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March 15, 2008

SPECIAL REPORT

Submitted to:
Accrediting Commission for Community and Junior Colleges
&
Accrediting Commission for Senior Colleges and Universities

Western Association of Schools and Colleges
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Statement on Special Report Preparation

On January 31, 2008 the Accrediting Commission for Community and Junior Colleges (ACCJC) informed the Northern Marianas College (NMC) that it was compelled to place the institution on Show Cause subject to Termination in January 2009 and to ask that Northern Marianas College correct deficiencies noted. The Commission asked that the College submit a Special Report by March 15, 2008 showing what steps the College has taken to address each of the fourteen findings of the FY2006 audit.

The issues raised in the January 31, 2008 letter were discussed in detail among the management team and also were shared with the College community in various forums. The issues were also discussed in detail with the Board of Regents at their special meeting held on February 28, 2008.

For the Special Report due March 15, 2008, President Carmen Fernandez directed the College's Chief Financial and Administrative Officer to immediately begin addressing the concerns and prepare the required report. Due to the specific nature of this report, the Chief Financial and Administrative Officer was charged with taking the lead in preparing the report, drawing on the assistance of various members of the finance and budget office and applicable federal program personnel. As part of the preparation of the report, the Chief Financial and Administrative Officer discussed and updated progress on the report to the Planning, Budget and Evaluation Council.

The final draft prior to final editing was presented for review to the Board of Regents on March 13-14, 2008. The Board reviewed the report with the management team and other members of the College Community. The Board unanimously voted to accept the report on March 14, 2008.

The March 15, 2008 Special Report is submitted for the purpose of addressing the concerns raised by the Accrediting Commission for Community and Junior Colleges.

Dr. Carmen Fernandez  
President  

Raj Kurapati  
Chief Financial & Administrative Officer

A Land Grant Institution accredited by the Accrediting Commission for Community and Junior Colleges and by the Senior Commission for Colleges and Universities of the Western Association for Schools and Colleges
FINANCIAL STATEMENT FINDINGS

Receivables

Finding No. 2006-1

Criteria: Receivables should be periodically assessed for validity and collectibility. Additionally, through this process, the adequacy of the allowance for doubtful accounts should be assessed and collection efforts pursued.

Condition: Numerous account balances approximating $2,100,000 have been outstanding for several fiscal years with little or no subsequent activity. Further, several accounts have negative balances totaling to $269,922. This condition was corrected through a proposed audit adjustment.

Cause: The cause of the above condition is that supporting documents for these long outstanding balances could not be located and receivable schedules were not reviewed at year end for propriety.

Effect: The effect of the above condition is that the College’s receivables are not being collected in a timely manner. Further, interim financial statements are misstated due to a lack of adequate provision for doubtful receivables.

Recommendation: We recommend that the College implement procedures requiring periodic review of all receivables for validity and collectibility. Accounts determined to be uncollectible should be written-off. This process should also address the adequacy of the related allowances for doubtful accounts.

Prior Year Status: Lack of review of receivable balances for validity and collectibility was reported as a finding in the audits of the College for fiscal years 2001 through 2005.

Corrective Action Plan per Audit Report:

The College concurs with the finding. The College has accumulated numerous large receivable balances over the years on which there has been little to no subsequent collection activity. The College feels, however, that it has adequately reserved for these balances. Several accounts have been referred to attorneys and collection agencies for further action. The College is of the opinion that there is still potential for recovery on some of these balances and is reluctant to write them off. The College will increase its efforts to collect these balances and periodically review the adequacy of related allowances. Unfortunately as often is the case, movement on collection cases is slow and when judgments are received in the College’s favor payment amounts are generally minimal. Also contributing to the high level of old balances is the lack of direct access to details for old balances on the MIPS accounting system. Details were not carried forward when the College migrated to the current accounting system (MIPS) several years ago. Thus, when attempts are made to collect old balances, extensive research of manual records is required and when produced often the amounts are disputed by the customers. This often results in the College having to resort to litigation for collection. Unfortunately, when we are forced to pursue collection through litigation the balances
cannot be written off until the case is resolved. The College will again review these old balances and where the statute of limitation has expired and no activity is noted will recommend to the Board of Regents for write-off.

Steps taken to address this audit finding as of March 15, 2008:

During the regular meeting of the College’s Board of Regents held on February 8, 2008, the College Administration recommended and requested approval for the write-off of approximately $1,950,000 in long outstanding receivables (dating back to FY1999) against which there has been little to no payment activity (Exhibit A). The legal statute of limitations has already expired voiding, to the most part, the College’s ability to pursue collection. On approval of this request, the College recorded the necessary adjustments to “write-off” these balances and remove them from our financial statements. Additionally, validity of credit balances in receivables were investigated and cleared. A reconciliation of the accounts receivable Subsidiary Ledger and the General Ledger was performed to ensure that they are in balance. Finally, an assessment of the remaining Allowance for Doubtful Accounts was performed as of September 30, 2007 (FY2007 year-end) and adjustments made to ensure the adequacy of the allowance for the remaining receivables balances. Although, the College has agreed to write-off the balance as per the recommendation of the auditor, it has already referred several of these balances to attorneys and collection agencies for further action and where arrangements have already been made for payment of these balances, the College will continue to pursue enforcement of these agreements. Based on the actions, the College has adequately addressed the concern and has resolved the audit finding.

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).

Interfund and Interdepartment Accounts

Finding No. 2006-2

Criteria: Interfund and interdepartment accounts should be reconciled in a timely manner. Further, variances between funds should be investigated and adjusted.

Condition: Interfund accounts for elimination do not agree by $85,213. Further, interdepartment accounts between the College and the College’s Bookstore reflected a variance of $286,864.

Cause: The cause of the above condition is untimely reconciliation and lack of adequate accounting staff during year 2006.

Effect: The effect of the above condition is a potential misstatement of amounts recorded in the College’s financial statements. An audit adjustment was proposed to correct this condition.
Recommendation: We recommend that the College ensure periodic review and monitoring of interfund and interdepartment accounts.

Corrective Action Plan per Audit Report:

We concur with the finding. As noted, the lack of adequate personnel in the accounting department as a result of resignations and subsequent hiring freezes implemented to cope with a reduction in our personnel budget has had a negative impact on operations. Interfund accounts reconciliations were being performed but were not completed during FY2006. NMC’s Bookstore Manager left the College in FY2006 and as a result of the hiring freeze this position was not filled in a timely manner. The Bookstore Assistant also resigned in FY06 and again this position was not filled in a timely manner due to funding constraints. Subsequently, the College elected to fill these positions by transferring employees from the School of Business and the Small Business Development Center (SBDC). Obviously, the lack of historical knowledge of the operations of the Bookstore contributed to the issues noted in the finding. Further in an effort to reduce expenses and increase efficiency, accounting for the College’s Bookstore was moved to the NMC Finance Office beginning FY2007. This move should assist in ensuring the interfund balances between the College and the Bookstore are reconciled in a timely manner.

Steps taken to address this audit finding as of March 15, 2008:

A reconciliation of all Bookstore financial statement balances was performed including a review of the inter-fund balances. Through this review process, all general ledger account balances were reconciled to the subsidiary details. The transfer of the accounting for the Bookstore to the NMC Finance Office has been implemented and it is expected that this will further improve controls over the finances of this auxiliary function. Further, the new Bookstore manager, Ms. Bernie Sablan, who assumed this position on August 21, 2006 (Exhibit C), is working closely with the staff to ensure that relevant internal controls and processes are adhered to.

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).

Inventories - Bookstore

Finding No. 2006-3

Criteria: Physical inventory procedures should be established and variances between the general ledger and the subsidiary ledger should be investigated and reconciled in a timely manner. The subsidiary ledger should reflect accurate information as to quantity and cost. Further, costs in the subsidiary ledger should be based on underlying invoices.

Condition:
a. Our observation of the Bookstore’s physical inventory count indicated the following:

- Verbal inventory instructions were given to the count team, which was composed of student aides. Based on observation, the students were not well informed as to required procedures.

- Inconsistencies in description and item codes were found in the inventory count sheets.

- Some of the count records were listed on scratch paper rather than on prenumbered count tags.

- The case goods inventory was generally stacked in an organized manner. However, the same inventory is sometimes stored at various locations. Since the Bookstore did not prepare an organized layout of the floor space, it became very time consuming to identify all locations where particular inventory is kept. The Bookstore omitted or overcounted certain inventory in their initial counts and was required to recount several times to ensure an accurate count.

- The Bookstore did not utilize tag controls in its counts. As a result, the Bookstore ran the risk of omitting or double counting floor inventories. This situation worsens, as there are multiple personnel involved. Again, the Bookstore had to recount several times to ensure there was no omission or double counting.

b. The inventories subsidiary ledger was not reconciled to the general ledger balance resulting in an overstatement of inventories of $224,869.

c. For twenty-two of thirty items tested, variances were noted in quantities between year-end inventory test counts and the final inventory listing.

d. Five of thirty test counts during the year end inventory count could not be traced to the final inventory count. Thus, it appears that the inventory records were not adjusted based on the count performed.

e. For ten of eighteen items tested, unit costs differ from underlying invoices.

**Cause:** The cause of the above condition is weak internal controls over inventories.

**Effect:** The effect of the above condition is untimely completion of inventory counts and reconciliation and misstatement of inventories. Audit adjustments were proposed to correct these conditions.

**Recommendation:** We recommend that the College establish adequate internal control measures over inventories. Further, we recommend that the College ensure that inventories are properly
valued and reconciliation of the inventory general ledger and subledger balances occur on a regular and timely basis.

Corrective Action Plan per Audit Report:

The College concurs with the finding. NMC’s Bookstore Manager left the College in FY2006 and as a result of the hiring freeze this position was not filled in a timely manner. The Bookstore Assistant also resigned in FY06 and again this position was not filled in a timely manner due to funding constraints. Subsequently, the College elected to fill these positions by transferring employees from the School of Business and the Small Business Development Center (SBDC). Obviously, the lack of historical knowledge of the operations of the Bookstore contributed to the issues noted in the finding. As also noted in Finding No. 2, in an effort to reduce expenses and increase efficiency, accounting for the College’s Bookstore was moved to the NMC Finance Office in FY2007. This move provides for direct oversight of the Bookstore’s operations.

Steps taken to address this audit finding as of March 15, 2008:

It should be noted that the College has made significant progress in addressing concerns relative to the Bookstore’s inventory. In FY2005 and in financial years prior to FY2005, the auditors were unable to express an opinion on the Bookstore’s inventory due to material problems with these balances and qualified their reports accordingly. In FY2006, although the auditors still identified various issues with inventory, they did not qualify their report on the same, a clear indication that we had made significant forward progress in rectifying the issues regarding Bookstore inventory.

To address the FY2006 audit finding, a reconciliation of all Bookstore accounts was performed including a review of the inventory costing report as of September 30, 2007 and the inventory count procedures being utilized. Through this review process all general account balances were reconciled to the subsidiary ledgers, including the inventory accounts. The transfer of the accounting for the Bookstore to the NMC Finance Office has been implemented and it is expected that this will further improve controls over the finances of this auxiliary function. Further, the new Bookstore manager, Ms. Bernie Sablan, who assumed this position on August 21, 2006 (Exhibit C), is working closely with the staff to ensure that relevant internal controls and processes are adhered to.

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).

Fixed Assets

Finding No. 2006-4

Criteria: The College should maintain property records detailing the description, cost, acquisition date and estimated useful life of its fixed assets. Such records should agree to the
balances recorded in the College’s financial statements. Additionally, periodic physical inventories of all fixed assets should be performed and accounting records should be updated based on the results of those instances.

**Condition:** A physical inventory of the College’s fixed assets has not been performed within the past two years. Additionally, the College was unable to produce a schedule of fixed assets as of September 30, 2006, and original cost data or alternative valuation data is not available.

**Cause:** The cause of the above condition is non-adherence to the College’s established fixed asset capitalization policy and a lack of adequate fixed asset subsidiary records.

**Effect:** The effect of the above condition is a potential misstatement of amounts recorded in the College’s financial statements.

**Recommendation:** We recommend that the College institute procedures to substantially identify and determine the cost of its fixed assets. Once valuation and identity have been established, we recommend that the College reconcile the balance of actual fixed assets on hand to the balance of assets recorded in its financial statements.

**Prior Year Status:** Lack of support of recorded fixed assets and periodic inventory of fixed assets was reported as a finding in the audits of the College for fiscal years 2001 through 2005.

**Corrective Action Plan per Audit Report:**

The College concurs with the finding. Although a physical inventory of the fixed assets commenced in FY2004 and continued into FY2005, the lack of adequate financial resources precluded the College from procuring the services of a professional to appraise its real properties. Additionally, funding for the purchase of the fixed assets module was requested from the College’s Planning, Budget and Evaluation Council. Once again funding constraints prevented this body from making the funds available for such purposes in FY2004 and 2005. Although funding was set-aside for this purpose in FY2006, it was cut in an effort to address a budget shortfall in FY2006. Funding for this purpose was requested of the NMC Foundation in FY2007 and $50,000 and was approved. The finding should be resolved in time for the FY2007 audit.

**Steps taken to address this audit finding as of March 15, 2008:**

There are two parts to addressing this finding:

1. Appraisal of the College’s real properties to support the carrying values of these properties in the financial statements and,
2. Substantiating the other fixed asset categories, specifically Furniture and Fixtures and Equipment, by updating the balances to reflect a physical inventory of the items.

The following is a summary of the actions taken by the institution to address the above two issues:
1. Appraisal of the College’s real properties:

The College Administration was able to successfully obtain funding of up to $50,000 from the NMC Foundation to address the issue of appraising its real properties, which is a critical piece to resolving this finding. A formal Request for Proposal on the same was published in the local media and two responsible bidders submitted proposals for the same. Work of appraisal of the properties commenced in March 2008 (Copy of the contract enclosed – Exhibit D). The College expects to receive the full report from the appraisers on the real properties (land and buildings) by March 27, 2008. For the purposes of this report, a preliminary report was requested and adjustments were effected to the financial statements to reflect the findings to date (A copy of the restricted preliminary report is enclosed – Exhibit D). On delivery of the final appraisal report, additional adjustments, if warranted, will be made to the respective financial statement accounts to bring the real property values to reflect what is supported by the appraisal report.

2. The physical inventory of other assets:

A physical inventory of the other asset categories has been completed and is available as of September 30, 2007. The College has made the necessary adjustments to its general ledger to reflect balances noted in the physical inventory and has also posted related adjusting entries to reflect the depreciated value of those assets as of September 30, 2007.

The College conducted a formal Request for Proposals for the fixed assets accounting module, as this module currently is not part of the accounting system. The Request for Proposals was published in the local media in December 2007 with formal proposals being received, after clarifications, in January 2008. There were two responsible bidders and through the internal proposal evaluation process Holland Consulting International was selected to provide the software and training on the fixed assets module. The contract for Holland Consulting has been approved and the installment and training schedule is being worked out with the company (Exhibit D).

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).

Accrued Leave

Finding No. 2006-5

Criteria: The accrued leave subsidiary schedule should be reconciled to the general ledger in a timely manner. Further, leave taken by employees should be supported by approved leave requests.
Condition: The accrued leave subsidiary schedule was not reconciled to the general ledger resulting in an overstatement of $252,392. Further, leave taken by one employee was not supported by an approved leave request.

Cause: The cause of the above condition is that adjustments to accrued leave only occur at calendar year end.

Effect: The effect of the above condition is a misstatement of the accrued annual leave liability. An audit adjustment was proposed to correct this condition.

Recommendation: We recommend that the College’s accrued annual leave schedule be reconciled to the general ledger in a timely manner and leave taken be supported by approved leave requests.

Prior Year Status: Lack of regular and timely reconciliation of the accrued annual leave schedule to the general ledger was reported as a finding in the audit of the College for fiscal year 2005.

Corrective Action Plan per Audit Report:

The College concurs with the finding. Due to the various challenges in personnel funding the College was forced to freeze various positions resulting in additional duties being assumed by existing personnel. Unfortunately, as the existing accounting staff members are already overwhelmed with day to day operations, recording of various adjustments to the financial statements were not effected during the course of the financial year and rather deferred to adjustment through the annual audit process. This will continue to be a challenge until such time that staffing levels are increased to meet the needs and demands of the office. Beginning in FY2004, the College started budgeting for such payouts and has seen quite of a few employees leave the College since and as a result cashing out their annual leave. As a matter of practice and for tracking purposes, such payouts are recorded as expenses and adjusted against the accruals at financial year-end.

Steps taken to address this audit finding as of March 15, 2008:

A reconciliation of the accrued annual leave balances has been performed as of September 30, 2007 and adjustments posted to the general ledger to ensure that it accurately reflects the balance per the subsidiary detail. Further, a review of all leave taken during the financial year was performed to ensure that all leave is properly supported by approved leave forms. The College is of the opinion that this resolves this audit finding.

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).
Retirement Expense

Finding No. 2006-6

Criteria: In accordance with Public Law 6-17, Section 8342(b), each autonomous agency, instrumentality, or public corporation of the Commonwealth Government shall make contributions to the Northern Mariana Islands Retirement Fund (the Fund) each year on an actuarially funded basis toward the annuities and benefits provided its members. Section 8342(d) requires both employee and employer contributions be remitted to the Fund within five working days following the end of each payroll date. Further, Public Law 6-41 (an amendment to certain provisions of Public Law 6-17), states that any employer who fails to pay or remit contributions as required shall pay a penalty of 10% per month or part thereof for which the contribution remains unpaid, up to a maximum penalty of 25% of the unpaid contribution.

Condition: The Fund increased the retirement contribution rate to 36.7727% effective October 1, 2005. The College elected not to contribute at this rate as the CNMI government and certain other component units were forgiven such an increase. Additionally, the College’s approved budget submission and its approved budget included the rate utilized by the College to calculate the liability included in the accompanying financial statements. Had the increase been recorded, accrued salaries and benefits payable and benefits expense would have increased by approximately $1,500,000 as of and for the year ended September 30, 2006.

Cause: The cause of the above condition is the uncertainty regarding the applicability of the increased rate.

Effect: The effect of the above condition is potential misstatement of amounts recorded in the College’s financial statements.

Recommendation: We recommend that the College adhere to the requirements of Public Law 6-17.

Corrective Action Plan per Audit Report:

The College concurs with the finding to the extent that if ultimately the College is not exempted from the increase rate of contribution, as in the case of another Government agency, adjustments will need to be made to the financial statements attached hereto. As noted in the finding, in FY2006 the CNMI Retirement Fund increased the rate of contribution for employers participating in the plan from approximately 24% to 36%. The College did not comply with this increased rate of contribution and further elected not to accrue such in the financial statements attached hereto for the following reasons:

- This was not a budgeted expense and the College’s funding from CNMI appropriations was reduced by approximately $2.1M from what was received in FY2005. Had the College elected to accrue for this increase in the contribution rate, the net impact would have been an additional $1.2M in unbudgeted expenses. The College communicated this financial challenge to the CNMI Government.
At the advice of the CNMI Government, the College continued, as is the case with other Governmental agencies and the central Government, to contribute at the approximately 24% rate.

The College will work with the CNMI Government to obtain an exemption from this large increase in the employer rate of contribution to the Retirement Fund and the unfunded obligation it creates for the institution.

**Steps taken to address this audit finding as of March 15, 2008:**

The College began efforts to address this as soon as it was informed of the increased rate of contribution to the CNMI Retirement Fund. Initially, there were differences in interpretations of the law relative to the accrual of the increased rate of contribution. Lawmakers who authored various legislations dealing with the retirement fund contribution rates were of the opinion that the liability for any amounts not funded to NMC would accrue as a liability of the general fund and not as a liability of the College. With the College being placed on “show cause” there is a real sense of urgency at both the Legislative and Administrative levels to assist the College in resolving this issue.

The College Administration made a presentation to the CNMI Legislature on February 13, 2008 regarding the current accreditation action and what is expected of the College to address the same. Included in this presentation was a specific section on the financial concerns and the audit issues which needed to be addressed in the March 15, 2008 Special Report to the Commission. We shared that this particular audit finding required either the resources to be provided to the College to pay the increased rate of contribution to the retirement fund or legislation specifically exempting the College from the rate increase, as was granted to the CNMI Public School System. After this and several subsequent meetings, a Bill was introduced in the House of Representatives (House Bill 16-54 – Exhibit E) to also exempt NMC along with the CNMI Public School System from any increases in the contribution rate to the CNMI Retirement Fund for a period of five years. The College has also obtained legal advice regarding this approach to this issue and received concurrence that it also has a reasonable basis for arguing this position (A copy of the preliminary legal analysis is enclosed – Exhibit E). Based on the College’s discussions with members of the legislature, we expect the Bill 16-54 to be acted on expeditiously and will have completed the legislative process by the end of March 2008. When this Bill becomes law, this audit finding is considered resolved.

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding (s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).
Journal Vouchers

Finding No. 2006-7

Criteria: Segregation of duties and an adequate system of internal control require that journal entries be reviewed for validity and accuracy by someone other than the preparer.

Condition: Journal entries are not always reviewed and approved prior to posting. This situation resulted in duplicate posting and several reversing or correcting entries.

Cause: The cause of the above condition is the absence of independent review of journal vouchers.

Effect: The effect of the above condition is that possible errors are not identified in a timely manner, which could result in misstatements of the financial statements.

Recommendation: We recommend that the College establish policies and procedures requiring that journal entries be reviewed and approved for entry by someone other than the preparer and that the review be evidenced by the reviewer’s signature.

Corrective Action Plan per Audit Report:

The College concurs with the finding. The College has implemented internal procedures that require all journal entries to be reviewed by the Chief Accountant and approved by the Chief Financial and Administrative Officer prior to such being recorded on the accounting system. The College believes this provides the necessary oversight to ensure that only valid and accurate entries are posted to the accounting system.

Steps taken to address this auditing finding as of March 13, 2008:

The College addressed this audit finding and recommendation even prior to such being identified in the audit report. A directive was sent of by the Chief Financial and Administrative Officer on May 16, 2007 (Exhibit F) to all Finance Office personnel wherein it is clearly noted that no journal entries are to be posted by any staff in the finance office prior to such being first reviewed and approved by the Chief Accountant, Ms. Solita Barnes. In addition to the review of the Chief Accountant, entries are also reviewed and approved, as needed, by the Chief Financial and Administrative Officer. Attached is a copy of a journal entry evidencing this review for your ready reference (Exhibit G). The College is of the opinion that the amended process addresses the audit finding.

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).
Procurement and Suspension and Debarment

Finding No. 2006-8

Program

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| U.S. Department of Education / Adult Education - State Grant Program and TRIO Programs / CFDA #s 84.002, 84.042, 84.044 and 84.047 / Federal Award #s V002A050055, P042A051370, P044A020234-05 and P047A030695-05 / Federal Award Periods 07/01/05 - 09/30/06 and 09/01/05 - 08/31/06 | Criteria: Federal regulations state that small purchase procedures are those relatively simple and informal procurement methods for securing services, supplies or other property that do not cost more than the simplified threshold fixed at 41 U.S.C. 403(11) (currently set at $100,000). If small purchase procedures are used, price or rate quotations shall be obtained from an adequate number of qualified sources. Condition: We noted the following: 
- Of total nonpayroll program expenditures of $156,877 under the Adult Education - State Grant Program, fourteen items amounting to $60,148 were tested. Price quotes for the procurement of airfare for two disbursements (check nos. 20376 and 22507) amounting to $6,336 were not provided for review. This matter is reportable as the projected questioned costs exceed the threshold. 
- Of total nonpayroll program expenditures of $334,598 under the TRIO Programs, thirty-five items amounting to $82,334 were tested. Price quotes for the procurement of airfare for eleven disbursements (check nos. 21814, 20400, 22229, 21814, 22191, 21169, 22028, 22673, 22890, 20375 and 22878) amounting to $29,582 were not provided for review. Cause: The cause of the above condition is noncompliance with established federal procurement regulations. Effect: The effect of the above condition is noncompliance with federal procurement regulations and possible questioned costs of $35,918. | $6,336 29,582 |

Corrective Action Plan per Audit Report:

The College strongly disagrees with the finding. The fact of the matter is that there is a limited pool of travel agents available on the island and the carriers which service the island, especially to the mainland, where the bulk of the College travel is made to, is also limited to two airlines (Continental and Northwest). Further, in an effort to avoid prior audit findings and questioned cost which were raised by the auditors, we ensure all travel is made on fully refundable economy tickets and as such, the fares do not differ from agency to agency.

The College makes every effort to ensure that travel expenditures are distributed among the available travel agencies and every effort is made to ensure that the College receives the lowest “fully refundable” fare available to the destination while also considering the frequency of the flight availability and routing of the itinerary. The College will implement procedures, which will require that all travel is alternated between the approximately four reputable travel agencies available in the CNMI in an effort to further systematically distribute such expenditures among travel agencies.
available on the island. The College is at a loss as to what other efforts it needs to make to meet the auditors’ concern.

**Steps taken to address this audit finding as of March 13, 2008:**

Although the College takes issue with the finding, it immediately implemented additional travel procedures to comply with the auditors’ concern. On July 12, 2007, the Chief Financial and Administrative Officer issued a directive outlining “Amended Travel Procedures” to address this audit finding (Exhibit H) to the entire College Community. This directive requires all departments, especially, federal programs, to adhere to a much stricter process for procuring travel and further requires specific documentation of adherence to the amended procedures to be maintained on file for review by the auditors. This is now standard operating procedure at the institution. Through the implementation of these additional procedures, the College is in compliance with recommendation of the auditors.

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).
Procurement and Suspension and Debarment

Finding No. 2006-9

Program
U.S. Department of Agriculture / Cooperative Extension Services and Payments to Agricultural Experiment Stations Under the Hatch Act / CFDA #s 10.500 and 10.203 / Federal Award #s 2006-41100-05700 and 2006-31100-06095 / Federal Award Period 10/01/05 - 09/30/06

Reason for Questioned Costs

Criteria: Federal regulations state that small purchase procedures are those relatively simple and informal procurement methods for securing services, supplies or other property that do not cost more than the simplified threshold fixed at 41 U.S.C. 403(11) (currently set at $100,000). If small purchase procedures are used, price or rate quotations shall be obtained from an adequate number of qualified sources.

Condition: We noted the following:

- Of the nonpayroll program expenditures of $231,432 under the Cooperative Extension Services Program, thirteen items amounting to $48,338 were tested. Price quotes for the procurement of airfare for two disbursements (check nos. 22136 and 22652) amounting to $4,559 were not provided for review. This matter is reportable as the projected questioned costs exceed the threshold.

- Of the nonpayroll program expenditures of $221,841 under the Payments to Agricultural Experiment Stations Under the Hatch Act, eighteen items amounting to $64,153 were tested. Price quotes for the procurement of airfare for three disbursements (check nos. 21149, 22707 and 22136) amounting to $7,512 were not provided for review. This matter is reportable as the projected questioned costs exceed the threshold.

Cause: The cause of the above condition is the lack of an established policy for the procurement of airfare.

Effect: The effect of the above condition is noncompliance with federal procurement regulations and possible questioned costs of $12,071.

Recommendation: We recommend that quotes be obtained for airfare or that travel agents be procured through a request for proposal.

Prior Year Status: Lack of established policy with federal procurement regulations was reported as a finding in the audit of the College for fiscal year 2005.

Total Questioned Costs $ 47,989

Corrective Action Plan per Audit Report:

The College strongly disagrees with the finding. The fact of the matter is that there is a limited pool of travel agents available on the island and the carriers which service the island, especially to the mainland, where the bulk of the College travel is made to, is also limited to two airlines (Continental and Northwest). Further, in an effort to avoid prior audit findings and questioned cost which were raised by the auditors, we ensure all travel is made on fully refundable economy tickets and as such, the fares do not differ from agency to agency.

The College makes every effort to ensure that travel expenditures are distributed among the available travel agencies and every effort is made to ensure that the College receives the lowest "fully refundable" fare available to the destination while also considering the frequency of the flight.
availability and routing of the itinerary. The College will implement procedures, which will require that all travel is alternated between the approximately four reputable travel agencies available in the CNMI in an effort to further systematically distribute such expenditures among travel agencies available on the island. The College is at a loss as to what other efforts it needs to make to meet the auditors’ concern.

Steps taken to address this audit finding as of March 13, 2008:

Although the College takes issue with the finding, it immediately implemented additional travel procedures to comply with the auditors’ concern. On July 12, 2007, the Chief Financial and Administrative Officer issued a directive outlining “Amended Travel Procedures” to address this audit finding (Exhibit H) to the entire College Community. This directive requires all departments, especially, federal programs, to adhere to a much stricter process for procuring travel and further requires specific documentation of adherence to the amended procedures to be maintained on file for review by the auditors. This is now standard operating procedure at the institution. Through the implementation of these additional procedures, the College is in compliance with the recommendation of the auditors.

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).

U.S. Department of Education
Cash Management - Adult Education - State Grant Program and Higher Education Institutional Aid
CFDA #s 84.002 and 84.031, Federal Award #s V002A050055 and P031A020233-05
Federal Award Periods 07/01/05 - 09/30/06 and 10/01/05 - 09/30/06

Finding No. 2006-10

Criteria: The Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments (the Common Rule) states: “Procedures for minimizing the time elapsing between the transfer of funds from the U.S. Treasury and disbursement by grantees and subgrantees must be followed whenever advance payment procedures are used. When advances are made by letter-of-credit of electronic transfer of funds methods, the grantee must make drawdowns as close as possible to the time of making the disbursements.”

Condition: We noted the following:

- Check no. 22521 amounting to $4,367 was released and cleared ninety-five days after cash was received from the grantor agency.
• The supporting invoice, contract or equivalent document could not be provided for one item (document no. CR 108664) amounting to $8,495. This was corrected through an adjustment. However, the check was not released to the vendor nor were the funds returned to the grantor.

• Payroll costs of $25,619 were charged for one employee who did not directly work for the Program. This was corrected through a proposed adjustment. However, the funds received were not returned to the grantor.

• A drawdown of $9,000 related to one purchase (check no. 22453); however, the items bought for the fund are not being used for the program. This was corrected through an adjustment; however, the funds received were not returned to the grantor.

• Supporting invoice, contract or any equivalent document could not be provided for one item (check no. 22762) amounting to $1,874. This was corrected through an adjustment; however, the funds received were not returned to the grantor.

Cause: The cause of the above condition is that the College appears to have overestimated its check clearing pattern and is drawing cash prior to actual check clearance.

Effect: The effect of the above condition is noncompliance with federal cash management requirements. However, no questioned costs result from the condition as the estimated interest liability to the grantor agency is less than $10,000.

Recommendation: We recommend that the College update its check clearing study and draw down in accordance with that study.

Prior Year Status: Lack of regular and timely update of the check clearing study and draw downs was reported as a finding in the audit of the College for fiscal year 2005.

Corrective Action Plan per Audit Report:

The College strongly disagrees with the finding. The College ensures that all cash drawdowns are disbursed in accordance with the federal cash management guidelines. The College has no control over when the vendors clear their checks through the banks. A cut-off test of the checks on hand will clearly evidence that checks are disbursed to the vendors in a timely manner. The cashier on receipt of the check from accounts payable, promptly calls the vendors for pick up. If the vendor does not pick up the check and does not bank the check in a timely manner the College cannot be held responsible. Further, certain off island vendors, as a natural consequence of our remote location, will not be able to bank their checks until received through the postal system. Again, the College has no control over such timing. In instances where the College has had to reclassify/reverse expenditures and drawdowns were already made for such expenses, the College freezes drawdown of funds against such grants until such time that the excess drawdown has been exhausted. As this is a repeat finding, the College, effective immediately, will only drawdown funds for the program after one week from the date of the payment to allow for greater time lapse prior to related cash being drawdown from the Payment Management System (PMS). We will
review the effect of this process on our federal cash balances and make further adjustments to the timing of our drawdowns to minimize the time lapsed between receipt of the cash and clearance from our accounts.

**Steps taken to address this audit finding as of March 13, 2008:**

Although the College takes issue with the finding, it continues to make efforts ensure that funds are only drawdown in time to disburse payments to the vendors. We also make every effort to distribute checks to vendors immediately after the checks are issued. We maintain that when vendors do not pick-up checks in a timely manner or bank them in a timely manner the institution cannot be held hostage to a finding. Further, often times the College advances funds for various federal programs pending receipt of approved budgets, as in the case of the USDA CREES programs, and this results in operations cash being tied up to fund federal program expenditures. Obviously, in these instances the tables are turned. As a matter of practice now, drawdowns are made on a weekly basis thus increasing the time lapsed between disbursements and receipt of the cash from the Payment Management System (PMS). Based on this the College is of the opinion that it has done all within its ability to address the concern.

**Equipment and Real Property Management - All Major Programs**

**Finding No. 2006-11**

**Criteria:** Section 74.34 of 34 CFR 74, *Administration of Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations*, requires grant recipients to maintain property management records and to perform a physical inventory of equipment at least once every two years.

**Condition:** Property management records are not maintained. Furthermore, a physical inventory of equipment has not been taken within the past two years.

**Cause:** The cause of the above condition is a lack of established policies and procedures related to equipment and real property management.

**Effect:** The effect of the above condition is noncompliance with federal property management standards.

**Recommendation:** We recommend that the College establish policies and procedures to ensure compliance with federal property management standards.

**Prior Year Status:** Noncompliance with federal property management standards was reported as a finding in the audits of the College for fiscal years 2001 through 2005.

**Prior Year Status:** Lack of policies and procedures to ensure compliance with federal property management standards was reported as a finding in the audit of the College for fiscal year 2005.
Corrective Action Plan per Audit Report:

The College concurs with the finding. Although a physical inventory of the fixed assets commenced in FY2004 and continued into FY2005, the lack of adequate financial resources precluded the College from procuring the services of a professional to appraise its real properties. Additionally, funding for the purchase of the fixed assets module was requested from the College’s Planning, Budget and Evaluation Council. Once again funding constraints prevented this body from making the funds available for such purposes in FY2004 and 2005. Although funding was set-aside for this purpose in FY2006, such was cut in an effort to address a budget shortfall in FY2006. Funding for this purpose was requested of the NMC Foundation in FY2007 $50,000 and was approved. The finding should be resolved in FY2007.

Steps taken to address this audit finding as of March 13, 2008:

There are two parts to addressing this finding:

1. Appraisal of the College’s real properties to support the carrying values of these properties in the financial statements and,

2. Substantiating the other fixed asset categories, specifically Furniture and Fixtures and Equipment, by updating the balances to reflect a physical inventory of the items.

The following is a summary of the actions taken by the institution to address the above two issues:

1. Appraisal of the College’s real properties:

The College Administration was able to successfully obtain funding of up to $50,000 from the NMC Foundation to address the issue of appraising its real properties, which is a critical piece to resolving this finding. A formal Request for Proposal on the same was published in the local media and two responsible bidders submitted proposals for the same. Work of appraisal of the properties commenced in March 2008 (Copy of the contract enclosed – Exhibit D). The College expects to receive the full report from the appraisers on the real properties (land and buildings) by March 27, 2008. For the purposes of this report, a preliminary report was requested and adjustments were effected to the financial statements to reflect the findings to date (A copy of the restricted preliminary report is enclosed – Exhibit D). On delivery of the final appraisal report, additional adjustments, if warranted, will be made to the respective financial statement accounts to bring the real property values to reflect what is supported by the appraisal report.

2. The physical inventory of other assets:

A physical inventory of the other asset categories has been completed and is available as of September 30, 2007. The College has made the necessary adjustments to its general ledger to reflect balances noted in the physical inventory and has also posted related adjusting entries to reflect the depreciated value of those assets as of September 30, 2007.
The College conducted a formal Request for Proposals for the fixed assets accounting module, as this module currently is not part of the accounting system. The Request for Proposals was published in the local media in December 2007 with formal proposals being received, after clarifications, in January 2008. There were two responsible bidders and through the internal proposal evaluation process Holland Consulting International was selected to provide the software and training on the fixed assets module. The contract for Holland Consulting has been approved and the installment and training schedule is being worked out with the company (Exhibit D).

The College has engaged the services of Deloitte and Touche to perform certain “agreed upon procedures” to ensure that the finding has been adequately addressed. Through this engagement the auditors will provide an independent review of the actions taken by the institution to address this and other findings and their conclusions on whether such actions adequately address the finding(s). A copy of the engagement letter is enclosed for your ready reference (Exhibit B).

U.S. Department of Education
Program Income - Adult Education - State Grant Program
CFDA # 84.002, Federal Award # V002A050055
Federal Award Period 07/01/05 - 09/30/06

Finding No. 2006-12

Criteria: OMB A-110 and CFR 34, Part 80, sec 80.25 allows state grantees of Adult Education and Family Literacy Act (AEFLA) awards to earn program income. Program income from tuition and fees must be: (1) governed by the terms of the agreement between the state grantee and the local subgrantee to which the state provides federal funds; (2) accounted for in the program records; and (3) used only for costs allowable under AEFLA.

Condition: An accounting of the use of program income and a declaration of total program income received for fiscal year 2006 was not included in the Financial Status Report.

Cause: The cause of the above condition is a lack of adherence to the condition and a lack of adequate accounting staff during fiscal year 2006.

Effect: The effect of the above condition is noncompliance with grant terms and conditions.

Recommendation: We recommend that the College ensure that compliance with the criteria is met.

Corrective Action Plan per Audit Report:

The College partially concurs and partially disagrees with the finding. The auditor was provided the documentation, which clearly accounts for all program income and evidences that such is used, as required by federal regulations, for enhancement of the program objectives. All related program income is held in a restricted special account and is accounted for accordingly. We do agree that the FSR did not include documentation and this was the result of lack of adequately trained personnel
on federal reporting requirements. The College, due to the various challenges in personnel funding, was forced to freeze various positions resulting in additional duties being assumed by existing personnel. The College’s federal accountant retired in December 2005 and federal reports due as of that date which covered the financial year ended September 30, 2005 and in subsequent FY2006 reporting quarters were delayed as this position remained vacant until May 2006. In spite of our best efforts to cover this void, due to already inadequate staffing levels in the office and lack of experience of existing staff on federal financial reporting requirements, various federal financial reports were delayed. The College did recruit for the position of Chief Accountant, which was filled in FY2007 and should alleviate some of the staffing concerns in the office and result in improved oversight of the office.

Steps taken to address this audit finding as of March 13, 2008:

As noted in our response to the finding above, this finding was attributable to the fact that various personnel departures as result of resignations and retirements led to a void in certain critical areas in the Finance Office. Recruitment of the vacant positions was also delayed due to the large reduction in the College’s budget in FY2006. This issue was addressed immediately citing the fact that lack of personnel has resulted in audit issues that will only increase if the personnel needs of the Finance Office were not addressed in a timely manner. As a result of these efforts, the College hired a Federal Program Accountant, Ms. Kathy Palacios, effective April 17, 2006 (Exhibit I). The College also filled the Chief Accountant position on April 2, 2007, by hiring Ms. Solita Barnes (Exhibit J). The College also invested resources in training these staff members by funding their travel to conferences and workshops hosted by various federal programs administered by the institution.

To specifically address the issue of the reporting of program income identified in this finding, the federal program accountant was directed to ensure that current and prior federal program Financial Status Reports were updated to reflect program income generated in the respective periods. These reports are now on file at the institution and have also been reported to the federal agencies.

U.S. Department of Education
Reporting - Adult Education - State Grant Program
CFDA # 84.002, Federal Award # V002A050055
Federal Award Period 07/01/05 - 09/30/06

Finding No. 2006-13

Criteria: OMB A-110 and CFR 34, Part 80, sec80.40, requires that the initial report for 15 months and the final report for 27 months (funds are available for obligation for 27 months) after initiation of the program are due 90 days after year end.

Condition: Expenses reported in the final SF-269 were overstated by $36,883.

Cause: The cause of the above condition is a lack of adequate accounting staff during fiscal year 2006.
Effect: The effect of the above condition is noncompliance with the criteria.

Recommendation: We recommend that control policies and procedures be implemented to ensure compliance with the criteria.

Prior Year Status: Lack of control policies and procedures to ensure that federal financial reporting requirements are complied with was reported as a finding in the audit of the College for fiscal year 2005.

Corrective Action Plan per Audit Report:

The College concurs with the finding. The College, due to the various challenges in personnel funding, was forced to freeze various positions resulting in additional duties being assumed by existing personnel. The College’s federal accountant retired in December 2005 and federal reports due as of that date which covered the financial year ended September 30, 2005 and in subsequent FY06 reporting quarters, were delayed as this position remained vacant until May 2006. In spite of our best efforts to cover this void, due to already inadequate staffing levels in the office and lack of experience of existing staff on federal financial reporting requirements, various federal financial reports were delayed. This will continue to be a challenge until such time that staffing levels are increased to meet the needs and demands of the office. The College did recruit for the position of Chief Accountant, which was filled in FY2007 and should alleviate some of the staffing concerns in the office and result in improved oversight of the office.

Steps taken to address this audit finding as of March 13, 2008:

As noted in our response to the finding above, this finding was attributable to the fact that various personnel departures as result of resignations and retirements led to a void in certain critical areas in the Finance Office. Recruitment of the vacant positions was also delayed due to the large reduction in the College’s budget in FY2006. This issue was addressed immediately citing the fact that lack of personnel has resulted in audit issues that will only increase if the personnel needs of the Finance Office were not addressed in a timely manner. As a result of these efforts, the College hired a Federal Program Accountant, Ms. Kathy Palacios, effective April 17, 2006 (Exhibit I). The College also filled the Chief Accountant position on April 2, 2007, by hiring Ms. Solita Barnes (Exhibit J). The College also invested resources in training these staff members by funding their travel to conferences and workshops hosted by various federal programs administered by the institution.

To specifically address the issue of delay in the filing of the related Financial Status report for this program, the federal program accountant was directed to work the Adult Basic Education Program Director to ensure federal reports related to the program are filed in a timely manner. These reports are now on file at the institution and have also been reported to the federal agencies.

U.S. Department of Agriculture
Reporting - Payments to Agricultural Experiment Stations under the Hatch Act
CFDA # 10.203, Federal Award # 311000609505
Federal Award Period 10/01/05 - 09/30/06

Finding No. 2006-14

Criteria: The College is required to submit SF 269 and SF 272, financial reports that should be supported by applicable accounting records and fairly presented in accordance with program requirements.

Condition: The SF 269 was not made available for review and we were therefore unable to determine if the report agreed with the College’s financial records.

Cause: The cause of the above condition is a lack of adequate accounting staff during fiscal year 2006.

Effect: The effect of the above condition is noncompliance with reporting requirements.

Recommendation: We recommend that reports be submitted when due and be supported by applicable accounting records.

Prior Year Status: Lack of management oversight and review was reported as a finding in the audit of the College for fiscal year 2005.

Corrective Action Plan per Audit Report:

The College concurs with the finding. The College, due to the various challenges in personnel funding, was forced to freeze various positions resulting in additional duties being assumed by existing personnel. The College’s federal accountant retired in December 2005 and federal reports due as of that date which covered the financial year ended September 30, 2005 and in subsequent FY06 reporting quarters were delayed as this position remained vacant until May 2006. In spite of our best efforts to cover this void, due to already inadequate staffing levels in the office and lack of experience of existing staff on federal reporting requirements, various federal financial reports were delayed. This will continue to be a challenge until such time that staffing levels are increased to meet the needs and demands of the office. The College did recruit for the position of Chief Accountant, which was filled in FY2007 and should alleviate some of the staffing concerns in the office and result in improved oversight of the office.

Steps taken to address this audit finding as of March 13, 2008:

As noted in our response to the finding above, this finding was attributable to the fact that various personnel departures as result of resignations and retirements led to a void in certain critical areas in the Finance Office. Recruitment of the vacant positions was also delayed due to the large reduction in the College’s budget in FY2006. This issue was addressed immediately citing the fact that lack of personnel has resulted in audit issues that will only increase if the personnel needs of the Finance Office were not addressed in a timely manner. As a result of these efforts, the College hired a
Federal Program Accountant, Ms. Kathy Palacios, effective April 17, 2006 (Exhibit I). The College also filled the Chief Accountant position on April 2, 2007, by hiring Ms. Solita Barnes (Exhibit J). The College also invested resources in training these staff members by funding their travel to conferences and workshops hosted by various federal programs administered by the institution.

To specifically address the issue of the delay in the filing of the related Financial Status reports for this program, the federal program accountant was directed to work with USDA CREES personnel to ensure that federal reports related to the program are filed in a timely manner. These reports are now on file at the institution and have also been submitted to the federal agencies.