
**Office of the Public
Auditor**

**Division of Customs
Assessment and Collection of Excise Taxes**



**OPA Report No.
14-01**



Office of the Public Auditor

Commonwealth of the Northern Mariana Islands

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September 29, 2014

Larrisa Larson
Secretary
Department of Finance
Saipan, MP 96950

Jose Mafnas
Director
Division of Customs
Saipan, MP 96950

RE: REPORT ON THE AUDIT OF THE DIVISION OF CUSTOMS

Dear Secretary and Director:

The Office of the Public Auditor (OPA) conducted a performance audit on the assessment and collection of excise taxes by the Division of Customs (Division). As reported in the Commonwealth of the Northern Mariana Islands (CNMI) government's financial audits for the fiscal years 2011 and 2012, unrecorded accounts receivable related to excise taxes amounted to \$5,017,961 and \$4,392,975, respectively. This indicated that excise taxes were not being properly recorded and serious collections efforts are needed to be performed. See Appendix E for prior Single Audit Findings.

The assessment and collection of excise, fuel, and cigarette taxes historically represents the third largest revenue source for the CNMI with total receipts reported in the audits of fiscal years 2011 and 2012 totaling \$23M and \$25M, respectively. Based on the audit findings, there is reasonable concern that proper accounting and internal control procedures were not being followed or in place.

Accordingly, OPA developed an audit program and audit plan which emphasized the following objectives and subsidiary objectives:

Is Customs making accurate tax assessments and timely collections?

- a. If the assessments are not accurate and collections are not timely, what are the consequences?
- b. If the consequences are significant, why are tax assessments poor and collections untimely?

To perform our audit, OPA conducted interviews with the Division's management and staff, observed the direct operations of the Division, reviewed the existing laws, regulations, and

policies, selected and tested samples of transactions, and created an overall flowchart of the Division's critical operations. The scope of our work was limited to the Division of Custom's Saipan Seaport operations for the period of January 1, 2013 to December 31, 2013.

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS) issued by the Comptroller General of the United States of America. These 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Background and detailed scope and methodology are discussed in Appendix A and B.

RESULTS IN BRIEF

The Division is organized to physically track the goods from its arrival at the dock, inspection of the goods (if applicable), assessment and collection of taxes and the release of the goods. Additionally, the Division is responsible for the detection of illegal goods, drugs and the storage of confiscated contraband goods.

Our audit disclosed inadequacies and inconsistencies in both the initial assessment of excise taxes and the collection of outstanding balances. Specifically, we found that the Division:

- (1) Failed to implement Public Law 17-64;
- (2) Improperly classified taxable goods;
- (3) Failed to hold cargo for delinquent taxpayers;
- (4) Had poor controls over consolidated shipments;
- (5) Lacked random inspection procedures;
- (6) Failed to timely collect taxes on bonded commodities; and
- (7) Failed to collect on overdue balances.

Finding nos. (1) and (6) were addressed by the Division prior to the conclusion of our fieldwork. Please see Appendix C for discussion of the findings.

RESPONSE IN BRIEF

The Director of Customs in his response dated August 29, 2014, agreed with OPA's recommendations with the exception of conducting random inspections. Further, many of the recommendations have been or are in the process of being implemented.

For the agency's full response, see Appendix F and for the Auditor's Response, see Appendix G.

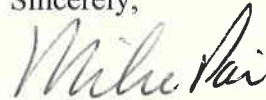
AUDITOR'S CONCLUSION

These findings result in a loss of income or forgone revenue for the CNMI. To address these findings, we recommend the following:

- Consult with the Department of Commerce with the goal to simplify the classification system, provide staff training and perform adequate and timely review of tax assessments;
- Adhere to existing regulations and policies of holding subsequent cargo until outstanding balances are paid in full before the release of cargo. Any exception must be approved by the Director and properly documented;
- Require consolidators to provide additional documents such as individual invoices before the release of cargo to the consolidator's warehouse;
- Develop and adopt procedures for the random selection of cargo for inspection; and
- Develop effective procedures to collect outstanding accounts.

Our recommendations, if implemented, will improve the overall operations of the Division as it relates to tax assessment and collection. Please see Appendix D for a discussion of the recommendations. During the course of our audit the Division's personnel were very cooperative and courteous. They exhibited a great desire to learn and improve. OPA sincerely thanks them for their assistance during our audit.

Sincerely,



Michael Pai, CPA
Public Auditor

cc: Governor
Lieutenant Governor
Senate President, 18th CNMI Legislature
House Speaker, 18th CNMI Legislature

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Appendix A. Background

Pursuant to 1 CMC § 2553 of the Commonwealth Code, the Division of Customs, through the authority of the Department of Finance, is responsible for ensuring that all imports and exports comply with the laws and regulations of the CNMI specifically defined under Title 4 Chapter 4 Article 1 Excise Tax and User Fees and Chapter 70-10.1 Customs Service Regulations. The Division of Customs processes all persons, baggage, cargo, and mail entering the CNMI at all entry ports. It restricts and intercepts contraband, including illegal drugs and non-registered weapons; assesses and collects excise taxes, fees, and penalties on imported goods.

The Division of Customs consists of the Airport and Seaport branches. The Airport branch is responsible for air freight and postal operations while the Seaport branch is responsible for the ocean freight operations. The Division of Customs also consists of the Compliance & Statistics, Detector Dog Unit and Customs Investigative Unit. The Director oversees the two branches including the DEA Task Force and the district offices located on Tinian and Rota. As of November 25, 2013 the Division of Customs had a total of 42 employees tasked with carrying out the Division's responsibilities.

The Division of Customs, Seaport (Seaport Branch) performs an important revenue collection function for the Division of Revenue and Taxation through the efforts of the:

1. Support staff consisting of specialists, inspectors, and officers who perform
 - a. Inspections, assessments, and collections of taxes on goods and merchandise imported into the CNMI by sea, and
 - b. Prevents prohibited goods or merchandise from being imported into the CNMI.
2. Compliance & Statistics Section who are responsible to collect on delinquent accounts and returned checks; adjust, abate and offset accounts; conduct administrative hearings; issue administrative orders; and prepare statistics and reports.

The Seaport Branch inspects cargo based on importer history, origin of the shipment, and other confidential factors in the goal of deterring and intercepting contraband. Importers are required to submit a bill of lading and invoice in order for Customs to evaluate and assess tax for each item being imported. The Seaport Branch imposes excise taxes by selecting the appropriate code for each invoice item from a list of 781 classification codes provided in the tax system. The classification codes are derived directly from the Harmonized Tariff Schedule of the United States which are assigned the applicable tax rates according to Chapter 4 Article 1 Excise Tax and User of the Commonwealth Code.

Generally, importers are required to make payment of taxes for the imported goods within 30 days after entry into the CNMI. Importers who fail to do so are automatically recorded in the Accounts Receivable (A/R) account of the Division's tax system which the Compliance and Statistics Section attempts to collect on. Notice letters have been mailed to customers in the past, however, collections were unsuccessful. As a result, the Compliance and Statistics Section

attempts to collect on overdue accounts by contacting delinquent taxpayers by telephone. Through its authority, holding and denying the release of cargo until outstanding balances are satisfied is the Seaport Branch's most effective method of collecting overdue accounts.

All monies collected by the Division of Customs are deposited by the Treasurer of the CNMI.

Appendix B. Detailed Scope and Methodology

The scope of the audit covered all assessments conducted at the Seaport Branch during calendar year 2013 including assessments of bonded commodities, and all unpaid taxes as of December 18, 2013. To achieve our objectives, we completed the following:

- Gained an understanding of applicable laws and regulations by thoroughly reviewing:
 - Chapter 4 Article 1 Excise Tax and User Fees
 - Chapter 70-10.1 Customs Service Regulations
 - Public Law 17-64 (amendment of the definition of “soft drink”)
- Gained an understanding of Customs seaport processes, systems, procedures, and internal controls used to manage tax assessments and collections by:
 - Conducting interviews with Customs management and staff
 - Conducting on-site observations and process walkthroughs
 - Developing flowcharts for the vessel clearance, tax assessment, inspection, DOE payment, and bonded warehouse processes
- Tested Seaport Customs records, both physical and computer generated, against attributes relevant to the audit objective. Specifically, we:
 - Tested a random sample of DOE’s processed in calendar year 2013
 - Tested a freight manifest from calendar year 2013 against the Tax System Records
 - Conducted a physical inventory of bonded goods using the inventory logs maintained at Customs, and tested related withdrawals against the Tax System records
 - Tested a random sample of Accounts Receivable (A/R) balances
 - Tested the Customs HTS Codes and Rates programmed in the Tax System against the Excise Tax Law
- Analyzed Accounts Receivable as of December 18, 2013
- Summarized audit findings

We conducted this performance audit in accordance with generally accepted government auditing standards issued by the Comptroller General of the United States of America. These 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusion based on our audit objectives.

Appendix C. Audit Results

A. Poor Tax Assessments

1. *Failure to Implement Public Law 17-64.* On December 20, 2011, Public Law 17-64 was enacted into law which redefined the definition of soft drinks and provided for higher taxes on certain types of beverages. The tax on soft drinks includes an excise tax of .005 cents per fluid ounce, a container tax of 0.05 cents per carton or bottle, and a beautification tax of 0.42 percent of total value. The old and new definitions of “soft drink” are the following:

Old definition: “Soft drink” is defined as “any drinkable carbonated or noncarbonated nonalcoholic beverage, other than drinkable dairy products, fruit or vegetable juices, bottled drinking water, or beverages containing tea or tea products, and those items that are not fit for consumption without mixing with other drinkable products (i.e. fruit punch concentrates, cocktail mixers, etc.).”

New definition: “Soft drink” means “any readily drinkable carbonated or noncarbonated nonalcoholic beverage, other than water, milk and 100 percent juice.”

The new definition applies to all beverages except alcohol, water, milk and 100 percent juice. In our testing of tax assessments, OPA noted that the Division failed to apply the correct tax rate to all beverages covered under the new definition. This situation continued until the Secretary of Finance was notified in a letter from OPA dated February 19, 2014, approximately 25 months after the law took effect.

During our survey, OPA reviewed 10 tax assessments which were processed by the Seaport Branch after the enactment of P.L. 17-64. Of the samples tested, OPA noted a total of \$22,122 of forgone taxes due to noncompliance with the new law. This amount represents approximately 10 percent of the total invoice value. The commodities that should have been taxed at the soft drink rate were instead charged a 1 percent excise tax rate. The tax categories used in these assessments were:

- Coffee, tea (instant),
- Tea,
- Juices, fruit and vegetable, and
- Food prep NESOI (not elsewhere specified or included)

The failure to implement the amendments of the law resulted in forgone revenues for the CNMI over a period of 2 years. Prior to the completion of our field work and as discussed above, the Division took corrective action on this issue in February 2014.

2. *Improper Classification of Taxable Commodities.* The Division utilizes the United States Harmonized Tariff Schedule¹ (HTS) to classify goods that are imported into the CNMI. From the listing provided by the Division, there are approximately 781 tax codes programmed into the CNMI Tax System that are taxed based upon 24 broad tax categories. See Appendix H for a list of CNMI tax rates and appropriate categories. During an assessment, the Customs officer will classify the items based on the description by selecting the appropriate tax code, and the CNMI Tax System will automatically calculate the tax amount based on the tax rate(s)² assigned to the individual tax codes.

Because of the number of codes available for selection, OPA found that Custom officers will simplify the assessment process by applying a single tax code with the appropriate tax rate established by CNMI law. In one sample tested, the invoice submitted included items such as instant coffee, chocolate, cough drops, etc.; however, the tax code applied by the Customs officer was “Vitamins All Kinds” subject to a 1 percent tax rate.

In two separate assessments reviewed, a Customs officer selected the wrong tax code resulting in the application of an incorrect tax amount. The law specifically exempts the application of a beautification tax on all food, and exempts excise tax on clothing and merchandise for children under the age of 24 months. In the sample selected for review, the tax code “Infant Clothing below 24 months” was used to assess baby food, therefore a beautification tax was incorrectly applied. The more appropriate tax code should have been “Infant Formulas and Food,” a code that has zero tax rate for excise and beautification.

These errors are due to a lack of supervisory review, inadequate training, and complexity of the HTS codes. During our observation, we noted that tax assessments were not being reviewed for accuracy due to a shortage of staff. Further, formal training for Custom employees is limited to 120 hours at the start of their employment. No follow up training is conducted by the Division. In addition, of the 781 tax codes, there are multiple codes with similar descriptions and sometimes various rates which make it difficult for Custom officers to properly classify imported goods. For example, there are two classification codes for “Travertine” with the following rates: (1) Salt, Sulfur, Earth and Stone, Lime and Cement at 1 percent, and (2) Ceramic Products at 5 percent.

Without adequate and proper training, supervisory review, and knowledge of the HTS codes and the assigned rates, the risk of an incorrect assessment is very likely.

¹ The HTS is broken down into 97 chapters, each of which pertain to a certain classification of goods, although sometimes goods may be classified under chapters 98 and 99 for different duty treatment. There are sub-codes under each chapter that is more specific to the nature of the goods being classified.

² The CNMI Tax System is designed to calculate other applicable tax rates such as the beautification tax and the container tax.

3. *Failure to Hold Cargo of Delinquent Taxpayers.* According to CNMI law and regulation, an importer has 30 days to pay the tax amount due, except for bonded goods where immediate payment is required when the goods are removed. The Division uses the date of arrival to determine the tax deadline. If an importer fails to pay this tax when due, the Division is authorized by regulation to hold cargo until such payment is made in full. At the same time, Custom officers are required to hold future cargo until management or the Compliance Branch verbally authorizes the release of cargo. OPA finds that this control of holding cargo, if implemented with additional controls, is a good control to ensure timely collection of taxes.

The tax system is designed to notify the Custom officer performing an assessment of an importer's overdue balance. At that point, the Custom officer will refer the importer to the Compliance Branch to discuss payment options. If an importer has set up a payment plan with the Compliance Branch, the importer will be allowed clearance of future imports as long as current taxes are paid up front.

In our review, we found that the Division does not always follow standard procedures. Of 52 tax assessments tested, 8 were not timely paid. Of the 8 importers, the Division did not hold subsequent cargo for 3 (or 37.5 percent) vendors. The Division's failure to hold cargo of importers who have outstanding balances encourages late payment and the possibility of non-payment. In reviewing the top 30 importers with the highest outstanding balances, approximately half are active importers³ that have outstanding balances greater than 1 year. See Appendix I.

4. *Lack of Controls over Consolidated Shipments.* Consolidators offer cargo transportation services that allow small shippers to take advantage of lower freight costs. A consolidator will usually purchase container space on a carrier at a discounted rate then resell sections of the space to individual shippers. Custom regulations allow the conditional release of goods to the consolidator's premises as long as such items are not released to individual consignees until clearance is obtained from Customs. The law prohibits any person from releasing or delivering goods to any person without prior clearance by the Division. Individual shippers may authorize the consolidator to obtain clearance from Customs if they choose not to do it themselves. Only during clearance and tax assessment is the shipper required to provide the invoice that shows a detailed description of the goods being imported.

During our audit, we noted that Customs fails to monitor consolidator movements to determine if compliance is being met. In addition, Customs requires very little documentation from consolidators for the conditional release of goods. Except for the bill of lading documents, which has general descriptions, Customs does not impose additional

³ For the purpose of the audit, we defined an "active importer" as one that imported at least one container in calendar year 2013.

requirements showing detailed descriptions and quantities of items imported. The fact that the Division does not perform adequate inventory of all cargo maintained at the consolidator's warehouse poses a risk that imported cargo may be released without the proper assessment and collection of tax and proper clearance.

5. *Lack of Random Inspection Procedures.* The Division may hold cargo during the assessment process for various reasons such as (1) if the importer has an overdue balance on previous assessments, (2) if the importer has been known to violate Customs law or regulation, (3) if the shipment origin is considered high-risk by the Division, or (4) if the Division suspects illegal activity. The Division will inform an importer if their cargo is held for inspection.

Although these procedures actively monitor high-risk importers, there are no procedures for random inspections over the general population. Random inspections can be a useful tool in tracking those importers who have adopted sophisticated methods to conceal illegal activity or falsify import documents.

B. Untimely Tax Collections and Poor Collection Efforts

- *Failure to Timely Collect Taxes on Bonded Commodities.* In 2013, four companies were authorized by the Division, for an annual fee, to store goods—usually cigarettes, tobacco or liquor—in a bonded warehouse. The bonded warehouse location must be approved by the Director and is situated within the company's property. The Division and the company share dual custody, each holding a key to one of the padlocks, in which goods cannot leave the warehouse without both of the parties present. The regulations allow bonded licensees to store goods without the immediate assessment or payment of excise tax. In addition, the regulations require that when goods are taken from the warehouse, immediate payment is required.

Our audit indicated that the Division allowed bonded licensees 30 days from the time of withdrawal to pay the tax. This reduces the immediate cash flow of the CNMI and increases the chance that ultimate payment will be delayed. OPA noted that prior to the end of field work, the Division took corrective action on this issue and is now requiring bonded licensees to submit payment before withdrawal.

- *Failure to Collect on Overdue Balances.* The accounts receivable listing provided by the Division as of December 18, 2013 shows a total outstanding amount of \$4.7M. Of this amount, approximately \$2M is classified as current, with the remaining amount greater than

30 days old. The amount overdue has accumulated from both active and inactive importers⁴. The Compliance & Statistical Section (Compliance Branch) is responsible for following up on outstanding balances. Except for poorly documented follow-up calls, the Compliance Branch currently does not use other methods to collect on outstanding accounts. The effect can be minimized by the Division if it strictly adheres to Custom regulations and denies Custom clearance to those actively utilizing the port until all outstanding taxes are paid. However, the Division has no leverage on inactive importers who have closed their business and cannot be contacted.

OPA was informed by the Compliance Branch that it ceased sending notices to taxpayers with outstanding accounts, because many of the delinquent taxpayers have invalid contact information. The statute of limitation to collect on taxes is 10 years. Outstanding accounts receivable dated 2003 and prior amount to about \$78K. The failure to collect on outstanding taxes will result in forgone revenues and create an unfair business advantage in the ultimate sale of goods to the general public by the delinquent importer.

The regulations state that a tax not paid in 90 days is considered delinquent and shall be forwarded to the Collections Branch at the Division of Revenue and Taxation. Currently, the Division does not forward delinquent accounts or work with the Collection Branch to collect on delinquent accounts.

Others

- *Failure to Formally Adopt Standard Operating Procedures.* The Division has drafted policies and procedures, but has not formally adopted all sections. According to the Director, the Division is in the process of reviewing the draft and is gradually leading to a full adoption of its policies.

⁴ For the purpose of the audit, we defined "inactive" importer as one who has not imported anything in calendar year 2013.

Appendix D. Recommendations

Assessments

Finding A1. This finding has been addressed, however OPA recommends training of Customs inspectors and officers regarding the changes in and the proper application of Public Law 17-64.

Finding A2. We recommend that the Division:

- Consult with the Department of Commerce to determine the necessity of the broad range of import classifications with the goal of reducing the number of classifications. While abundant statistical data can be an import by-product of the assessment process, it should not detract from the main goal of the Division.
- Provide follow-up training to staff regarding the HTS codes and the assigned tax rates and in other areas to enhance and improve Customs operations.
- Perform supervisory review of tax assessments for errors or inconsistencies.

Finding A3. We recommend that the Division strictly adheres to its policy of holding future cargo until outstanding balances are satisfied. If cargo is released without the full payment of outstanding taxes or without the approval of a payment plan, adequate documentation and approval by the Director should be maintained in the files.

Further, our review of existing Laws indicated no formal procedures or time tables were given to the Division to ultimately resale these held items in order to collect past due amounts. We recommend that the Division seek a legal opinion on this matter to determine if a change in the law is required or if such can be incorporated through revised regulations.

Finding A4. We recommend that the Division require consolidators to provide additional information prior to the release of cargo to the consolidator's warehouse. Such documents should include but not limited to invoices provided by the individual consignees with a detailed description, quantity, and value of the goods being imported. Consolidated shipments should not be released until all invoices have been presented to and assessed by the Division.

Finding A5. The Division prioritizes inspections on importers based certain criterias, however, the majority of cargoes are not inspected. We recommend that a method of random inspection be developed which would include all major importers over the course of each year. It is very difficult to determine if a particular importer is high risk or not, without some form of inspection to determine compliance.

Collections

Finding B1. This finding has been addressed, however OPA recommends that the requirement to collect the tax on bonded goods at the time of withdrawal be clearly stated in the policies and procedures manual.

Finding B2. OPA recommends written procedures be developed to immediately pursue importers with outstanding receivable balances that are greater than 30 days past due. OPA also recommends receivables greater than 90 days be forwarded to the Division of Revenue and Taxation, Collection Branch, in accordance with §70-10.1-150.

Others

- OPA's concern regarding collections is not limited to the actions of the Division, but also other government agencies which share similar issues. OPA recommends that the Secretary of Finance consider, in consultation with Division and Department Directors, autonomous agencies, and the Attorney General's Office, if the creation of a specialized collection Division or Department would be beneficial to the overall CNMI collections process. Should such a Division or Department materialize, OPA is willing to act as a facilitator for the group.

Appendix E. Single Audit Findings for FY2012 and FY2011

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2012

Tax Receivables - Division of Customs

Finding No. 2012-08

Criteria: Excise tax collections should occur when the shipped items are transferred to taxpayers.

Condition: Outstanding tax receivables (including penalty and interest) were identified as of November 19, 2013 according to the Director of the Division of Customs, as follows:

<u>Description</u>	<u>Amount</u>
Tax	\$ 3,984,187
Interest	200,864
Penalty	<u>207,924</u>
Total	\$ <u>4,392,975</u>

The CNMI could not provide a listing of outstanding tax receivables as of September 30, 2012. The above receivables are not recorded in the CNMI general ledger.

Cause: The cause of the above condition is lack of established policies and procedures to monitor outstanding excise tax receivables.

Effect: The effect of the above condition is potential lost revenues.

Recommendation: We recommend that all receivables be timely collected.

Prior Year Status: The lack of established policies and procedures to monitor outstanding excise tax receivables was reported as a finding in the Single Audit of the CNMI for fiscal year 2011.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Jose Mafnas, Director, Customs Services

Corrective Action: Taxpayers have thirty days to pay their taxes after picking up shipments so there will always be a receivable balance. Currently, there is an ongoing effort to collect outstanding receivables including holding of all future shipments until outstanding receivables are addressed with Customs management. Aggressive collection efforts continue and are ongoing.

Proposed Completion Date: Ongoing.

COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2011

Tax Receivables - Division of Customs

Finding No. 2011-10

Criteria: Excise tax collections should occur when the shipped items are transferred to taxpayers.

Condition: Outstanding tax receivables (including penalty and interest) were identified as of June 20, 2012 according to the Director of the Division of Customs, as follows:

<u>Description</u>	<u>Amount</u>
Tax	\$ 5,017,961
Tax	\$ 4,117,732
Interest	\$ 455,432
Penalty	\$ 444,797

The CNMI could not provide a listing of outstanding tax receivables as of September 30, 2011. The above receivables are not recorded in the CNMI general ledger.

Cause: The cause of the above condition is lack of established policies and procedures to monitor outstanding excise tax receivables.

Effect: The effect of the above condition is potential lost revenues.

Recommendation: We recommend that all receivables be timely collected.

Auditee Response and Corrective Action Plan:

Name of Contact Person: Jose Mafnas, Director, Customs Services

Corrective Action: Taxpayers have thirty days to pay their taxes after picking up shipments so there will always be a receivable. The system problems noted in the corrective action for Finding No. 2011-02 impacted the calculation and reporting of receivables as well. Most of the receivable balances noted are for one taxpayer and collection efforts have been ongoing.

Proposed Completion Date: Ongoing.

Appendix F. Agency Response



Division of Customs Service
Department of Finance



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August 29, 2014



David J. Blake, CPA
Audit Manager
Office of the Public Auditor
P.O. Box 501399, 1236 Yap Drive, Capitol Hill
Saipan, MP 96950

Dear Mr. Blake:

Here are our responses to the draft audit report generated by your office. Please review and let me know if you have any questions. Thank you.

Sincerely,


Jose C. Mafnas
Director

In 2014, a reorganization within our agency was made to establish two major sections: the Assessment and Collection section and the Enforcement section. The officer assigned to the Assessment and Collection (AC) section focuses on tax assessments (i.e. review documents such as ladings and invoices, for inconsistencies). Whereas officers assigned to the Enforcement section focuses on inspection of loose and containerized cargoes. Their primary function is to focus on the inspections of contraband (i.e. illegal drugs, pesticides, dangerous weapons, etc.) interdiction. However, during the inspection process, an AC officer joins the enforcement officers. He or she compares the items on the invoice versus what is unloaded from the container. The reorganization resulted in an increase of revenue collections and contraband interdictions.

Customs Response

Finding A1: Addressed and corrected. Beginning July 2013, Customs conducted training for all Customs officers, new and permanent employees. On August 25, 2014, the 3rd cycle Customs Basic Training began. Part of the training includes all laws affecting the Division of Customs Service.

Finding A2: (bullet point #3)

Customs agrees with this finding and has taken corrective action to address the recommendation. Specifically, Customs assigned two additional personnel to the Compliance section to focus on accounts receivables and to conduct a post-audit on all DOEs (excise tax assessments). After the 3rd cycle training, one more personnel will be added to Compliance Section.

Finding A3: Customs agrees with this finding. Customs has made corrective action to not release cargo to an importer/business with outstanding accounts. And, installment payment plan shall be at the approval of the Director.

Finding A5: Customs disagrees with this finding. Customs has implemented a procedure that is used by Customs globally. Beginning 2013, Customs has increased interceptions of contrabands e.g. illegal cigarettes, pesticides, counterfeits, undeclared and undervalued of goods, etc.

The random inspection that OPA recommends is practiced on passenger clearance.

Finding B2: Customs agrees with this finding. Specifically, Customs is in the process of amending §70-101.1-150 of its regulations to enable Customs to collect its own receivables that are greater than 90 days.

Appendix G. Auditor's Response

Based upon our discussions with and the written comments received from the Department of Customs following our fieldwork and the issuance of the draft report, it appears that the Department is moving forward in implementing the related recommendations with the exception of establishing procedures and policies for random inspections. In addition, the Department did not address Finding and Recommendation No. 4 in their written response.

From our review of various publications, most prominently the Customs-Trade Partnership Against Terrorism (C-TPAT), by the US Customs and Border Protection Agency, random inspections are recommended as a best practice, in conjunction with risk evaluation inspections.

The Office of the Public Auditor reserves the right to review at a later date the status of the recommendations in order to determine if the related findings are closed or remain open.

Appendix H. CNMI Tax Rates and Categories

For the privilege of first sale, use, manufacture, lease, or rental, *Chapter 4 Article 1 Excise Tax and User Fees* establishes tax rates for the following goods, commodities, resources and merchandise.

Commodities	Excise Tax rate	Beautification Tax	Beverage Container Tax
Agricultural Commodities	1% ad valorem	.42% ad valorem	
Beer and Malt Beverage	\$0.02 per fluid oz. or fraction equivalent	.42% ad valorem	
Boats and Yachts in excess of \$500,000	5.75% ad valorem	.42% ad valorem	
Boats and Yachts under \$500,000	5% ad valorem	.42% ad valorem	
Cigarettes	\$2.00 per 20 cigarettes or fraction equivalent	.42% ad valorem	
Construction Equipment, Materials, and Machinery	3% ad valorem	.42% ad valorem	
Cosmetics	17.25% ad valorem	.42% ad valorem	
Distilled Alcoholic Beverages	\$0.18 per fluid oz. or fraction equivalent	.42% ad valorem	\$0.05 per container
Foodstuff	1% ad valorem	Exempt	
Goods derived locally	1% ad valorem	.42% ad valorem	
Hygiene and Toiletries	1% ad valorem	.42% ad valorem	
Jewelry	5.75% ad valorem	.42% ad valorem	
Leather Goods	5.75% ad valorem	.42% ad valorem	
Passenger Vehicle not exceeding \$30,000 per unit	5% ad valorem	.42% ad valorem	
Passenger Vehicle in excess of \$30,000 per unit	5.75% ad valorem	.42% ad valorem	
Perfumery	23% ad valorem	.42% ad valorem	
Precious metals, precious or semi-precious stones	5.75% ad valorem	.42% ad valorem	
Prescription Drugs or Medicines	1% ad valorem	Exempt	
Soft Drinks	\$0.005 per fl. oz. or fraction equivalent	.42% ad valorem	\$0.05 per container
Tobacco/ Tobacco Substitute other than cigarettes	60% ad valorem	.42% ad valorem	
Wine & Sake	\$0.05 per fluid oz. or fraction equivalent	.42% ad valorem	\$0.05 per container
Liquid Fuel	\$0.15 per gallon	.42% ad valorem	
Personal Effects (Exceeding the fair market value of \$1000.00)	5% ad valorem	.42% ad valorem	
All others (not otherwise provided by law)	5% ad valorem	.42% ad valorem	

Appendix I. Top 30 Vendor Outstanding Balances

	CURRENT	30-60	60-90	90-120	120+	TOTAL DUE	OLDEST A/R	NEWEST A/R		Newest Arrivals	Location
1	336,408.85	219,047.99	231,656.22	243,868.54	7,004.63	1,037,986.23	08/09/08	12/17/13			
2	222,066.36	166,926.92	1,898.45	20.09	43,284.28	434,196.10	07/15/13	12/16/13	12/31/2013	AS2	
3	251,389.45	101.63	-	0.26	10,893.59	262,384.93	05/02/09	12/17/13			
4	255,318.53	-	-	-	-	255,318.53	11/21/13	12/17/13	12/30/2013	SS	
5	250,805.86	6.45	-	-	113.28	250,925.59	05/11/09	12/15/13			
6	-	-	-	-	147,612.02	147,612.02	06/04/04	01/09/09	12/27/2013	AR	
7	-	-	-	-	147,529.41	147,529.41	07/26/05	08/24/07			
8	-	-	-	-	125,751.20	125,751.20	12/06/05	02/12/12			
9	-	-	-	-	94,675.69	94,675.69	04/14/01	12/12/12	1/13/2013	SR	
10	-	-	-	-	72,206.87	72,206.87	02/26/09	01/29/12			
11	-	-	-	-	54,543.12	54,543.12	04/22/06	02/14/10	12/31/2013	AR	
									11/12/2013	AS2	
									12/24/2013	PR	
									12/18/2013	SR	
12	-	-	-	-	54,505.72	54,505.72	05/04/07	12/04/09			
13	11,552.63	2,977.68	39.76	14,489.08	20,151.71	49,210.86	02/10/12	12/12/13			
14	20.85	621.83	-	886.06	47,351.81	48,880.55	02/05/09	12/09/13	12/11/2013	AS2	
									12/30/2013	CK	
15	7,720.75	-	-	1,747.10	34,991.71	44,459.56	08/21/08	11/20/13			
16	13,883.44	11,558.28	367.84	158.31	7,983.36	33,951.23	02/24/11	12/17/13			
17	31,511.22	23.80	-	-	134.46	31,669.48	09/05/07	12/18/13			
18	19,452.61	9,751.40	-	3.21	1,828.21	31,035.43	11/30/12	12/14/13	12/28/2013	AS2	
19	-	668.91	93.50	-	30,085.47	30,847.88	09/25/04	11/17/13			
20	13,886.04	479.85	534.14	867.48	14,769.21	30,536.72	02/24/09	12/18/13			
21	-	-	365.90	7.96	29,713.65	30,087.51	06/15/07	09/27/13			
22	28,880.58	-	-	-	-	28,880.58	11/21/13	12/17/13	12/30/2013	AS2	
									12/27/2013	CK	
									12/29/2013	SS	
23	14,995.94	1,513.45	16.34	10,769.31	213.29	27,508.33	08/06/10	12/13/13			
24	27,008.51	-	-	-	2.90	27,011.41	06/27/13	12/18/13	12/26/2013	CK	
25	90.90	-	-	-	26,904.82	26,995.72	11/09/09	12/03/13			
26	21,029.96	2,476.18	21.76	304.47	1,115.66	24,948.03	09/07/12	12/15/13			
27	83.90	140.38	0.51	0.13	24,598.11	24,823.03	10/02/12	12/11/13			
28	-	-	-	-	23,114.42	23,114.42	05/31/07	02/26/09			
29	21,513.09	-	-	-	-	21,513.09	11/26/13	12/13/13	12/29/2013	AS2	
30	18,644.37	-	-	-	-	18,644.37	11/22/13	12/06/13	12/16/2013	AS2	
									12/20/2013	SS	
	1,546,263.84	416,294.75	234,994.42	273,122.00	1,021,078.60	3,491,753.61					

16 active importers that have outstanding balances that go back more than one year.



Division of Customs Assessment and Collection of Excise Taxes
Report No. 14-01, September 2014

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Geraldine Tenorio, CGAP, Audit Supervisor
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Michael Pai, CPA, Public Auditor

REPORTING FRAUD, WASTE AND ABUSE

- Call the OPA HOTLINE at (670) 235-3937
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