

June 24, 2011

Tel: 1-671-646-3884
Fax: 1-671-649-4932
www.deloitte.com

Ms. Benita Manglona
Acting Director
Department of Administration
Government of Guam
P.O. Box 884
Hagatna, GU 96910

Dear Ms. Manglona:

In planning and performing our audit of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Government of Guam (GovGuam) for the year ended September 30, 2010, which collectively comprise GovGuam's basic financial statements (on which we have issued our report dated June 24, 2011 and which includes reference to other auditors), in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, we considered GovGuam's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of GovGuam's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of GovGuam's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting. However, in connection with our audit, we identified, and included in the attached Appendix I, deficiencies related to GovGuam's internal control over financial reporting and other matters as of September 30, 2010 that we wish to bring to your attention.

We have also issued a separate report to the Governor of Guam, also dated June 24, 2011, on our consideration of GovGuam's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters.

The definition of a deficiency is also set forth in the attached Appendix I.

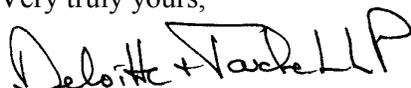
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with this report.

This report is intended solely for the information and use of the management of GovGuam and the Office of Public Accountability and is not intended to be and should not be used by anyone other than these specified parties. However, this report is also a matter of public record.

We will be pleased to discuss the attached comments with you and, if desired, to assist you in implementing any of the suggestions.

We wish to thank the staff and management of the GovGuam for their cooperation and assistance during the course of this engagement.

Very truly yours,



SECTION I – CONTROL DEFICIENCIES

We identified no control deficiencies involving GovGuam’s internal control over financial reporting as of September 30, 2010.

SECTION II – OTHER MATTERS

We identified, and have included below, other matters involving GovGuam’s internal control over financial reporting as of September 30, 2010 that we wish to bring to your attention:

DIVISION OF ACCOUNTS

(1) Cash Imprest Reconciliation

Comment: Reconciliation of general ledger account 110010110 with a balance of \$48,635 or a supporting schedule of imprest accounts was not available during the audit.

Recommendation: General ledger balances should be timely reconciled to detailed sub-ledgers.

(2) Encumbrances

Comment:

- a. Over \$2.5M of encumbrances expired or were invalid as of 09/30/10. An audit adjustment was proposed to decrease the reserve.
- b. \$387K of contracts encumbered were not provided for examination. The validity of these encumbrances was not determinable.

Recommendation: Encumbrances should be periodically approved and reviewed for ongoing pertinence.

(3) Revenues

Comment:

- a. Income tax or gross receipt tax revenues should be supported by a filed tax form.

Five Gross Receipt Tax (GRT) tax forms totaling \$986K were not provided for examination. Classification of the collections was not determinable.

- b. Transactions should be recorded to the proper account.
 1. Ninety-one income tax entries were examined. Approximately \$1.6M of income tax revenues were misclassified within income tax categories.
 2. General Ledger account 110023218 records Guam Tobacco Deposits totaling \$443K. Per 11 GCA - Finance & Taxation, Division 2 - Taxes §26603. Rates 4(d), tobacco tax deposits should be deposited to the Healthy Futures Fund and should not be co-mingled with the General Fund. For the year ended September 30, 2010, ~~we noted~~ these deposits were recorded in the General Fund. We requested POS receipt number 2010361648 for \$24,995; however, such could not be located.

(3) Revenues, Continued

- c. All taxes are entered in or transferred to the system which records revenues and receivables.

GRT1 Receipt #2010501986 was recorded in the amount of \$99,999 on October 20, 2009. The transaction represents a partial payment; however, the tax form filed was stamped paid for the entire amount due, without indication that such was a partial payment. The unpaid GRT balance owed is \$25,493 as of September 30, 2010. The related receivable was not recorded. The extrapolated error yielded an understatement approximately \$1.7M.

Recommendation: We recommend that the Division of Accounts in coordination with the Department of Revenue and Taxation ensure that all revenues are accounted for and processed; revenues are supported by underlying documentation such as an invoice, tax form or other equivalent documentation; and ensure that such are recorded in the proper account classification.

(4) Deposit Liability Account

Comment: Deposit liability accounts should represent assets to be reverted to a party, entity or customer after an obligation, contract or agreement has been fulfilled or satisfied.

1. General ledger account 110023302 represents \$521K of deposits from the Federal Emergency Management Agency (FEMA). A total of \$382K of expenditures were offset against the deposit liability account and were not correctly accounted for in the financial statements.
2. General ledger account 110023268 accounts for transactions related to the Cooperative Agreement Number N40192-08-2-9003. The agreement represents a \$4.4M contract with GovGuam's Department of Agriculture and the U.S. Department of the Navy. A total of \$889K of expenditures were incurred and unreported in the Schedule of Expenditures of Federal Awards. Expenditures were incorrectly reflected against a liability account where an original liability was not established and a corresponding grant receivable was not recognized.

Recommendation: We recommend the Division of Accounts re-examine the nature of the deposit liability accounts and correctly record expenditures and collections in the financial statements.

GUAM POLICE DEPARTMENT / GUAM FIRE DEPARTMENT

(5) Expenditures

Comment: Fuel receipts should be matched to billing details.

The Guam Police Department and the Guam Fire Department did not reconcile fuel charges to underlying fuel receipts.

On an annual basis, GovGuam spends over \$2M on fuel.

Recommendation: We recommend management strengthen controls to ensure fuel receipts are reconciled to underlying billing records.

CUSTOMS, AGRICULTURE AND QUARANTINE

(6) Permanent Transfer

Comment: The Customs, Agriculture and Quarantine Fund (Fund #209) as of September 30, 2010 had a deficit of \$2,195,448. An operating transfer from the General Fund was necessary to address this shortfall.

Recommendation: The Customs, Agriculture and Quarantine division should be monitored to minimize fund deficiencies. The shortfall of the aforementioned fund was primarily due to a building lease that is funded from airport collections and over expenditures. Collections were insufficient to cover the lease commitment. We further recommend Customs, Agriculture and Quarantine seek alternative sources to cover lease obligations or consider including this request in the annual budget.

OFFICE OF THE ATTORNEY-GENERAL

(7) Reconciliation of Account

Comment: Liabilities for the following general ledger accounts did not reconcile to subsidiary ledgers provided by the Child Support Enforcement Division.

	<u>Per DOA</u>	
110021519 - Unclaimed checks		\$ 2,102,815
110027000 - Collections - Child Support		2,190,397
110027100 - Collections - Child Support		<u>1,558,036</u>
Total		\$ <u>5,851,248</u>
	<u>Per Child Support Enforcement Division</u>	
Total		\$ <u>5,288,948</u>
Variance		\$ <u>562,300</u>

Recommendation: Controls should be strengthened over ensuring that general ledger balances are timely reconciled to detailed sub-ledgers

UNIFIED COURTS OF GUAM

(8) Monitoring of A/R Accounts

Comment: The status of probation cases should be timely monitored to enable the issuance of an official court order to facilitate the closure and write-off of uncollectible accounts. The related allowance is \$4.8M, which includes expired probation cases that have had no movement for in excess of five years.

Recommendation: The status of probation cases should be monitored to allow for the legal and timely write-off of expired probation cases.

GENERAL SERVICES AGENCY

(9) Safekeeping of Documents

Comment: A vendor invoice of \$36,571 could not be located in support of a purchase made for supplies/materials.

Recommendation: Documents in support of purchases should be on file.

(10) Procurement

Comment: In accordance with applicable procurement requirements, the grantee will conduct procurement transactions in a manner providing full and open competition, and will maintain records sufficient to detail the significant history of procurement. These records will include a rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price.

Of 98 general fund and other nonmajor governmental funds transactions tested, the procurement rationale was not documented for the following:

<u>Reference no.</u>	<u>Amount</u>
P106A00890	\$ 394,000
P106A01879	78,264
	\$ <u>472,264</u>

Purchase orders used sole source procurement for services rendered, based on the rationale that the vendor was the only distributor/agent. No documentation was on file to indicate or determine that no other vendor could provide the required services.

Recommendation: General Services Agency management should demonstrate open competition in the selection of any vendor in accordance with applicable procurement requirements.

DEPARTMENT OF REVENUE AND TAXATION

(11) IT Investments

Comment: Financial reporting requirements may be significantly impacted if the Single Audit deadline is moved to March 31. Current processes at the Department of Revenue and Taxation utilized to formulate the income tax provision should be reviewed to determine if additional IT investments are warranted. For the year ended September 30, 2010, processing of tax returns to allow for the verification of the income tax provision was not completed until eight months after year end.

Recommendation: Department of Revenue and Taxation management should consider automating the tax filing process to facilitate more timely processing of tax returns and allow for the timely verification of the income tax provision.

(12) Collections of Real Property Tax

Comment: During tests of real property tax revenues, one of thirteen (approx. 8%) items tested resulted in no collection of real property tax and is noted as a delinquent property. We further noted that procedures for delinquency have not occurred.

Recommendation: As real property taxes are due by February 20 for the first installment and April 20 for the second installment, the Department of Revenue and Taxation should ensure controls and procedures are in place to comply with the law.

SECTION III – DEFINITIONS

The definition of a deficiency that is established in AU 325, *Communicating Internal Control Related Matters Identified in an Audit*, is as follows:

A *deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when (a) a properly designed control does not operate as designed, or (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively.

MANAGEMENT'S RESPONSIBILITY FOR, AND THE OBJECTIVES AND LIMITATIONS OF, INTERNAL CONTROL OVER FINANCIAL REPORTING

The following comments concerning management's responsibility for internal control over financial reporting and the objectives and inherent limitations of internal control over financial reporting are adapted from auditing standards generally accepted in the United States of America.

Management's Responsibility

GovGuam's management is responsible for the overall accuracy of the financial statements and their conformity with generally accepted accounting principles. In this regard, management is also responsible for establishing and maintaining effective internal control over financial reporting.

Objectives of Internal Control over Financial Reporting

Internal control over financial reporting is a process affected by those charged with governance, management, and other personnel and designed to provide reasonable assurance about the achievement of the entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. Internal control over the safeguarding of assets against unauthorized acquisition, use, or disposition may include controls related to financial reporting and operations objectives. Generally, controls that are relevant to an audit of financial statements are those that pertain to the entity's objective of reliable financial reporting (i.e., the preparation of reliable financial statements that are fairly presented in conformity with generally accepted accounting principles).

Inherent Limitations of Internal Control over Financial Reporting

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.