with quarries showed that DPL failed to collect substantial amounts of lease rentals and interest during the six lease years from 1990 to 1995. The audit identified a potential recovery of about \$4.7 million of which \$946,968 was written-off, leaving a balance of about \$3.7 million still recoverable. Of the \$3.7 million, only \$896,747 was recovered from seven quarry operators as stated on the "Report on CNMI Agencies' Implementation of Audit Recommendations as of December 31, 2014" issued by OPA.

Department of Interior, Office of Inspector General

Audit Report No. 96-I-596

The United States Department of the Interior, Office of the Inspector General (OIG) also released an audit report on the management of public lands on March 20, 1996. OIG concluded that DPL did not effectively develop management policies, procedures, and controls related to public land, which resulted in the following: (1) the Commonwealth lost \$118.4 million on completed exchanges of public lands; (2) lost revenues of \$25.1 million on exchanged public lands that was leased to a developer by landowners; (3) lease revenues of \$565,000 were lost; (4) homestead recipients improperly received \$7 million from unauthorized sale or lease of the lots; and (5) homestead lots were awarded to applicants who were ineligible or who did not have the greatest need.

Appendix 3. OPA Response

Auditor's Response to Agency's Comments:

Pursuant to 1 CMC § 7823(a) audited entities are required to submit a response within 30 days explaining whether the entity agrees or disagrees with OPA's findings. The law further states that recommendations shall be implemented unless otherwise agreed on by the Public Auditor.

DPL provided OPA with a 19-page response on June 26, 2018. OPA updated *EXHIBIT C* to include three additional categories at DPL's request on page five of the report. We appreciate DPL's responses in this regard.

However, the bulk of DPL's response related not to the audit findings or recommendations, but to various circumstances that would excuse or mitigate the findings. In this regard OPA has found nothing to change the basic report findings. The complete response by DPL can be found in *APPENDIX 4*.

The following is OPA's comments to specific statements in DPL's response.

OPA Detailed Response to Auditee Concerns:

General Concerns:

DPL expressed concern regarding the established scope of the audit. As noted in *APPENDIX 1*, the scope of our audit covered leases and temporary permit, as well as, the revenues assessed and collected from October 1, 2014 through March 31, 2017. Scope is determined by the auditor and can be modified by the auditor when necessary. This is particularly true when a mistake is discovered in one year that actually occurred either before or after the year(s) in question.

DPL responded that had OPA conducted an audit sooner for leases and permits, it was likely that regulations would have been in place or that a comprehensive land use plan would have been adopted sooner. OPA disagrees with DPL's response. DPL's performance should not be contingent on whether OPA conducts an audit or not. In addition, OPA noted that previous audits found reoccurring findings dating back to 1996 that have not been addressed to date.

OPA FINDINGS	OPA'S RESPONSE
<p>1. DPL did not adopt an updated comprehensive land use plan as required by law.</p>	<p>OPA acknowledges DPL's efforts in updating the comprehensive land use plan (Plan). OPA noted DPL's July 2018 completion date for the final draft and adoption by August 2018. Nevertheless, the Public Lands Act of 2006 (Act) required DPL to adopt and promulgate a Plan by February 2007. The Act also required that the Plan to be updated every five years, thereafter. As noted in this report, DPL missed both the deadline for the report but also the subsequent updates. If DPL feels that the required updates are too frequent, DPL should work with the legislature to amend the requirements of the Act.</p> <p>Furthermore, OPA acknowledges the Attorney General's response in Standing Committee Report No. 20-61 pertaining to House Bill (HB) 20-81. However, the Attorney General also commented that "if the legislature's concern is the DPL's activities in managing public lands without the land use plan may result in public land use that is inconsistent with a future land use plan, then the bill may be sufficient." At the minimum, a revision to clarify that the bill will only apply to new leases and that it shall sunset when DPL adopts a land use plan was also suggested by the Attorney General. In essence, had HB 20-81 (inclusive of the suggested revision) been passed into law, it could have affected revenue generation from future land leases.</p> <p>OPA will conduct a follow-up review semi-annually to determine if DPL has adopted and implemented a comprehensive land use plan.</p>
<p>2. DPL did not renew lease agreements and temporary permits in a timely manner.</p>	<p>OPA acknowledges and supports DPL's creation of true internal auditor position. In addition, whether or not DPL experiences loss of revenue on expired leases or permits, it is best practice to have leases/permits renewed in a timely manner to avoid any potential liability and ensure timely payment.</p> <p>OPA will conduct a follow-up review semi-annually to determine if DPL has developed written guidelines that establishes clear lines of responsibility and coordination among the divisions for the execution of timely renewals of leases and permits.</p>
<p>3. DPL did not closely monitor compliance with lease agreements and permits.</p>	<p>The results of our audit revealed that DPL did not closely monitor compliance with lease agreements and permits. Furthermore, DPL also provided OPA a copy of "Directive No. 005" evidencing the lack of monitoring and reconciliation procedures as a recurring finding by the independent auditor which dates back to 2010.</p> <p>OPA will conduct a follow-up review semi-annually to determine if DPL has developed a tracking system to monitor the submission of required documents when due and adopt an updated SOP to ensure compliance with the terms and conditions of agreements, applicable laws and regulations.</p>
<p>4. DPL did not prepare billings, accurately assess fees, and keep</p>	<p>DPL concurred that the department did not send billings regularly during the scope of the audit. OPA disagrees that "notices in the form of a billing is not necessary". On the contrary, billings serve as a reminder to clients of when payment is due and the applicable fees would have been assessed if payment</p>

<p>reliable accounting records.</p>	<p>is not received timely. This also ensures that staff are consistently monitoring client’s accounts and assessing the correct fees.</p> <p>OPA acknowledges DPL’s purchase of an accounting software—SAGE 100 ERP, sometime last year, and its efforts in procuring a specialized trainer for DPL’s accounting staff. OPA will conduct a follow-up review semi-annually to determine if the new accounting software has been fully implemented.</p>
<p>5. DPL did not effectively communicate with the Tinian and Rota District Offices.</p>	<p>In her response, DPL Secretary stated that she will now require: 1) biannual visits to the district offices; 2) provide training for new hires and existing staff, including attendance at DPL’s annual Professional Development Day; 3) resident directors to commute to Saipan bi-annually to keep apprised of DPL matters and to follow-up on their respective matters; and 4) establish guidelines for tracking incoming and outgoing documents to the district offices.</p> <p>OPA commends DPL for consulting with the district offices to determine a better communication plan to streamline its processes and other matters. OPA will conduct a follow-up review semi-annually to determine if DPL’s corrective action plan addresses OPA’s finding and recommendations.</p>
<p>6. DPL did not adopt standard operating procedures for the management of public land leases and permits.</p>	<p>OPA acknowledges that DPL inherited SOPs from its predecessor. However, OPA disagrees that the existing MPLA SOP is sufficient in carrying out DPL’s existing goals and objectives because it does not reflect nor support DPL’s current processes. DPL staff have confirmed during interview that the existing SOPs are outdated and some have not received a copy of the SOPs. In addition, OPA requested for copies of existing SOPs, in which, all but one (Compliance Division) could not provide OPA with the requested document. Furthermore, 1 CMC § 2808(c) requires that DPL develop administrative policies, procedures, controls related to public land. This statement in essence, requires DPL to adopt SOPs or update its existing SOP. SOPs are detailed steps or procedures required to perform an activity within a process. DPL claims that the rules and regulations are sufficient; however, it does not indicate specifics of how a task is to be accomplished.</p> <p>OPA will conduct a follow-up review semi-annually to determine if DPL has adequately developed and adopted administrative policies and updated its SOPs to ensure accountability, compliance with laws and regulations, guidance for decision-making, and streamline its internal processes.</p>

Appendix 4. Agency Response



Commonwealth of the Northern Mariana Islands
Office of the Governor
DEPARTMENT OF PUBLIC LANDS



June 26, 2018

Mr. Michael Pai, CPA
Public Auditor
Office of the Public Auditor
P.O. Box 501399
Saipan, MP 96950

RE: DPL's response to OPA's Draft Report on the Audit of the Department of Public Lands Management of Public Land Leases and Temporary Permits

Dear Public Auditor Pai:

Thank you for your letter dated May 18, 2018, to the Department of Public Lands (DPL) with the attached draft audit report for leases and temporary permits.

Inconsistencies appear in that the Office of the Public Auditor (OPA) established a scope from October 1, 2014 through March 31, 2017, and yet references to past audits and a house bill that have not become law. DPL feels that the report went outside of its scope and must therefore remove these references inclusive of references to DPL's predecessors. As this report will become public, the progress DPL made under this administration and during my tenure as DPL Secretary, will be overshadowed by past findings, and alleged past wrongdoings of former MPLA Board, and previous DPL Secretaries actions and inactions.

Thank you for recognizing DPL's current accomplishments and our efforts in improving internal processes. We are committed to DPL's bottom line by maximizing collections for the benefit of the rightful owners of public lands, the people of Northern Marianas descent.

OPA: Results in Brief (page 2) *Although DPL has belatedly adopted needed regulations, it has delayed full implementation.*

DPL response: DPL delayed implementing the renewal of temporary permits due to inadvertent rates that were adopted on February 7, 2016 (Attachment 1), as part of DPL's rules and regulations (see attached Notice of Adoption) (Attachment 2). This includes rates for parking permits being assessed at a quarterly rate instead of annual rate. This inadvertently quadrupled parking permit rates. DPL notified affected permittees of this rate hike as seen in the attached letter to M&H Corporation (Attachment 3). Although it was always DPL's intent to correct the rate, the overwhelming opposition to the new rate led to DPL delaying implementation until the permit fee was corrected and properly adjusted to reflect an annual basis instead of the inadvertent quarterly rate (see attached memo dated June 15, 2017, Attachment 4). Therefore, it

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was not until the new rate went into effect on June 7, 2017, that DPL proceeded to implement the correct (amended) rate.

Additionally, DPL delayed implementation of the Agricultural and Grazing Permit (AGP) rates, as DPL needed legal clarification. For clarification, DPL promulgated and published regs in January 2016. It was adopted on February 7, 2016. I assumed the position on 02/01/2016 and in one of my first meetings with the division directors; I learned that the regulations were drafted by DPL's Legal Counsel but not all divisions were given the opportunity to vet or comment on the proposed regulations. Should the divisions be allowed to participate in the drafting of the regulations, the issues that occurred would have likely been cleared before being adopted.

AGP permit holders were required to pay higher rates as required in the February 7, 2016 regulation. In the process of amending the AGP rules and regulations, DPL consulted with United States Department of Agriculture (USDA) Natural Resources Conservation Service (NRCS) to obtain feedback on appropriate standards for the sizing for cattle head per area, for subsistence use, and the rates proposed. Please see attached comments from Ignacio V. Cabrera and Pamela Aguon dated April 26, 2017 (Attachment 5). After consultation with NRCS, DPL proceeded with additional amendments to reduce the fee by removing the additional per square meter fee imposed as described in the November 28, 2017, Commonwealth Register (Attachment 6) which was adopted on December 7, 2017 (see attached Notice of Adoption) (Attachment 7). As seen in the attached letter dated June 1, 2018 from Compliance Division Director to the DPL Secretary, DPL will proceed with implementing the new rates and renewing AGP permits.

DPL also experienced delays in implementing the regulations as there were no insurance requirements for AGP outlined in the regulations. DPL's Legal Counsel at the time advised that where insurance was silent in the TOA section of the regulations, DPL had to use the lease insurance minimum, which was at \$1,000,000 up to \$5,000,000. This high premium for leaseholds impacted AGP's whom operate for family subsistence. This caused several permittees to cancel permits and even delayed the issuance of new and renewal permits as this insurance requirement had to be satisfied. It was not until promulgation of the amendments adopted on June 7, 2017 (Attachment 8), that DPL was finally able to implement the regulations as TOA's were given their own set of insurance requirements, which excluded AGP's.

OPA: We found, however, that without the necessary controls in place and the periodic review of those controls, the CNMI risks potential loss of revenue, improper or unauthorized use of public lands, and noncompliance with laws and regulations.

DPL response: DPL opposes this statement. There are controls in place – Standard Operating Procedures (SOP's) and necessary triggers for periodic review. DPL's Finance Division charges compounded interest to all permittees and lessees who do not pay. For example, DPL's Real Estate Division will initiate a renewal Temporary Occupancy Agreement (TOA) or a lease. During the renewal process, Finance Division will still charge a holdover rate plus compounded interest up until a renewal is executed. Therefore, the statement of loss of revenue is inaccurate. DPL's Compliance Division also conducts inspections. Clients are notified of pending documents for submission during these inspections. There are controls in place, the statement of

loss of revenue is inaccurate, as DPL’s collections have surpassed forecasted revenue year over year for the past three years.

	Forecasted Revenue	Actual Collections	Surplus
2016	\$3,632,188	\$4,340,678.45	\$708,490.91
2017	\$4,291,375.64	\$5,238,008.87	\$946,633.20
2018	\$4,854,044	\$3,491,239	\$1,362,805

Since the Office of the Public Auditor (OPA) believes this statement to be true, it should provide some recommendations on what “necessary controls” to employ. Also, please clarify what use of public lands is improper. This statement is ambiguous.

OPA: Introduction, Background (page 4) *Since its inception in the 1990’s until 2016, DPL had no developed regulations to manage public land leases and temporary permits*

DPL response: As stated on page 3, DPL was created by Public Law 15-2 on February 22, 2006. Reference to DPL’s inception in the 1990’s is therefore incorrect as the previous entities were unique and had different legal structures. Also, since it is stated in Appendix 1 that the scope of the audit was from October 1, 2014 through March 31, 2017, references to DPL or its predecessors before or after this specified scope should be removed. Should there be a need to reference predecessors, please state the name of the entity such as Marianas Public Land Corporation, Division of Public Lands under the Department of Lands and Natural Resources, Office of Public Lands, Marianas Public Lands Authority, or some other entity.

Although I cannot answer for 1990-2015, I firmly believe that if OPA audited DPL sooner for leases and temporary permits, it is likely that the regulations would have been in place much sooner.

Exhibit C (page 5)

DPL response: Please correct Exhibit C to include the following changes:

- Insert Parking Non- Commercial/Non-Profit annual rate - \$2.00 per square meters for all zones
- Insert Signboard Non- Commercial/Non-Profit annual rate - \$250.00 annually; \$50.00 monthly for all zones
- Insert annual Telecomm Underground rate of 5.0% per year of 50.0% of the average market price of lands on the island where trenching occurs

OPA: Findings (page 6) *Adopt an updated comprehensive land use plan as required by law and Findings, Paragraph 2 (page 7)*

DPL response: The first land use plan was adopted in 1989. The horizon of that plan was 25 years placing us at 2014. Upon creation of DPL, PL 15-2 mandated DPL to adopt a land use plan. In 2007, DPL attempted to update the land use plan but the plan did not finalize. In 2015, DPL issued RFP 15-DPL-070 (Attachment 9). In 2015, all of the proposals were in excess of

DPL's budget of \$300,000 with the exception of Ristroph Law. After DPL selected Ristroph to update the plan, they rescinded their proposal. DPL then went into negotiations with the second best proposee, SSFM. However, since SSFM's best and final offer exceeded DPL's budget, DPL did not enter into a contract with SSFM. DPL went to the legislature to request for more funding and secured \$1,000,000 to update the land use plan (Attachment 10). In 2016, DPL proceeded with issuing an RFP for the land use plan, which led to signing a contract with SSFM otherwise now known as PEGS.

In fact, the draft plan was published on DPL's website in February 2018. The final draft will be available in July 2018 and depending on the comments from the public and stakeholders, DPL may adopt the plan in August 2018. By the time this report is published, DPL would have already satisfied PL 15-2 in this respect.

DPL questions OPA's claim that the lack of an updated land use plan impeded "*DPL's inability to maximize the use and development of public lands and avoid revenue loss.*" There are simply too many factors to consider to simply state that a land use plan would have prevented such loss. Please note that demand for public lands is market driven and that the land use plan has no impact on the market pricing. However, DPL did continue to collect revenue from all leases even in the absence of an updated land use plan. To state that an adoption of the land use plan would avoid revenue loss is unfounded. DPL has also refrained from leasing sites of community interest such as Garapan Fishing Base and Mt. Tapochao, in the absence of a land use plan. DPL's Planning Division also conducted periodic land use reviews for all potential land leases or permits.

OPA: Findings (page 6) *Renew lease agreements and temporary permits in a timely manner*

DPL response: DPL has made strides in improving internal processes, which in turn allow for timely processing extensions of lease agreements and renewal of temporary permits. Formation of DPL's regulations has been a priority to allow for consistency amongst leases and permit issuances and now DPL's next objective is to update existing SOP's to improve internal processes. As such, DPL recently hired an internal auditor, who will perform the following duties (Attachment 11):

Ensures compliance of established DPL mission, objectives, policies and procedures, relevant federal and Commonwealth statutes and regulations; assists in developing strategies, goals, and objectives for the Department; assists in preparation of the annual audit plan that identifies and plans internal audits of the operations to ensure program compliance; performs audits, reviews, and evaluations of Division operations; and performs other related duties as assigned.

The incumbent began on June 11, 2018. This position will work closely with the following divisions: Real Estate, Compliance, Accounting, and Land Claims to audit processes and make recommendations to improve areas of inefficiency or oversight.

OPA: Findings (page 6) *Closely monitor compliance with lease agreements and permits*

DPL response: Tying into the earlier finding (above), DPL's standard operating procedures, which established a system currently in place, ensures regular monitoring of all leases and

permits and that they are in compliance with their respective agreements by way of conducting periodic on-site inspections. In order to ease inspections, DPL adopted a uniform expiration policy. For example, all AGP's expire on January 31, parking permits expire on February 28, and signboards and maintenance expire on March 31, etc. This policy helped to streamline and ease the inspection processes as well as allow Real Estate, Compliance, and Finance Divisions to smoothly transition all renewals.

OPA: Findings (page 6) *Prepare billings, accurately assess fees and keep reliable accounting records*

DPL response: To understand better, the concept of billings is not a typical process in the case of land leases as the lessee and lessor established rent at the time of lease was executed. Each lease clearly indicates rental amounts and when appraisals are due. Additionally, the frequencies of those payments are already determined. Therefore, notice in the form of a billing is not necessary. However, DPL's Finance Division has continued to review accounts receivables and have called clients regarding unpaid accounts.

It is DPL's practice to send billings to customers whose accounts are 30 days or over. This practice ensures that accounts do not become delinquent. Once an account becomes non-compliant i.e. delinquent, Finance Division notifies the Compliance Division so that they issue a Notice of Violation (NOV). For your reference, you will find a copy of DPL's letter to lessee L9403S (Attachment 12). During the scope of this audit, DPL did not send billings regularly as the Finance Division identified that more staff were needed and there was an absence of positions for their division. However, since creating two new full-time positions and hiring two (2) accounting personnel, DPL has been able to identify delinquent accounts within the statute of limitation and has been billing them in an effort to collect on this debt.

The efforts DPL has made in correcting this should be recognized. DPL already procured a new accounting software system, which will improve the ability to maintain the General Ledger System, a required system of internal control. The contracted representative, Ernst & Young (EY), advised DPL that their employee who specialized in Sage 100 ERP, terminated employment with them and therefore, EY could no longer fulfill the training component. This delayed implementation due to lack of training; however, a bid has already been published (Attachment 13). Presently, DPL is in the process of procuring a trainer specialized in Sage 100 to train all accounting staff. Once implemented, it will eliminate redundant manual inputting of transactions and improve the integrity of our financial management system and DPL's reporting capabilities. This measure will also be an added measure to ensure compliance with lease agreements and permits where it concerns collections. Also, as mentioned earlier, DPL hired an internal auditor to help monitor necessary controls.

Furthermore, because I am fully aware of my fiduciary responsibility and in the interest of working for the rightful landowners, people of Northern Marianas descent collectively, I have instituted Directive No. 005 (Attachment 14). DPL division directors for Accounting, Compliance, and Real Estate meet monthly with the Special Advisor and/or the Secretary to discuss the following:

- Establishing new goals and procedures, identifying areas needing improvement;

- Discussion of progress made for lessees and permittees;
- Delinquent accounts;
- Billing summaries (updated monthly)
- Discussion of newly executed leases and permits;
- Discussion of improving internal process through creation of a database to house all information pertaining to leases and permits, with a tracking mechanism and alert of expiration and scheduled inspections, with monitoring for selected users such as the Secretary, Finance Director, Compliance Director, Real Estate Director, Internal Auditor, and Financial Management Advisor; and
- Discussion of creating checklists advising when BGR and appraisals are due to be placed in Finance and Compliance files for monitoring.

OPA: Findings (page 6) *Effectively communicate with the Tinian and Rota district offices*

DPL response: A system is already in place wherein Resident Directors submit to the Secretary monthly reports detailing status updates, delays, progress, and recommendations. The Secretary then responds to these reports and follows-up with other respective division directors or legal counsel on the status of pending matters. Please note that DPL divisions are interdependent on each other. Division Directors have and continue to assist Resident Offices with various processes (Attachment 15). Additionally, Resident Directors teleconference the main office during DPL's monthly director's meeting.

Consultation with the Tinian and Rota office determined that better communication measures must be implemented. As such, I will require:

- Secretary to visit Tinian and Rota bi-annually;
- District Offices to send their new hires to Saipan for training purposes and provide training refreshers for existing staff;
- Resident Directors to fly to Saipan bi-annually to keep apprised of DPL matters and to follow-up on their respective matters;
- Establishment of better guidelines in tracking incoming and outgoing documents to the District Offices
- Require annual participation in Professional Development Day (PDD)

Lastly, I have reminded all directors to utilize the resources available for communication purposes – email correspondence, phone calls, memos, etc. These means of communication are all in practice already and have been effective.

OPA: Findings (page 6) *Adopt standard operating procedures for the management of public land leases and permits and Findings, Standard Operating Procedures Were Not Adopted, Paragraph 4 (page 15)*

DPL response: Please note that a meeting with all directors on June 7, 2018, confirmed that every division does have a standard operating procedures (SOP) in place. It states that there is an absence of SOP's for the leasing of public lands. Please see the attached SOP's for leasing of public lands (Attachment 14). Also, DPL uses the adopted rules and regulations to guide the

process of executing new leases and permits as well as renewals. Further, an interested lessee must submit all documents under the requirements to lease public land (Attachment 16). These can also be found on our website.

DPL inherited all existing SOP's from its predecessor and feels that the SOP's, as is, are sufficient in carrying out existing goals and objectives. However, this audit did reveal that DPL must prioritize re-training all personnel in understanding the organizational structure and internal processes. All staff were required to attend DPL's PDD which was held on September 30, 2017. DPL's Legal Counsel spoke at the PDD and discussed the processes of DPL's regulations. Smaller mentoring sessions were held at DPL's conference room on at least two other occasions.

To mitigate this matter, DPL will:

1. Re-train existing personnel, including Tinian and Rota Directors, to review and understand existing SOP's
2. Require all new hires (especially Rota and Tinian personnel) to receive formal training in their respective field at the main Saipan office
3. Require all Division Directors to review existing SOP's and make recommendations to update annually and as needed

As noted earlier, with DPL's new hire of an Internal Auditor, implementing Sage 100, and employing new internal policies, DPL can proceed in refining its internal processes and adopting policies that are consistent with DPL's goals and objectives. However, please note that nowhere in PL 15-2 does it require DPL to adopt SOP's on leasing land. The rules and regulations are sufficient. Instead, this "finding" should simply be a recommendation.

OPA: Findings, Paragraph 2 (page 6)

DPL response: The \$17.4 million allowance for bad debts accounts are the accumulated delinquent customers since the 1980's. Some of these companies went out of business and are no longer in existence. Our letters to them have been returned which tells us that they may no longer be on-island and most of these bad debts stem from signing of public land leases in the 80's and 90's and some in 2000 without DPL (at the time) ensuring developers were financially capable of completing their projects. A lease was signed and Finance continued to assess fees on rental plus compounded interest, but the lessee failed to build and never developed the property. DPL then terminated the lease (later) for abandonment. However, charges accrued from the inception of the lease to the termination. To remedy this, DPL strictly enforces all items under the "Basic Requirements for Leasing" (earlier stated as Attachment 17), specifically, ensuring that there is verifiable evidence of funding for completion of the developer's project. Of the total bad debt, \$12,446,556.19 is proposed to be written off. Please see attached letter to Deloitte and Touche, which mentions the draft write-off policy (Attachment 12).

In addition, DPL hired two (2) additional accounting staff to assist with monitoring aged receivables. DPL has been billing all delinquent accountings since March 2018. As an example, please see the attached letter (Attachment 17). Since we began initiating this process, DPL has billed a total of \$608,991.10 and as of June 18, 2018, \$354,532.10 was collected.

OPA: Findings, Paragraph 3 (page 6)

DPL response: DPL has made substantial efforts in implementing regulations pertaining to public land leases and temporary occupancy agreements (TOA's or permits) plus DPL has consistently collected revenue higher than projections – refer to the table on page 3. This should not be underscored by the fact that DPL is still in the process of making amendments to existing regulations as DPL is constantly looking to refine, improve, and streamline its processes thereby creating an efficient, consistent, and fair application to all lease and TOA transactions.

It must also be recognized that DPL created the position of Internal Auditor to ensure that one employee with accounting and auditing experience is dedicated daily to review all internal processes not just limited to Finance Division's processes but also inclusive of land exchange transactions, etc. Thank you for recognizing that DPL has made some progress in 2016 and 2017 (Paragraph 3, Page 6).

OPA: Findings, Paragraph 3 (page 7)

DPL response: As stated in Standing Committee Report No. 20-61 dated August 14, 2017, Honorable Attorney General Edward Manibusan noted that he "reviewed the N.M.I. Constitution and applicable law and find no legal impediment to its desired outcome." Further, AG Manibusan stated that "this [the bill] conflicts with Article XI §4(f) which vests control over public lands within the Executive Branch as well as Public Law 15-2 which requires DPL to adopt a comprehensive land use plan (Attachment 18)." The bill was clearly in conflict with PL15-2 and the functions within the Executive Branch. To assume that the bill (if it became law) would lead to revenue loss is a matter of speculation. The mention of this bill to further OPA's position is outright wrong. OPA's findings should come from a matter of fact and not an assumption.

Further, OPA audited DPL in 2013 and did not cite DPL for lack of land use plan. Should OPA have cited DPL at the time, it is likely that a plan may have been implemented sooner. The legislature also continued to request DPL at budget hearings and the land use plan was a full-blown topic. Thank you for recognizing "current DPL management for awarding the LUP contract" (Paragraph 5, Page 7).

OPA: Findings, Paragraph 4 and 5 (page 7)

DPL response: DPL takes the position that OPA's report is 12 years past due and that this finding is incredibly untimely as DPL will have a land use plan adopted in a matter of two months.

There is no mandate to develop such strategic management plan that in the absence of, led to a 12-year delay of adopting a land use plan. Where is OPA going with this? This comment should be a recommendation, not a finding. Again, should OPA have cited DPL years ago, secretaries before me may have initiated a land use plan already.

OPA: Findings, Leases and Temporary Permit Renewals Were Untimely, Leases (page 7, 8, 9, and 10)

OPA: Paragraph 1 (page 7)

DPL response: DPL’s regulations require the lessee to inform DPL of their desire to extend at least two years prior to the expiration of the lease. Almost all of the existing leases predate DPL’s regulations. If the regulations do not apply to leases executed before the adoption of the regulations, then OPA cannot state, “all agreements include a clause requiring lessees and permittees to submit renewal requests two years prior to lease expiration and two months prior to permit expiration...”

OPA: Paragraph 1 (page 8)

DPL response: Although most of the leases predate the regulations, there is the language of holdover fees in the lease agreements. Leases that do not have holdover fees were based on management decisions in granting and executing a lease at the time. Therefore, there were no “additional revenues” to collect because the agreements were written that way. However, since the adoption of the regulations, all new leases are subject to the holdover fees.

Lease	Expiration	DPL Comment
L86-10S	02/28/2012	<ul style="list-style-type: none"> • Lease expired February 28, 2012 (25 years) • Lease agreement contains holdover clause • Request for lease extension submitted to DPL on June 11, 2011 • Appraisal submitted by Lessee on March 5, 2012 • Lessee requested to reduce leasehold size on March 7, 2012. New survey and appraisal report required of Lessee • Approved survey to reduce leasehold size submitted to DPL on February 25, 2013 • New appraisal report for reduced area submitted but needed revision. Revised appraisal received on April 10, 2013 and approved by DPL Secretary on May 6, 2013 • Original Lease Agreement does not have option to extend lease • Lessee submitted letter to amend lease to include provision for an option to extend the lease on March 26, 2014. • First Amendment to include option to extend lease for an additional 15 years. Lessee accepted amendment. • First Amendment signed on June 30, 2014 by the Acting Attorney General Gilbert Birnbrich and former Secretary, Pedro A. Tenorio on July 7, 2014. • DPL transmitted signed First Amendment to Lessee for signature, however, it was returned unsigned. • Main contact for the Lessee resigned. • DPL was assigned new Legal Counsel in 2015 that advised on how expired leases will be processed if extension is requested. New appraisal report with improvements required. Annual rental now based on 6% of appraised market value. • New contact for Lessee introduced and informed of lease renewal process. • Received appraisal report with improvements on March 21, 2017 • Per DPL new rules and regulations, Conversion to Telecommunications Tower Temporary Occupancy Agreement (TOA) recommended and approved, due to higher percentage (8%) of annual rental based on appraisal.
L86-27S	10/31/2006	<ul style="list-style-type: none"> • Lease expired on October 31, 2006 • 10 year lease with three options to extend for 5 years each

		<ul style="list-style-type: none"> • Lease agreement contains holdover clause • Lessee requested for a new 25 year lease on October 24, 2006 • DPL drafted new lease agreement for negotiations with Lessee in May 2011 and continued. • Changes in DPL Legal Counsel from May 2011 to February 19, 2015, (4 DPL Legal Counsels within the period) • Draft lease agreement still negotiated in 2015 • New Legal Counsel assigned to DPL in 2015 advised possible reconsideration of whether to enter into lease or not as lease is related to federal government • Former Secretary Pedro A. Tenorio put negotiations on hold in December 2015 • New regulations state that all leases shall be commercial. This is a non-commercial activity. Reviewing authorization of land encumbrance with DPL Legal Counsel.
L86-09S	02/03/2012	<ul style="list-style-type: none"> • 25 year lease • Lease agreement contains holdover clause • Request to extend lease received on February 27, 2012 (after its expiration on February 3, 2012) • DPL requested for payment of lease extension application fee and appraisal report without improvements on April 18, 2012 • Appraisal report received on April 12, 2014 in relation to the request for lease extension • Appraisal was reviewed by former Staff Appraiser and returned to Lessee on September 30, 2013 for revisions. • Appraisal received on March 12, 2014 NOTE: Normally, after the review of the appraisal report and if approval is recommended, the report is forwarded to the Real Estate Division to incorporate the new rental fee in the draft extension or lease renewal agreement • New appraisal report with improvements required. Annual rental now based on 6% of appraised fair market value • Real Estate will process lease renewal upon review and approval of the appraisal report
L89-02S	01/17/2014	<ul style="list-style-type: none"> • 25 year lease. • Lease agreement contains holdover clause • Request to extend lease received on June 12, 2013 • Account reflected outstanding balance at time of lease extension request • Request to waive interest fees by Lessee • Request from Lessee to offset certain repairs after Typhoon Soudelor • Specified amount for Typhoon Soudelor expenses approved by DPL for offset • Lessee in arrears to date • Real Estate will finalize process of lease renewal upon Lessee's clearing its arrears and other compliance matters
L89-01S	01/17/2014	<ul style="list-style-type: none"> • 25 year lease • Lease agreement contains holdover clause • Request to extend lease received on June 1, 2011. • DPL requested for payment of lease extension processing fee and appraisal without improvements on October 3, 2011. • Lease extension processing fee received on May 2014. • Secretary approved the appraisal report on January 10, 2018 for the 2nd ten-year period. A new appraisal is needed for the lease extension. • Real Estate will process lease renewal upon review and approval of the appraisal report

L91-04S	11/31/2014	<ul style="list-style-type: none"> • 25 year lease • Lease agreement contains holdover clause • Request to extend lease received on August 15, 2013 • Lessee requested to include an adjacent public land site approved by DPL predecessor, MPLA (Board) with the lease extension. • Amendment to lease to include adjacent public land prepared. Signed by DPL and Lessee in October 2014. • On June 18, 2018, DPL concurred that rent for additional public land should be charged from the date of second amendment. • Real Estate will finalize process of lease renewal upon Lessee's clearing its arrears and other compliance matters
L90-06S	12/31/2014	<ul style="list-style-type: none"> • Lease agreement does not contain holdover clause • Request to extend lease received on January 29, 2015 • Recommend to convert the lease to an encroachment TOA as a portion of the building is on public land and majority is on private land. TOA Rental will be based on 8% of appraised market value or 3% BGR.
L07-001S	12/25/2016	<ul style="list-style-type: none"> • 10 year lease with option to extend for additional 10 years • Lessee was informed verbally to submit renewal letter • Request to reduce monthly payment with submittal of appraisal report on November 29, 2012 • Staff Appraiser reviewed appraisal, which was returned to Lessee on July 1, 2013 with a letter from Staff Appraiser to conduct re-survey of property and recommendations for revisions (copy of this letter delivered to appraiser). • Our records do not show that a revised appraisal report was submitted • Recommend to convert the lease to a commercial encroachment TOA as a portion of the building is on public land and majority is on private land. The lease on private land will expire prior to a 15-year extension. TOA Rental will be based on 8% of appraised market value or 3% BGR, whichever is greater.

Some lessees that submitted lease extension requests were not in compliance with their leases, including non-payment and non-submission of appraisals. Some examples of the lessees in arrears are L89-02S and L91-04S and DPL has been working with these lessees to bring their accounts up-to-date. For leases L86-10S, L90-06S, and L07-001S, they consist of small premises and encroachments, and recommendations will be made to convert them to Temporary Occupancy Agreements for Telecommunications Tower (based on 8% of Appraised market value (AMV) vs. 6% of AMV and no alternative BGR, can be renewed up to 25 years) and Commercial Encroachment (based on 8% of AMV and or 3% of BGR, whichever is higher, vs. 6% of AMV and no alternative BGR).

The Real Estate Division in the past, upon receiving a lease extension request would forward a memo to both Compliance and Finance Divisions alerting them of the extension requests. The memo would ask for assistance in determining whether the lessee is in compliance with terms and payments, and if it is recommended to extend such lease. RED will continue to do such and develop a check list for the Secretary, Internal Auditor, Finance Division, Compliance Division, Real Estate Division, and DPL's Legal Counsel, to ensure follow-ups and all aspects of lease extensions are processed correctly and in a timely manner. An interoffice routing sheet for all correspondence from DPL and from the lessee regarding the lease extension is in draft form will

be prepared and utilized to allow proper circulation to all DPL divisions and staff involved in the lease extension process.

OPA: Paragraph 4 (page 8)

DPL response: Beach concessions and AGP's would be part of the list of the 169 expired permits. As discussed on the first page of this response, DPL is in the process of updating and processing renewals for all AGP's. With the new regulations came new and higher fees for Agricultural and/or Grazing activities.

RED experienced delays renewing TOAs due to the following factors:

- Not receiving all documents or payments from permittees to update their file and determine them in compliance with their permit or TOA. The Real Estate Division (RED) developed a renewal form with the Compliance Division with a checklist of these items according to the type of business entity they are registered as in the CNMI. A copy of this form was provided to OPA by RED Director (Attachment 19).
- Regulations adopted in 2016 – The regulations for Temporary Occupancy did not include insurance coverage amounts, therefore the former legal counsel advised to utilize the insurance coverage amounts for long-term leases as follows:

LIABILITY INSURANCE

The Lessee shall, from the Commencement Date of this Lease, procure and maintain in during the entire term of this Lease or any extension thereof, at its sole expense, commercial general liability insurance (all risk) for the Premises and operations conducted thereon, with the DPL and the CNMI Government as named co-insured, in a company or companies authorized to do business in the Northern Mariana Islands, with a minimum coverage of \$1,000,000 per occurrence / \$5,000,000 in the aggregate or such higher amounts as the DPL may reasonably require. Copies of such policies shall be delivered to the DPL within thirty (30) days of their issuance, and shall contain a clause requiring at least thirty (30) days' written notice shall be given to the DPL prior to cancellation or refusal to renew any such policies. Lessee agrees that if such insurance policies are not kept in force during the entire term of this Lease, the DPL may procure the necessary insurance, pay the premium therefore, and such premium shall be repaid to the DPL immediately upon the DPL's demand.

All insurance obtained by the Lessee in compliance with this Lease shall be obtained from reputable companies acceptable to the DPL.

Obtaining insurance with required coverage for temporary occupancy was quite difficult for most of our applicants and permittees renewing. The Secretary met with the president and members of the Pacific Insurance Association regarding the insurance coverage for DPL permittees in which the insurance companies stated that it was complicated to provide coverage as it was at risk to the insurance companies themselves (Attachment 20). The liability insurance coverage amounts for TOAs have adjusted accordingly with the regulation amendments on June 6, 2017. The example TOA renewals provided in Exhibit E of the audit report were affected by higher

insurance coverage requirements. For TOA 11-029S, RED staff also had to follow-up on other pending documents.

Other issues included TOAs up for renewals that the DPL Legal Counsel determined not permissible, such as activities on public lands within the 150-foot high water mark.

OPA: Paragraph 1 (page 9) *Our sample testing showed that DPL had not renewed AGP's for many years prior to the adoption of the new regulations in January 2016. For one permit (A94-01R), expired in 2009, and two permits (06-03S, A06-03T) expired in 2012.*

DPL response:

- A94-01R – Although the AGP was last renewed in 2009, the Permittee continued to remit its payment until 2017 when it decided to cancel its AGP due to the increase in the fee. Therefore, there is no loss of income.
- A06-03S – The delay in renewing this AGP was caused due to a portion of the AGP was conveyed under the Quitclaim Deed Agricultural Homestead Waiver in 2012, including interest for a commercial permit. Despite this, client has paid and the account remains up to date.
- A06-03T – This matter is within and under the US Military Leaseback Area, and is undergoing administrative and legal review. DPL has been advised by the Legal Counsel that DPL cannot pay the US Government any amount for the leaseback land in Tinian. Under advisement, DPL will be discussing with the Municipality of Tinian and Aguigan to manage the leaseback area directly with the US Military for cattle grazing in Tinian.

As seen in the attached memo signed (Attachment 21) by Legal Counsel, Matthew Pugh, Director of Compliance Division, Gregory Deleon Guerrero, and Secretary, Marianne Concepcion-Teregeyo, DPL will proceed with renewing all AGP permits. While the permits cited were expired years before the regulations were adopted, DPL is cognizant of what internal controls to employ – such as the database that will serve as an inventory log of all public land leases and permits, inclusive of tickers when expirations are approaching, when inspections are needed, etc.

As it is a temporary permit (TP) for renewal in Rota, drafts of renewals are to be reviewed by respective office Director as with TP No. A94-01R, and sent directly from the respective office to DPL Secretary and DPL Counsel for review. Real Estate was able to track, with the assistance of the Rota Office through monthly reports, that the above process was followed and awaiting finalization from Legal Counsel. The last email correspondence for this particular permit to RED for assistance for one-year renewal is May 2008, and the permit was signed by former Secretary on May 27, 2008.

The Real Estate Division received an email from the Tinian Office stating they received the one-year renewal signed by former DPL Secretary for Temporary Permit No. A06-03T on March 16, 2006. Director of RED did not locate any other emails for renewal after and the last saved

renewal on the RED directory drive was in 2006. As it is a temporary permit (TP) for renewal in Tinian, drafts of renewals are to be reviewed by the respective office Director and sent directly from respective office to Secretary for review.

OPA: Paragraph 2 (page 9)

DPL response: A14-003T was an applicant that was assigned a permit number but a permit was not executed. This is an internal process that DPL will investigate and look to improve.

For the request to process a new permit with the number A14-003T RED was copied in emails in 2014 with Tinian staff and Tinian Director for review and it was noted that permit would also be sent to RED after Tinian Director's review (copy of email provided by Tinian DPL). Unfortunately, a break in the process occurred as a year's records from 2013 to 2014 of the RED Directors are not recoverable. RED cannot track email responses for this period in 2014. A follow-up email was received from Tinian office in March 2015. The site for this AGP is in the leaseback, therefore process was likely put on hold because of the proposed military use and relocation of AGPs from the leaseback area.

RED sends email follow-ups periodically, if not weekly, and will continue and utilizes a follow-up log sheet for each new and renewal process. For AGP applications and renewals, some that were directly forwarded to the former Legal Counsel for review and Rota DPL continued to follow-up with his office. DPL RD Alejo Mendiola was required to visit Saipan in June 2018 so that all pending Rota issues can be resolved. The Tinian RD, Ray Cing, will also be visiting the Saipan office soon.

OPA: Paragraph 3 (page 9)

DPL response: Please refer to information provided for Paragraph 4 (Page 8)

OPA: Exhibit E –

DPL response: is example of TOA renewals affected by higher insurance coverage requirements. For TOA 11-029S, RED staff also had to follow-up on other pending documents.

OPA: Paragraph 4 (page 9)

DPL response: Beach Concessions - In 2013, a tourism task force was developed by the late Governor Eloy S. Inos, which would affect the beach concessionaires permitted by DPL. Renewals of the Beach Concessions were put on hold, as the task force was assigned to determine whether, the concessions would all be relocated to one designated area, or bid out for the locations currently occupied and possibly have the hotels bid out. Compliance Division has been conducting reviews of each of the beach concession files to determine who are the owners (to identify duplicate owners, shareholder, officers, members) and if they are in compliance with payment and proper utilization. All Beach Concessions that have complied and can operate pursuant to DPL's regulations will be forwarded to RED and renewed accordingly within the next few months. DPL recently found that one particular permittee was operating inconsistently with the regulations. Therefore, DPL issued a letter to rectify this (Attachment 22).

OPA: Paragraph 2 (page 10)

DPL response: To say that DPL “does not rigorously enforce lease and permit provisions” is very subjective and misplaced. DPL enforces the regulations to the furthest extent possible especially during my tenure at DPL. When DPL is faced with non-compliance, DPL works to ensure that the lessee/permittee comes into compliance. While the lessee and/or permittee works to come into compliance, DPL is still collecting rent. After exhausting all methods to mitigate non-compliance, DPL will terminate a lease/permit. DPL forwarded cases to Legal Counsel for further legal action.

RED still experiences problems collecting updated documents, insurance policies, and payments upon execution of new and renewal TOAs. RED issues final notices (usually 15 calendar days) to submit requirements. If requirements are not received within the time allotted, application and request for renewal are void. Void renewals are still collected on and Compliance is advised to have the (void) permittee vacate (Attachment 23). Non-compliance matters are still charged a fee until they are vacated.

OPA: Findings, Compliance with Lease Agreements and Permits Were Not Closely Monitored (page 11)

Lease #	DPL Comment
L09-04S	Appraisal report received on April 11, 2014 FS 2017 stamp received on February 26, 2018
L08-009T	Appraisal report was submitted to DPL on September 28, 2017
L90-03R	Appraisal report received on March 14, 2017 FS 2017 was received on June 6, 2018
L11-03S	FS 2017 was stamp received on February 26, 2018
BGR	
05-51S	BGR was submitted on 02/23/18
16-031S	BGR was submitted on 09/21/17
02-21S	BGR was submitted on 03/14/18
12-032T	BGR was submitted on 06/15/18

OPA: Paragraph 2 OPA identified a promissory note for a sub-lessee who did not vacate public land after their lease expired OPA conducted a follow-up interview and found that DPL discovered the sub-lessee's presence on public land only by chance.

DPL response: CORRECTION – the company name is Advance Marine Saipan Corporation (AMSC), which did not have a lease with DPL (Attachment 24). A Settlement Agreement was executed which required the company to pay rental to DPL for previous years of occupancy and execute a promissory note with DPL. The PN was executed on January 30, 2016 with \$16,366.88 amortized in 36 equal monthly payments of \$538.23 which ends on August 1, 2019. The other stipulation of the settlement agreement was to submit DPL's lease requirements in order for AMSC to acquire a long-term lease. A lease agreement was drafted and at this time, a public benefit is being negotiated. Some history on this matter, the area where Advanced Marine is located was formerly leased to Nanyo Shoji. Shoji vacated in 2006. From 2006 to 2016, there

were no collections. In 2016, DPL wrote a letter to tenants of Shoji to include Spectrum, Advanced Marine, and TBK, to apply for a lease for public land and make payments. The PN was retroactive to include rent from 2006 to 2016. DPL should be commended for finally taking all previous squatters to court and receiving long overdue payments (Attachment 25).

This finding should be removed as it was not a sub-lessee as described and the matter was already resolved via settlement agreement. A lease is still in draft form.

OPA: Paragraph 3 (last paragraph) *However, OPA noted during its review of 14 temporary permits that the Compliance Division did not conduct an inspection for six permittees in 2014 and 2015, four permittees in 2016, and eight permittees in 2017. For AGP's, two of the eight were not inspected within the last three years. If inspections are not conducted every year, annual renewals required by regulations may be difficult to implement.*

DPL response: We do not deny that a few permits were not inspected annually as a result of shortage of staff or human error however, DPL believes for the most part that inspections were made and that misfiling of reports (due to resignation of staff) are the cause of OPA's findings. The Compliance Division staff is working on conducting its filing system at 4pm daily including updating its permit listing to ensure all permits are renewed accordingly.

OPA: Findings, Compliance with Lease Agreements and Permits Were Not Closely Monitored, Paragraph 2 (page 12) *DPL currently does not have a monitoring system to ensure that required documents are submitted when due, and not merely when inspections are scheduled. Untimely submission of, or complete failure to submit, required appraisals and financial documents may result in potential loss of revenue.*

DPL response: DPL conducts annual inspections on public land leases and permits. Inspections ensure that DPL's records are up-to-date. To require DPL to ensure that documents are submitted when due and not merely when inspections are scheduled is unnecessary. Documents are due at the time of inspection or immediately after. This mechanism works for DPL. While DPL enforces its regulations fully, external factors such as the delays on the clients' end contribute to untimely submission of documents or failure to submit. When this occurs, the Compliance Division issues a NOV.

OPA: Paragraph 3 (page 12) *During our interview, DPL claimed that it collects back rentals once an overdue appraisal report is submitted. However, the collection of back rentals could potentially become difficult if the dollar amount is significant. To illustrate, the independent auditors reported that in FY 2016, DPL's receivable amounted to about \$18.9 million, and of this total, DPL expects to collect about \$1.5 million (or 7 percent) in net receivables. This indicates that historically, collections have been problematic, with a history-to-date allowance for bad debt of \$17.4 million or 93 percent considered uncollectible.*

DPL response: Please don't mix apples and oranges. The bad debt is not due to overdue appraisals. This statement is misleading. As mentioned earlier, bad debt was due to failed leases. Should OPA have audited DPL years ago, this issue may have gotten the necessary attention in the past. Please recognize the directive mentioned earlier (Directive No. 005) and the good intentions from current management to resolve bad debts. Further, if the lessee failed to submit

the appraisal on time, DPL does charge the appraisal rate + interest when it is submitted. There are no waivers of interest when it is the fault of DPL. Most of these appraisals were overdue way before I got to DPL. I have also instituted that the DPL Staff Appraiser remind Compliance and Accounting of appraisal deadlines.

Also, DPL purchased a new accounting system as stated earlier called Sage 100 ERP. This system has a function wherein appraisals, renewals/extensions, and due dates, are inputted and flagged once they near expiration. The RFP is in progress for a support team to assist in the implementation of Sage which requires the training of all accounting staff.

As for the \$17.4 million allowance for bad debt, these amounts are the accumulation of delinquent accounts since 1980's. Many of these businesses are no longer in existence and have moved off-island. DPL has made efforts to collect from delinquent accounts but ultimately, \$12,446,556.19 is being proposed for write-off. DPL is in the process of finalizing a write-off policy and once adopted, it will alleviate this finding.

OPA: Billing Records Were Not Produced; Fees Were Not Accurately Assessed; Records Were Unreliable, Paragraph 2 (page 12) *Regular billings are not a standard practice at DPL, and instead, DPL relies on the lessee or permittee to submit their payments on time.*

DPL response: Except for leases executed in the early 1980's that did not have this provision, all other lease agreements state that "All rents payable pursuant to the terms of this Lease shall be deemed to have commenced on the first day of the month after the Commencement Date of the Lease, and shall be paid without prior notice or demand." Therefore, such finding is unreasonable.

OPA: Paragraph 1 (page 13)

DPL response: L11-03S BGR computation was corrected and the customer was billed. The payment was received on February 27, 2018.

DPL inadvertently accepted payment from permittee (07-22T) based on the fees outlined in the regulations; however, a closer look at the agreement indicated a lower rate. DPL will review its processes to determine what control measures can be employed to prevent future-like findings.

OPA: Paragraph 2

DPL response: TP02-12S was corrected to reflect a billing of \$10,700.93 which was billed on April 7, 2017. There were no earlier adjustments made to this permittee's account and computation was done and payment was received on April 19, 2017.

In summary, DPL acknowledges that there is room for improvement. To this end, DPL will take OPA's report under advisement and will create policies and procedures that are consistent with DPL's goals and objectives.

DPL has been cognizant of these matters through reiterations from audit reports, which I would like to highlight that DPL had its first unqualified opinion for FY2016. It is also important to

note that although OPA's last audit of DPL was in 2013, DPL continued to commission for an annual single audit. These audits have always been provided to OPA.

At present, DPL has a tracking mechanism on Microsoft Excel called MCT Tracking which I have instituted. This file is read-only and accessible to all division directors and management staff. They are able to review the log of incoming and outgoing information. I also discussed with directors in several director's meetings and advised them to review and monitor pending correspondence, and monitor tasks assigned to their divisions. This was implemented in 2016.

Other factors that hindered DPL's performance during the period of this audit were:

- Typhoon Soudelor in 2015 – the devastating impact of Saipan required community members to come together to assist with relief efforts. DPL's personnel at the time aided emergency responders for several months, which ultimately delayed several inspections and reports and consequently delayed the processing of all new and renewal lease and permits.
- Attrition – DPL experienced personnel changes, which peaked during Soudelor and in the aftermath of it. The process of replacing vacant positions and creating new positions has taken years. Realizing the magnitude of work and the backlog, I requested for new FTE's for Real Estate and Finance. Even now, with DPL close to full staff, key positions such as Staff Appraiser, which is being advertised continuously, and Civil Engineer, which was advertised twice, still remain vacant.
- Understaffing Issues – As mentioned in several annual reports over the years, one of the challenges from the Real Estate Division, was that it was understaffed, at times only 3 staff were available to process the different types of requests, extensions, renewals, etc. in RED. In past years, the total staff allotted to RED was four (4) employees, with one of the staff on two occasions working in a different DPL division. At my urging and directive, we requested for three (3) additional RED staff and two (2) additional Finance staff. As of 2018, both divisions are now fully staffed.

In closing, I would like to indicate that DPL has come a long way. We continue to collect revenue higher than projections, which is due to a very aggressive DPL team. Our work from 2016 to present is commendable, receiving a first ever unqualified audit in 2017 for FY2016.

DPL also has offered for the first time professional development training in September 2017, which we plan to do annually. This audit will certainly be one of the topics on our next professional development agenda. We also had OPA Legal Counsel, Ashley Cost, present to DPL at that development training regarding ethics.

DPL has been actively and aggressively written to unauthorized users of public land to have them comply and pay for using public land. In fact, as mentioned earlier, DPL has pending cases before the Superior Court for unauthorized use of public lands.

DPL has also taken it a step further and sought legislative assistance from the House Speaker Ralph Demapan and Senate President Arnold Palacios to seek remedies in allowing DPL to collect from individuals or establishments that have encroached on public land without paying

(Attachment 26). DPL has also written to AG and had personal discussions regarding such matter. However, to this date, DPL is legally prohibited from collecting from Surf Club, Kanoa Resort, PIC, etc., for encroaching and building facilities on public land. However, because this is within 150 feet of the high water mark, DPL cannot collect. DPL and AGO are in active discussion on requiring encroachers to remove buildings and permanent structures on public land.

I also want to thank you for acknowledging DPL's current management team in attempting and working closely to resolve internal control deficiencies. It is unfair that OPA's Audit titled "Department of Public Lands Management of Land Leases and Temporary permits" was done in 2017 and that the draft report is only now being released, well over a year after the entrance conference. I also find it discouraging that despite a first ever unqualified opinion for DPL's 2016 single audit by Deloitte and Touche, DPL is being cited for alleged wrongdoings dating back to the 90's. Those findings should be eliminated by statute of limitations. The label is misleading because it is being released now, in 2018, but the citations occurred previously. Should OPA have audited previous management of MPLA/DPL, the label would have been appropriate. However, Public Lands Management under the autonomous board of MPLA and previous secretaries will now be referenced to existing DPL Management. This is strongly misleading. Our strides in progress and accomplishments from 2016 to current is only beginning and we look forward to working diligently to protecting our NMD assets, public lands.

The position of Internal Auditor is brand new to DPL and it is our goal to be as efficient, productive, and accountable for our progress. I look forward to receiving recommendations for internal controls instead of just citations. Please incorporate our comments in your audit report and we request that references outside of your audit scope timeframe be removed.

If you have any additional questions and/or concerns, please reach me at mariannet@dpl.gov.mp or 234-3751.

Sincerely,



Marianne Concepcion-Teregeyo
Secretary, DPL

/mca/mct

cc: Real Estate, DPL
Compliance, DPL
Accounting, DPL
Legal Counsel, DPL
Financial Management Advisor, DPL

Appendix 5: Status of Recommendation

No.	Recommendation	Status
1	Adopt a comprehensive land use plan as required by law.	Unresolved
2	The Secretary or the designee should monitor all functions and hold employees accountable for their work.	Unresolved
3	<p>Adequately develop and adopt administrative policies and update SOPs to ensure:</p> <ul style="list-style-type: none"> a. clear lines of responsibility and coordination among the divisions and district offices to ensure the timely execution of leases and permits, maintenance of adequate land lease records; b. leases and permits are reviewed and monitored for compliance; c. rental fees are timely billed, assessed, and collected; d. pertinent information is communicated to the district offices to carry out DPL’s mission and comply with laws and regulations. 	Unresolved
4	Develop a tracking system to monitor the submission of required documents and consistently review, maintain, and update the master list in order to accurately track all active public land leases.	Unresolved
5	Assist and provide adequate training for accounting staff; and utilize a reliable accounting software to eliminate redundant tasks and process transactions efficiently.	Unresolved



Department of Public Lands
Management of Public Land Leases and Temporary Permits
Report No. AR-18-01, July 2018

CONSTITUTIONAL MANDATE

Article III, Section 12 of the CNMI Constitution and the Commonwealth Auditing Act (1 CMC, 2301, 7812 et. seq. of the Commonwealth Code) established the Office of the Public Auditor as an independent agency of the Commonwealth Government to audit the receipt, possession, and disbursement of public funds and to perform such other duties as required by law.

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