

GOVERNMENT OF GUAM RETIREMENT FUND

Report on Compliance and Internal Control over Financial Reporting
Based on an Audit of Financial Statements Performed in Accordance With
Government Auditing Standards

September 30, 2004 and 2003

BURGER & COMER, P.C.
CERTIFIED PUBLIC ACCOUNTANTS

Report on Compliance and Internal Control over Financial Reporting
Based on an Audit of Financial Statements Performed in Accordance With
Government Auditing Standards

The Board of Trustees
Government of Guam Retirement Fund

We have audited the accompanying financial statements of the Government of Guam Retirement Fund (GGRF), as of and for the fiscal years ended September 30, 2004 and 2003, and have issued our report thereon dated March 31, 2005. We conducted our audits 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.

Compliance

As part of obtaining reasonable assurance about whether the GGRF's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards* which are described in the accompanying schedule of findings as Findings 2004-1, 2002-5 and 2002-10.

We also noted certain additional matters that we reported to the Board of Trustees of GGRF in a separate letter dated March 31, 2005.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the GGRF's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the GGRF's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings as item number 2001-17.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider item 2001-17 to be a material weakness.

This report is intended for the information and use of the audit committee, management and the Board of Trustees of the GGRF. However, this report is a matter of public record and its distribution is not limited.

Burger & Conner, P.C.

Tamuning, Guam
March 31, 2005

CURRENT YEAR FINDINGS

Finding No. 2004-1

Criteria

4GCA, Chapter 8, §8127(a) states “At least once each year during the first five (5) years following the allowance of a disability annuity to any member, and at least once in every three (3) year period thereafter, the Board of Trustees shall require any disability annuitant to undergo a medical examination to be made by a place mutually agreed upon, by a physician or physicians engaged by the Board...”

Condition

In two of five disability retiree files tested, there is no indication that the retirees obtained the required medical examinations.

Cause

Lack of enforcement.

Effect

We can not determine whether these disability annuitants remain qualified to receive their annuities. We can not determine whether these annuitants are able to return to gainful employment.

Recommendation

GGRF personnel should enforce compliance with Guam statutes and should perform regular reviews of disability annuitant files to ensure that the required medical examinations are being conducted.

Auditee Response/Corrective Action Plan

We agree with this finding.

The finding is a result of a backlog of documents to be filed into respective individual records. The Records Division is staffed with one (1) clerk supervisor. The Fund is in the process of recruitment of additional clerical staff to address these shortcomings. These positions are expected to be filled prior to the end of fiscal year 2005.

Finding No. 2004-2

Criteria

4GCA, Chapter 8, §8127(a) states “Employees of Fund – The Director may employ such clerical, medical or other assistance as shall be necessary for the proper administration of the Fund. The Director may also engage actuarial or other professional services (this includes computer programmers) to assist in the preparation of the annual reports...”

Condition

The Fund experiences difficulties and delays in the generation of reports from its computer system. The person in charge of generating these reports often is unable to generate these reports without outside assistance.

Cause

The system in place was developed by an outside programming and maintenance company. The person in charge of generating various reports needed for operational purposes seems to lack the required training and experience.

Effect

GGRF may be incurring unnecessary costs to generate what should be routine reports.

Recommendation

GGRF should evaluate the capabilities of the staff in the information technology department to determine if the GGRF’s needs are being met.

Auditee Response/Corrective Action Plan

We agree with this finding.

The Fund is currently seeking training opportunities for our data management staff. The Controller has been tasked with ensuring that data management staffers receive proper training for the Fund’s systems. This will occur during fiscal year 2005.

Finding No. 2004-3

Criteria

4GCA, Chapter 8, § authorizes GGRF to obtain quotes for credit life insurance to protect against the risk that annuitants will pass away before repaying their obligations under the early retirement incentive program (ERIP). The cost of this insurance to GGRF would be the same amount that is provided to all Government of Guam employees under its group term life insurance program. ERIP participants were allowed to purchase up to five years of service, and to pay for these purchases over a period not to exceed fifteen years.

Condition

GGRF has not purchased credit life insurance to cover the ERIP notes. Some of the annuitants have passed away without repaying their notes. GGRF is unable to collect the balance owed by these annuitants, and has obtained a legal opinion that they cannot seek repayment from the annuitants' survivors.

Cause

At the time the ERIP came into existence, management evaluated the cost of obtaining credit life insurance and determined that the cost was prohibitive.

Effect

For the year ended September 30, 2004 GGRF is writing off more than \$319,000 in uncollectible notes receivable. The financial impact is far greater than \$319,000, as the annuities were calculated using the additional years of service being purchased under the ERIP. Even if the ERIP notes are not fully collected by GGRF, the amount of the annuity is not changed. The survivor will collect the higher annuity until the survivor passes away. Further, since GGRF will not collect the entire amount due under the note, GGRF is not able to put those funds to use to produce investment returns.

Recommendation

We believe that current management should consider establishing a reserve to offset the future impact of having to write-off uncollectible note balances.

Management should determine whether they can legally require the survivors to continue paying for the ERIP notes, or find any other appropriate means of collecting on the notes. Alternatively, management should determine whether they can legally reduce the calculated annuity due to the non-payment for the years of service purchased.

Auditee Response/Corrective Action Plan

We agree with this finding.

The Fund was authorized via statute to obtain credit life insurance for participants in this program; however, this was not performed. The Controller has been tasked with developing a viable solution for this finding. He will work with Fund legal counsel to develop legal remedies. This is expected to be completed during fiscal year 2005.

Finding 2004-4

Criteria

Insurance provider rosters should be periodically compared to active DC plan member listings to ensure that all active DC plan members are covered by the group disability/life insurance policy.

Condition

Government of Guam agencies pay premiums to the GGRF. The GGRF determines the premium to pay to the insurance company. GGRF personnel have not compared the payroll information to the insurance provider rosters.

Cause

Unknown.

Effect

Some active members may not be covered. GGRF may be over/under paying the premiums. Additionally, premiums collected from the respective agencies have exceeded the premiums remitted to the providers throughout the years.

Recommendation

Develop policies and procedures to ensure all members are covered and to identify any potential overpayments by the respective agencies.

Auditee Response/Corrective Action Plan

We agree with this finding.

The Fund implemented reconciliation procedures in December 2004 to address this finding. It is important to note that no member has been denied death or disability coverage due to non-payment of premiums.

PRIOR YEAR FINDINGS BEING REPEATED

Finding No. 2003-1 Refund of Contributions

Criteria

4GCA, Chapter 8, §8130 states “Refund on Separation. (a) Upon complete separation from service before a member shall have completed at least twenty (20) years of total contributions, including regular interest, but no payment of interest shall be made in any case which total service is less than one (1) year. Total contributions shall include all contributions made by a member to obtain various types of credit authorized by this Chapter...”

4GCA, Chapter 8, §8137 (b) states “...The amount of contributions by the Government shall be determined by applying the applicable percentage rate of contributions as hereinabove prescribed to the total salaries paid to the members during each payroll period, and all such amounts shall be paid into the Fund following the close of each payroll period, concurrently with the contributions made to the Fund by the members. For the purposes of this Section, the term total salaries of members shall be interpreted to include Base Pay, as defined in 4 GCA § 8301 (1), of members participating in the Government Defined Contribution System.”

4GCA, Chapter 8, §8137 (c) states “An amount resulting from the application of a rate equal to the average rate of return on the investment of retirement funds in the preceding fiscal year of total delinquent payments during the period when such payments are delinquent. In addition an amount equal to one percent (1%) per year of delinquent payments shall be paid over to the Fund as penalty for late payment. As used in this Section, delinquent payments means payments due the Fund pursuant to 4 GCA § 8136 and Subsections (a) and (b) of this Section which are not paid over to the Fund within ten (10) working days after the issuance of payroll checks...”

Condition

In our testing of 20 refunds, we found that refunds to members were for the amount of contributions actually remitted to GGRF, plus interest thereon. In 4 of the 20 refunds tested during the fiscal year 2003 audit, we noted that amounts had been withheld from the member but not remitted to GGRF. If those contributions had been remitted to the GGRF, the members would have received interest on those amounts. As it stands, some members receiving refunds have not received the full amount to which they otherwise would have been entitled.

Cause

GGRF staff computed interest only on contributions actually received.

Finding No. 2003-1, continued

Effect

Members may be entitled to larger refunds, and may have a cause of action to pursue.

Recommendation

We recommend that GGRF consult with legal counsel on this issue.

Auditee response/Corrective Action Plan

We do not agree with this finding. The Fund has a policy of not calculating this interest component unless all contributions are received from the agency that employs the member.

Finding Update

We continue to disagree with this finding. The Fund has a policy of not calculating this interest component unless all contributions are received from the agency that employs the member.

Finding 2002-2 Finalization of Annuity Computations

Criteria

Members who apply for retirement are entitled to an annuity based on average annual salary and years of service. The final annuity must be approved by the Chairman of the Board of Trustees.

Condition

In 17 of the 75 files tested during the fiscal year 2002 audit, the final annuity was not determined in some cases for more than one year.

Cause

There appear to be at least four reasons for such delays:

1. Incomplete documentation provided by the member.
2. Delayed follow-up on pending items by the GGRF staff.
3. List of pending items not maintained in file.
4. Lack of personnel at records section

Effect

Retirees are paid an estimated annuity during the time from being initially approved until the final annuity is determined, and retroactive adjustment is made. Ultimately, the proper annuity is paid to the retiree.

Recommendations

- a. A list of incomplete or pending applications should be maintained.
- b. GGRF staff should follow up on pending items regularly and aggressively.
- c. Documentation should be maintained in the respective files to show that GGRF is acting the pending items consistently.

Auditee Response/Corrective Action Plan

We agree with this finding.

The implementation of an estimated annuity was the result of the delays of any and all income transactions or postings of employee and employer contributions towards individual member accounts, and retrieval of source documents from employing agencies that would complete service and annuity finalizations.

Finding 2002-2 Finalization of Annuity Computations, continued

The Members and Benefits Administrator is working with the Fund's Quality Assurance Section to review and amend standards and procedures to address the tracking, maintenance, and follow up on pending files for annuity finalizations.

Finding Update

The Fund in its fiscal year 2005 budget has budgeted for additional staff to assist with annuity finalizations. These positions are expected to be filled before the end of fiscal year 2005. As previously noted, the implementation of an estimated annuity was the result of the delays of any and all income transactions or postings of employee and employer contributions towards individual member accounts, and retrieval of source documents from employing agencies that would complete service and annuity finalizations. We continue to work with all agencies for the timely receipt of contribution information and contribution receipts, however, the Fund is subject to delays from the members employing agency in the retirement process.

Finding 2002-3 Member Files

Criteria

Files must be maintained for all members and retirees to allow for the proper treatment of contributions and determination of annuities. These files must contain certain documents as required by statute.

Condition

In most of the 75 DB plan and 86 DC plan files selected for testing, we found the files to be disorganized and incomplete. In addition, 3 of the 89 DC plan files requested for fiscal year 2004 could not be located.

Cause

The number of files in the storage area is in the thousands. An indexing system was not put in place when the GGRF was created. Accordingly, there is not one standard system for organizing the documents in the files.

Effect

Determination of contributions, years of service, eligibility, beneficiaries, and other important issues is difficult and inefficient.

Recommendation

Member files should be orderly and should include a checklist of the required documents on the front inside cover of the file. The files should be divided into standardized sections, with the same type of documents placed in the same location in every single file.

Auditee Response/Corrective Action Plan

We agree with this finding.

The Members and Benefits Administrator is working with the Fund's Quality Assurance Section to review and amend standards, procedures, and guidelines to address the discrepancies with the current filing systems. A member file index guide is being created to provide organization of the required source documents. Additionally, The Fund has considered the recruitment of employee positions to augment records division.

Finding 2002-3 Member Files, continued

Finding Update

The Fund in its fiscal year 2005 budget, budgeted for the addition of staff to assist with the filing and records management of member and annuitant files. These positions are expected to be filled before the end of fiscal year 2005.

Finding No. 2002-4 Verification of DC Plan Contributions

Criteria

Article 4 Sections 4.1 (Employee Contributions) and 4.2 (Employer Contributions); indicate that mandatory contributions are to be made at the rates indicated at GCA Section 8208 and 8209, respectively. The rate indicated is 5% in both instances.

Condition

Certain contributions are not being remitted to the plan administrator.

Cause

Participants are not completing enrollment forms in a timely manner.

Effect

At September 30, 2002, more than \$95,000 in unremitted contributions were being held by GGRF. This figure has grown to approximately \$200,000 at September 30, 2003.

Recommendation

Request of all agencies that they require employees to obtain a certification of plan eligibility as well as provide proof of enrollment in the appropriate plan prior to processing the participant's payroll.

Auditee response/Corrective Action Plan

We agree with this finding. However, the Fund has no control over individual employee plan enrollment. We have discussed this with Great-West and they do send correspondence to new employees who fail to enroll. It is up to the individual employee to comply with the mandates of the law. We continue to send out reminder notices to each personnel/human resource department at each respective agency/department to emphasize the importance of the enrollment process.

Finding Update

The Fund in fiscal year 2004 provided all agency heads with a listing of their employees that have not submitted the proper documentation for enrollment in the Defined Contribution Plan. The Fund maintains these member contributions in a separate interest bearing account and will remit these funds to Great-West upon proper enrollment of the member. The Fund continues to work with all agencies to ensure that all new Government of Guam employees provide all the necessary documentation for proper enrollment in the Defined Contribution Plan.

Finding No. 2002-5 Recovery of Fees

Criteria

The recovery or refund of fees previously paid related to the purchase of certain investments should be allocated to the participants.

Condition

Recovered fees are being used to pay the general and administrative charges incurred by the plan administrator.

Cause

Lack of formal guidance in statute or regulation.

Effect

Participants are not being credited with amounts to which they may be entitled.

Recommendation

Adopt regulations addressing the proper treatment of these recoveries. However, until such time GGRF may wish to consider holding any recoveries in a reserve account until appropriate treatment is identified.

Auditee response/Corrective Action Plan

We agree with this finding. The Fund, in fiscal year 2004, is in the process of formulating regulations, potential legislation, and required plan amendments addressing this issue. The Controller, with the assistance of the Investment Specialist, will submit their research to the Investment Committee and their recommendations will be submitted to the Board of Trustees for their review and approval. The Fund will also submit any required draft legislation to the Fund's senate oversight chair for appropriate action.

Finding Update

The Controller and the Investment Specialist have completed their research and will be submitting their findings to the Investment Committee at their regularly scheduled meeting in August 2005 with recommendations that a policy be established by the Board of Trustees formalizing the treatment of these recoveries.

Finding No. 2002-9 Allocation of Forfeitures

Criteria

Title 4, Chapter VIII, Article 2, Section 8210 provides that non-vested employer contributions be credited to a suspense account in the event of a participant's termination. The suspense account is to be maintained for a period of five years following the termination of the member contemplating a return to employment and reinstatement of the forfeited amount. In the event that the forfeited amount is not reinstated, the amount attributable to such member will be released and used to offset future employer contributions in an amount proportionate to the respective employer's contributions in the preceding five years.

Condition

The plan is in its ninth year of existence. It is uncertain if the mechanism is in place to allocate forfeited amounts to the respective employer's future contributions.

Cause

This issue has yet to be encountered and therefore may not have been addressed.

Effect

Proper allocation of the forfeited amounts may prove difficult.

Recommendation

Ensure mechanism to allocate forfeitures is in place and will operate properly.

Auditee response/Corrective Action Plan

We agree with this finding. The Fund, in fiscal year 2004, is in the process of formulating regulations, potential legislation, and required plan amendments addressing this issue. The Controller, with the assistance of the Investment Specialist, will submit their research to the Investment Committee and their recommendations will be submitted to the Board of Trustees for their review and approval. The Fund will also submit any required draft legislation to the Fund's senate oversight chair for appropriate action.

Finding Update

The Controller and the Investment Specialist have completed their research and will be submitting their findings to the Investment Committee at their regularly scheduled meeting in August 2005 with recommendations for policy implementation in accordance with Title 4, Guam Code Annotated, Chapter 8 § 8210 to the Board of Trustees.

Finding No. 2002-10 Use of Forfeitures to Pay Administrative Expenses

Criteria

Section 8210(e) of Article 2, Chapter 4 as amended indicates that forfeitures released from the suspense account shall be first applied to the payment of the plan's administrative expenses as allowed by Section 8217. Section 8217(a) allows the Board of Trustees to assess the plan participants up to two percent (2%) of member and employer contributions as a reimbursement of administrative expenses. Furthermore, Section 8217(c) was added to Article 2, Chapter 8 of Title 4 to indicate that for fiscal years beginning after October 2001 and thereafter, the Board of Trustees may use the forfeitures to offset administrative charges and fees allowed under this section.

Condition

Subsequent to year-end, forfeitures were used to offset administrative expenses. The only fees and charges allowed under Section 8217 are those that are charged to the participants. Since there was no charge to the participants in fiscal year 2002, it may not be appropriate to use these amounts to offset administrative expenses

Cause

We believe the intent of the enacted legislation was to allow the GGRF to recover administrative expenses. We believe that the wording of the legislation does not clearly convey the intent.

Effect

General and administrative expenses may be understated.

Recommendation

If the intent of the legislation was to allow the fund to offset general and administrative expenses without first having to charge the participants, then it may be necessary to amend the legislation. Until this is clarified, GGRF may wish to consider holding any released forfeitures in a reserve account until appropriate treatment is identified.

Auditee response/Corrective Action Plan

We agree with this finding. The Fund, in fiscal year 2004, is in the process of formulating regulations, potential legislation, and required plan amendments addressing this issue. The Controller, with the assistance of the Investment Specialist, will submit their research to the Investment Committee and their recommendations will be submitted to the Board of Trustees for their review and approval. The Fund will also submit any required draft legislation to the Fund's senate oversight chair for appropriate action.

Finding No. 2002-10 Use of Forfeitures to Pay Administrative Expenses, continued

Finding Update

The Controller and the Investment Specialist have completed their research and will be submitting their findings to the Investment Committee at their regularly scheduled meeting in August 2005 with recommendations for policy implementation in accordance with Title 4, Guam Code Annotated, Chapter 8 § 8210 to the Board of Trustees.

Finding No. 2001-17 – DC Plan General Ledger Details

Criteria

General ledger accounts should be routinely reconciled.

Condition

With the exception of cash, earnings, change in value and administrative fees, virtually all general ledger accounts are not routinely reconciled to underlying records and source documents.

Cause

Lack of formal accounting policies and procedures.

Effect

Financial reporting can become unreliable.

Recommendation

Establish formal accounting policies that include the reconciliation of significant general ledger accounts.

Prior Year Status

This finding was reported in fiscal year 2000 and 1999 as Finding 1999-6.

Auditee response/Corrective Action Plan

We agree with this finding.

Monthly/Quarterly reconciliations are being performed to tie transactions per G/L to FASCORP statements.

Finding Update

The Fund experienced the loss of the General Accounting Supervisor and Accountant II during the months of October 2004 and November 2004 respectively. This loss resulted in the shifting of their accounting responsibilities to other staff as additions to their regular responsibilities for both the defined Benefit Plan and the Defined Contribution Plan. The Fund is in the process of hiring for both positions and expects to fill the positions by the close of fiscal year 2005.