



Republic of the Philippines
COMMISSION ON AUDIT
Quezon City

ANNUAL AUDIT REPORT

on the

CAGAYAN ECONOMIC ZONE AUTHORITY

For the Years Ended December 31, 2019 and 2018

EXECUTIVE SUMMARY

INTRODUCTION

The Cagayan Economic Zone Authority (CEZA) was created by virtue of Republic Act No. 7922, otherwise known as the "Cagayan Special Economic Zone Act of 1995." It is a government corporate body mandated to develop, promote, manage and operate the Cagayan Special Economic Zone and Freeport (CSEZFP) as a viable investment and transshipment hub, agro-industrial business, and an attractive tourist destination in order to boost employment and economic opportunities in Northern Philippines.

Spatially, the CSEZFP covers the entire Municipality of Sta. Ana and the Islands of Fuga, Barit, Mabbag in the Municipality of Aparri, Cagayan. Approximately 54,199 hectares of land for prime development falls within the jurisdiction of CEZA broken down as follows:

| | |
|--------------------------------------|--------|
| • Forest Area | 29,800 |
| • Residential Area/Ecotourism/Rivers | 21,252 |
| • Industrial Area | 1,900 |
| • Agro Industrial Area | 1,247 |

CSEZFP has been identified as a potential development impetus for the North Luzon Region. It is a major transshipment point for trade in the Asia-Pacific Rim due to its strategic location between the Pacific Ocean and the South China Sea. The geography is suitable for the development of a seaport and an airport and there is ample suitable surrounding land for the establishment of industrial, commercial and tourism developments.

CEZA is headed by Secretary Raul L. Lambino, Administrator and Chief Executive Officer. The Board of Directors is composed of 12 members and chaired by the Secretary of the Department of Trade and Industry.

Personnel complement as of December 31, 2019 stood at 58 permanent/regular positions, 35 of which are assigned at the Main Office in Mandaluyong City while the remaining are at the Satellite Office in Tuguegarao and Annex Office in Sta Ana, Cagayan. Meanwhile, to ensure that services to clients and stakeholders will not be interrupted, a total of 288 outsourced personnel were deployed in the three offices.

For CY 2019, CEZA has an approved Corporate Operating Budget of P2.635 billion.

FINANCIAL HIGHLIGHTS

Comparative Financial Position

| | 2019 | 2018 | Increase (Decrease) |
|-------------|---------------|---------------|------------------------|
| Assets | 6,902,908,751 | 6,927,553,836 | (24,645,085) |
| Liabilities | 153,466,224 | 188,072,618 | (34,606,394) |
| Equity | 6,749,442,527 | 6,739,481,218 | 9,961,309 |

Comparative Results of Operations

| | 2019 | 2018 | Increase (Decrease) |
|-----------------------|-------------|-------------|------------------------|
| Income | 456,906,085 | 740,551,957 | (283,645,872) |
| Personnel Services | 46,518,632 | 42,594,324 | 3,924,308 |
| Maintenance and Other | | | |
| Operating Expenses | 157,992,498 | 123,147,034 | 34,845,464 |
| Non-Cash Expenses | 195,201,971 | 170,123,579 | 25,078,392 |
| Finance Expenses | 4,940,990 | 2,728 | 4,938,262 |
| Losses | 34,829,988 | 0 | 34,829,988 |
| Income Before Tax | 17,422,006 | 404,684,292 | (387,262,286) |
| Income Tax Expense | 8,365,968 | 109,720,169 | (101,354,201) |
| Net Income/Loss | 9,056,038 | 294,964,123 | (285,908,085) |

SCOPE AND OBJECTIVES OF AUDIT

Our audit covered the examination, on a test basis, of the accounts and transactions of CEZA for the period January 1 to December 31, 2019 in accordance with International Standards of Supreme Audit Institutions (ISSAIs) to enable us to express an opinion on the fairness of presentation of the financial statements for the years ended December 31, 2019 and 2018. Also, we conducted our audits to assess compliance with pertinent laws, rules and regulations as well as adherence to prescribed policies and procedures.

INDEPENDENT AUDITOR'S OPINION ON THE FINANCIAL STATEMENTS

We rendered an unmodified opinion on the fairness of presentation of the financial statements of CEZA for the years 2019 and 2018.

SIGNIFICANT AUDIT OBSERVATIONS AND RECOMMENDATIONS

1. The accuracy and completeness of the Revenue from Licensing Fees amounting to P187.131 million as of December 31, 2019 cannot be ascertained due to insufficient examination and validation of records by CEZA and the Audit Team was unable to conduct validation due to non-access to the system of First Cagayan Leisure and Resort Corporation (FCLRC).

We recommended that Management:

- a) Require its authorized representative/s (including a certified public accountant), as provided in the agreement, to examine and validate regularly the reports submitted by FCLRC to ensure the correctness and completeness of the Revenue from Licensing Fees recognized in CEZA's books; and
 - b) Make representation with FCLRC to provide the COA Audit Team access to its system for audit purposes.
2. The faithful representation of the Lease Income amounting to P14.050 million as of December 31, 2019 could not be ascertained due to the absence of lease agreements between CEZA and two of its tenants, Smart Communications Inc. and Cagayan Electric Cooperative II (CAGELCO II).

We recommended that Management expedite the execution of lease agreements with current lessees who have no existing contracts to cover all CEZA properties being rented out to support the income recognized in its books and determine the accuracy of account balances presented in the financial statements.

3. The monthly rental of P45,000 for the substation leased by CAGELCO II is too low. At this rate, it will take 70 years to recover the cost of this property which has an economic useful life of 30 years only.

We recommended that Management:

- a) Direct the personnel handling the rental of the CEZA properties to monitor the lease agreements and coordinate with the lessees to facilitate the early negotiations for the extension or renewal of agreement at least one month prior to the expiration of the contract; and
 - b) Revisit the terms and conditions of the lease agreements to ensure that the executed contracts are not disadvantageous to CEZA.
4. Provisions of the lease agreement with First Cagayan Leisure and Resort Corporation (FCLRC) were not strictly enforced, thus, its unpaid rental fee accumulated to P10.753 million as of December 31, 2019.

We recommended that Management:

- a) Demand immediate payment from FCLRC and resort to legal action as provided under Section 12 of the lease agreement, if warranted;
 - b) Designate one personnel to review all lease agreements, continuously monitor the compliance of each lessee to the provisions of the terms and conditions of the contract; and
 - c) Include in the lease agreement a provision imposing fines and penalties in case of default or late payments to discourage late payment of rental fees.
5. Several parcels of land purchased with total area of 619,435 square meters worth P8.593 million are still not transferred/registered in the name of CEZA despite the lapse of 20 years, thereby precluding CEZA from claiming full ownership of said parcels of land.

We recommended that Management:

- a) Follow up with the concerned government agencies and secure all the required documents to expedite the processing and transfer of titles in the name of CEZA;
- b) Direct the Legal Department and the Committee on Land Use Reclassification and Land Use Conversion to evaluate immediately the problems encountered during the titling process and instigate legal remedies to facilitate the immediate transfer of land titles to CEZA; and

- c) Take the necessary actions to ensure that the said properties are safeguarded against misuse.

Status of Audit Suspensions, Disallowances and Charges

As of December 31, 2019, the balance of audit disallowances amounted to P3.230 million as indicated in the Statement of Audit Suspensions, Disallowances and Charges (SASDC). The audit disallowances, which remained unsettled, were issued prior to October 6, 2009, the effectivity of COA Rules and Regulations on Settlement of Accounts (RRSA). Of this amount, P2.753 million or 85.23 per cent were suspensions which matured into audit disallowance and the remaining P0.477 million or 14.77 per cent were outright disallowances.

Status of Implementation of Prior Year's Audit Recommendations

Of the fifteen audit recommendations embodied in the CY 2018 Annual Audit Report, ten were implemented, two were partially implemented and three were not implemented. Details are presented in Part III of this Report.

CAGAYAN ECONOMIC ZONE AUTHORITY
STATEMENTS OF FINANCIAL POSITION

December 31, 2019 and 2018

(In Philippine Peso)

| | Note | 2019 | 2018 |
|--------------------------------------|------|----------------------|----------------------|
| ASSETS | | | |
| Current Assets | | | |
| Cash | 3 | 1,588,195,522 | 1,835,542,865 |
| Receivables, net | 4 | 95,805,777 | 147,863,065 |
| Inventories | 5 | 954,690 | 613,683 |
| Total Current Assets | | 1,684,955,989 | 1,984,019,613 |
| Non-Current Assets | | | |
| Investment in Joint Venture | 6 | 691,000,000 | 691,000,000 |
| Other Investments | 7 | 10,000,000 | 10,000,000 |
| Investment Property | 8 | 75,403,894 | 79,693,337 |
| Property and Equipment, net | 9 | 4,282,540,614 | 4,119,885,923 |
| Deferred Tax Assets | | 0 | 4,558,040 |
| Other Non-Current Assets | 10 | 159,008,254 | 38,396,923 |
| Total Non-Current Assets | | 5,217,952,762 | 4,943,534,223 |
| TOTAL ASSETS | | 6,902,908,751 | 6,927,553,836 |
| LIABILITIES AND EQUITY | | | |
| Current Liabilities | | | |
| Financial Liabilities | 11 | 74,383,163 | 4,477,138 |
| Inter-Agency Payables | 12 | 21,179,515 | 174,008,259 |
| Other Payables | 13 | 769,104 | 3,077,319 |
| Total Current Liabilities | | 96,331,782 | 181,562,716 |
| Non-Current Liabilities | | | |
| Trust Liabilities | 14 | 53,105,527 | 5,967,402 |
| Deferred Credits | 15 | 4,028,915 | 542,500 |
| Total Non-Current Liabilities | | 57,134,442 | 6,509,902 |
| Total Liabilities | | 153,466,224 | 188,072,618 |
| EQUITY | | | |
| Government Equity | 16 | 6,749,442,527 | 6,739,481,218 |
| TOTAL LIABILITIES AND EQUITY | | 6,902,908,751 | 6,927,553,836 |

The notes on pages 9 to 43 form part of these financial statements.

CAGAYAN ECONOMIC ZONE AUTHORITY
STATEMENTS OF COMPREHENSIVE INCOME
For the years ended December 31, 2019 and 2018
(In Philippine Peso)

| | Note | 2019 | 2018 |
|--|------|---------------------|-------------|
| REVENUE | | | |
| | 17 | | |
| Licensing Fees | | 187,131,781 | 189,867,269 |
| Processing Fees | | 180,831,410 | 476,315,357 |
| Lease Income | | 14,050,017 | 11,337,810 |
| Seaport System Fees | | 12,362,714 | 7,483,967 |
| Passport, Visa and Application Fees | | 5,720,741 | 7,267,174 |
| Sewerage/Garbage Fees | | 481,200 | 384,000 |
| Permit Fees | | 402,331 | 371,357 |
| Other Business Income | | 1,244,400 | 159,000 |
| | | 402,224,594 | 693,185,934 |
| EXPENSES | | | |
| Personnel Services | 18 | 46,518,632 | 42,594,324 |
| Maintenance and Other Operating Expenses | 19 | 353,194,469 | 293,270,613 |
| | | 399,713,101 | 335,864,937 |
| INCOME FROM OPERATIONS | | 2,511,493 | 357,320,997 |
| OTHER INCOME (EXPENSES) | | | |
| Interest Income | | 5,296,342 | 5,229,284 |
| Loss on Sale of Property and Equipment | | (234,640) | 0 |
| Finance Expenses | | (4,940,990) | (2,728) |
| Gain (Loss) on Foreign Currency Exchange | | (34,595,348) | 26,917,477 |
| Other Fines and Penalties | | 29,388,442 | 8,373,627 |
| Miscellaneous Income | | 542,000 | 1,159,195 |
| | | (4,544,194) | 41,676,855 |
| INCOME (LOSS) BEFORE INCOME TAX | | (2,032,701) | 398,997,852 |
| INCOME TAX EXPENSE | | 8,365,968 | 109,720,169 |
| PROFIT (LOSS) AFTER INCOME TAX | | (10,398,669) | 289,277,683 |
| Subsidy from the National Government | 20 | 19,454,707 | 5,686,440 |
| NET INCOME/TOTAL COMPREHENSIVE INCOME | | 9,056,038 | 294,964,123 |

The notes on pages 9 to 43 form part of these financial statements.

CAGAYAN ECONOMIC ZONE AUTHORITY
STATEMENTS OF CHANGES IN EQUITY
For the years ended December 31, 2019 and 2018
(In Philippine Peso)

| | Note | Share Capital (Note 16) | Retained Earnings (Note 2.8) | Total Equity |
|--|------|-------------------------------|------------------------------------|----------------------|
| Balances, December 31, 2017 | | 5,755,141,585 | 833,845,433 | 6,588,987,018 |
| Changes in Equity for 2018 | | | | |
| Net income for the year | | | 294,964,123 | 294,964,123 |
| Dividends | 12 | | (144,638,841) | (144,638,841) |
| Prior year adjustments, net | | | 168,918 | 168,918 |
| Balances, December 31, 2018 | | 5,755,141,585 | 984,339,633 | 6,739,481,218 |
| Changes in Equity for 2019 | | | | |
| Net income for the year | | | 9,056,038 | 9,056,038 |
| Adjustment in dividends payable for 2018 | 23 | | 15,053,893 | 15,053,893 |
| Dividends | 23 | | (12,269,900) | (12,269,900) |
| Adjustment in the adoption of PFRS 16 | | | (1,878,722) | (1,878,722) |
| Balances, December 31, 2019 | | 5,755,141,585 | 994,300,942 | 6,749,442,527 |

The notes on pages 9 to 43 form part of these financial statements.

CAGAYAN ECONOMIC ZONE AUTHORITY
STATEMENTS OF CASH FLOWS

For the years ended December 31, 2019 and 2018
(In Philippine Peso)

| | Note | 2019 | 2018 |
|--|------|----------------------|----------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | | |
| Receipt of income from operations | | 348,970,084 | 555,186,477 |
| Collection of receivables | | 134,178,814 | 13,077,280 |
| Receipt of subsidy from the National Government | | 19,454,707 | 5,686,440 |
| Receipt of interests from deposits | | 5,296,342 | 5,229,284 |
| Receipt of customers' deposit | | 4,217,500 | 16,202,295 |
| Receipt of unearned income/revenue | | 3,800,000 | 0 |
| Refund of disallowances/cancelled checks | | 3,153,219 | 1,750,932 |
| Amounts received in trust - sale of bid documents, VAT and donations | | 2,415,675 | 1,039,932 |
| Refund of cash advances | | 2,059,305 | 1,939,409 |
| Receipt of guaranty deposit | | 1,949,750 | 600,000 |
| Receipt of miscellaneous income | | 541,000 | 1,159,195 |
| Payment of finance expenses | | (7,266) | (2,728) |
| Payment of guaranty deposit and prepayment | | (770,446) | (6,702,834) |
| Payment of customers' deposit | | (1,849,750) | (13,538,157) |
| Advances to government corporation | | (1,960,400) | 0 |
| Payment of other payables | | (4,342,422) | (2,047,966) |
| Payment of trust receipts - honorarium of BAC members, etc. | | (5,403,316) | (1,199,348) |
| Cash advances to officers & employees | | (11,616,276) | (9,827,521) |
| Payment of personnel services | | (43,529,788) | (42,088,334) |
| Payment of maintenance and other operating expenses | | (165,555,816) | (119,987,074) |
| Net cash generated from operations | | 291,000,916 | 406,477,282 |
| Income taxes paid | | (29,552,245) | (81,916,354) |
| Net cash provided by operating activities | | 261,448,671 | 324,560,928 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | |
| Proceeds from sale of disposed asset | | 8,585 | 0 |
| Capital expenditures | | (346,830,486) | (192,282,169) |
| Net cash used in investing activities | | (346,821,901) | (192,282,169) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | | |
| Payment of dividends | | (129,585,989) | 0 |
| Net cash used in financing activities | | (129,585,989) | 0 |
| EFFECT OF EXCHANGE RATE CHANGES ON CASH | | (32,388,124) | 26,917,477 |
| NET INCREASE (DECREASE) IN CASH | | (247,347,343) | 159,196,236 |
| CASH AT BEGINNING OF YEAR | | 1,835,542,865 | 1,676,346,629 |
| CASH AT END OF YEAR | 3 | 1,588,195,522 | 1,835,542,865 |

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