

**GUAM WATERWORKS AUTHORITY**

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**INDEPENDENT AUDITORS' REPORT ON  
COMPLIANCE AND ON INTERNAL CONTROL**

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**SEPTEMBER 30, 2004**

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND COMPLIANCE AND OTHER MATTERS BASED UPON THE AUDIT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Consolidated Commission on Utilities:

We have audited the financial statements of the Guam Waterworks Authority (the Authority) as of and for the year ended September 30, 2004, and have issued our report thereon dated June 17, 2005. We conducted our audit 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Authority'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 operations of the internal control over financial reporting that, in our judgment, could adversely affect the Authority's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items number 2004-01 to 2004-19.

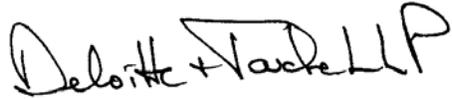
A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected 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, we believe the reportable conditions described above are not material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority'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 no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

However, we noted other matters involving the internal control over financial reporting that we have reported to management of the Authority in a separate letter dated June 17, 2005.

This report is intended for the information of the management of the Guam Waterworks Authority, the Consolidated Commission on Utilities, the Office of the Public Auditor of Guam, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

A handwritten signature in black ink that reads "Deloitte + Touche LLP". The signature is written in a cursive, stylized font.

June 17, 2005

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND INTERNAL CONTROL  
OVER COMPLIANCE APPLICABLE TO EACH MAJOR FEDERAL AWARD PROGRAM  
AND ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

Consolidated Commission on Utilities:

Compliance

We have audited the compliance of the Guam Waterworks Authority (the Authority) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2004. The Authority's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Authority's management. Our responsibility is to express an opinion on the Authority's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Authority's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Authority's compliance with those requirements.

As described in item 2004-01 in the accompanying Schedule of Findings and Questioned Costs, the Authority did not comply with the requirement regarding procurement that is applicable to its Environmental Protection Agency (66.476) program. Compliance with such requirement is necessary, in our opinion, for the Authority to comply with requirements applicable to its program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Authority complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2004.

### Internal Control Over Compliance

The management of the Authority is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Authority's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

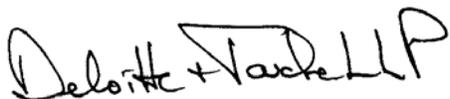
We noted a matter involving the internal control over compliance and its operation that we consider to be reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Authority's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grants. The reportable condition is described in the accompanying Schedule of Findings and Questioned Costs as item 2004-01.

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 noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program 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 compliance 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, we believe the reportable condition described above is not a material weakness.

### Schedule of Expenditures of Federal Awards

We have audited the financial statements of the Guam Waterworks Authority as of and for the year ended September 30, 2004, and have issued our report thereon dated June 17, 2005. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Supplementary Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. This schedule is the responsibility of the management of the Authority. Such information has been subjected to the auditing procedures applied in our audit of the financial statements and, in our opinion, is fairly stated, in all material respects when considered in relation to the basic financial statements taken as a whole.

This report is intended for the information of the management of the Guam Waterworks Authority, the Consolidated Commission on Utilities, the Office of the Public Auditor of Guam, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.



June 17, 2005

**GUAM WATERWORKS AUTHORITY**

Schedule of Expenditures of Federal Awards  
Year Ended September 30, 2004

CFDA #	Federal Grantor/Program Title	Accrued (Deferred) Balance at September 30, 2003	Expenditures	Cash Receipts	Accrued (Deferred) Balance at September 30, 2004
<b>U.S. Department of the Interior</b>					
Pass-Through Government of Guam Department of Administration					
15.875	Economic, Social and Political Development of the Territories and Freely Associated States	\$ 287,561	\$ -	\$ -	\$ 287,561
	Total U.S. Department of the Interior	<u>287,561</u>	<u>-</u>	<u>-</u>	<u>287,561</u>
<b>U.S. Environmental Protection Agency</b>					
Direct Grant					
66.418	Construction Grants for Wastewater Treatment Works	-	345,854 *	(292,575)	53,279
66.468	Safe Drinking Water State Revolving Fund	-	35,503	(35,503)	-
66.476	Vulnerability Assessments and Related Security Improvements at Large Drinking Water Utilities	(115,000)	115,000 *	-	-
66.600	Comprehensive Water Resources Master Plan - Phase I	<u>-</u>	<u>208,000 *</u>	<u>-</u>	<u>208,000</u>
	Total U.S. Environmental Protection Agency	<u>(115,000)</u>	<u>704,357</u>	<u>(328,078)</u>	<u>261,279</u>
<b>Federal Emergency Management Agency</b>					
Pass-Through Government of Guam Department of Administration					
83.544	Public Assistance Grants	<u>(138,338)</u>	<u>30,636</u>	<u>(269,020)</u>	<u>(376,722)</u>
	Total Federal Emergency Management Agency	<u>(138,338)</u>	<u>30,636</u>	<u>(269,020)</u>	<u>(376,722)</u>
	Total Federal Assistance	<u>\$ 34,223</u>	<u>\$ 734,993</u>	<u>\$ (597,098)</u>	<u>\$ 172,118</u>

\*Denotes a major program as defined by OMB Circular A-133.

The Schedule of Expenditures of Federal Awards is prepared on the accrual basis of accounting.

# GUAM WATERWORKS AUTHORITY

## Schedule of Findings and Questioned Costs Year Ended September 30, 2004

### Part I - Summary of Auditors' Results

1. The Independent Auditors' Report on the financial statements expressed an unqualified opinion.
2. Reportable conditions in internal control over financial reporting were identified, none of which were considered to be material weaknesses.
3. No instances of noncompliance considered material to the financial statements were disclosed by the audit.
4. A reportable condition in internal control over compliance with requirements applicable to major federal award programs was identified, which was not considered to be a material weakness.
5. The Independent Auditors' Report on compliance with requirements applicable to major federal award programs expressed a qualified opinion.
6. The audit disclosed findings required to be reported by OMB Circular A-133.
7. The Authority's major programs are:

<u>Name of Federal Program or Cluster</u>	<u>CFDA Number</u>
Environmental Protection Agency	66.418
Environmental Protection Agency	66.476
Environmental Protection Agency	66.600

8. A threshold of \$300,000 was used to distinguish between Type A and Type B programs as those terms are defined in OMB Circular A-133.
9. The Authority did not qualify as a low-risk auditee as that term is defined in OMB Circular A-133.

### Part II - Financial Statement Findings Section

<u>Reference Number</u>	<u>Finding</u>	<u>Questioned Costs</u>
2004-01	Procurement	\$ -
2004-02	Inventory Costing	\$ -
2004-03	Project Costs	\$ -
2004-04	Supporting Documents	\$ -
2004-05	Construction Contract Management and Accounting	\$ -
2004-06	Exception in Meter Readings	\$ -
2004-07	Disconnection Policies	\$ -
2004-08	Policies and Procedures, Systems Control Over New Accounts	\$ -
2004-09	Fixed Assets Existence	\$ -
2004-10	Fixed Assets: Capitalization Policy	\$ -
2004-11	Internal Audit	\$ -
2004-12	Monthly Bank Reconciliation	\$ -
2004-13	Federal Compliance Administrator	\$ -
2004-14	Disbursement Processing	\$ -

# GUAM WATERWORKS AUTHORITY

## Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2004

### Part II - Financial Statement Findings Section, Continued

<u>Reference Number</u>	<u>Finding</u>	<u>Questioned Costs</u>
2004-15	Redundant AS/400 Users	\$ -
2004-16	System Values	\$ -
2004-17	Proper User Class Settings	\$ -
2004-18	User Class Special Authorities and Limited Capabilities	\$ -
2004-19	Accounts payable: Delayed Resolution of Disputed Charges	\$ -

### Part III - Federal Award Findings and Questioned Cost Section

<u>Reference Number</u>	<u>CFDA Number</u>	<u>Finding</u>	<u>Questioned Costs</u>
2004-01	66.476	Procurement	\$ 115,000

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding No.: 2004-01  
CFDA No.: 66.476  
Program Name: U.S. Environmental Protection Agency  
Grant Agreement #: 83005501  
Area: Procurement  
Questioned Costs: \$115,000

Criteria:

Management should ensure that procurement files related to Federal funds are safeguarded throughout the duration of the project and for a specified period thereafter in accordance with Federal requirements.

Condition:

The Authority is unable to provide evaluation reports supporting the selection of the vendor who received the following payments:

<u>Invoice No.</u>	<u>Amount</u>
COP # 1	\$ 13,500
COP # 2	25,000
COP # 3	35,000
Final Billing	<u>41,500</u>
Total Questioned Costs	\$ <u>115,000</u>

Cause:

The underlying cause appears to be due to a lack of internal controls over the safeguarding of procurement files.

Effect:

No known material effect on the financial statements results from this finding. However, questioned costs may affect the entity's ability to receive future Federal funds.

Recommendation:

Management should maintain procurement files for the duration of the particular project in accordance with Federal requirements.

Auditee Response:

GWA concurs with this finding.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-02 – Inventory Costing

Criteria:

Costing of inventory should be consistent with current policy (weighted average FIFO methodology).

Condition:

We tested nineteen items with a total book value of approximately \$1,246,000. The costs of the following items were misstated:

<u>Item No</u>	<u>Description</u>	<u>Unit Cost</u>			<u>Qty</u>	<u>Total</u>
		<u>Book</u>	<u>Curr Invoice</u>	<u>Variance</u>		<u>Variance</u>
N/A	Brass Ball Valve w pad wing ¾”	34	20	14	2,234	\$ 32,200
17-0050	Repair clamp 1 1/2” x 6”	58	5	53	296	15,703
N/A	Gate Valve MJ	450	464	(14)	165	(2,295)
12-0111	D.B. Full Circle Clamp 12 x 10”	476	495	(19)	343	(6,517)
03-0300	Submersible Motor 30 hp	6,720	3,800	2,920	3	8,760
03-0055	Submersible Motor 60 hp	6,500	3,902	2,598	3	7,794
N/A	Full Circle Clamp	220	129	91	460	41,730
15-0150	PVC pipe 2 x 20”	28	27	1	3,423	3,174
01-0110	MJ Gate Valve	900	972	(72)	54	(3,900)
N/A	PVC Pipe	550	12	538	51	<u>27,418</u>
						\$ <u>124,067</u>

Cause:

Inventory movements were not tracked and the costing application included within the inventory module was not scrutinized.

There appears to be lack of internal control over inventory receipt and issuance. There is also a lack of control over the safeguarding of documentation related to recording inventory receipts and issuances.

Effect:

Inventory was immaterially misstated. However, management adjusted the above when such were brought to their attention during the audit process.

Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

Recommendation:

The Authority should ensure that procedures are in place to identify inventory items and should properly record items as they are received and issued. All documentation related to goods received or issued should be properly filed and safeguarded.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-02 – Inventory Costing, Continued

Auditee Response:

GWA is aware of the finding and the related problems tracking and controlling inventory items. An initiative is underway to improve the usage of the inventory module in GWA's enterprise wide software package. GWA believes this will reduce the occurrences of this type of finding.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-03 – Project Costs

Criteria:

Accumulated project costs should be maintained in a systematic way to allow for efficient analysis and reporting. Comparing expected costs against historical costs is intrinsic to the planning process and should occur for every project. Furthermore, purchase orders and respective contracts with vendors should be limited to the expected amounts.

Condition:

Project descriptions are not easily identified on the purchase orders. Apparently, the procurement process is not being utilized in these instances to limit and identify costs to related projects.

Cause:

Because the Project Cost Tracking module within the IBM/JDE system is not being utilized, there is a lack of historical information on project costs. Project managers and end-users cannot utilize any portion of the module.

Effect:

Operating expenses, particularly project cost related, may be uncontrolled. The Authority may be experiencing cost overruns. Future projects cannot be adequately planned in terms of projecting and controlling costs.

Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

Recommendation:

The Authority should implement and utilize the Project Cost Tracking module for all projects. Members of accounting and engineering should conduct periodic field audits to ensure costs are reasonable and identifiable to a project.

Auditee Response:

GWA is aware of the problem. GWA has hired a Chief Engineer and have tasked him with working to address this problem.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-04 –Supporting Documents

Criteria:

Effort should be made to ensure the proper safekeeping of supporting documents.

Condition:

The following supporting documents, i.e. vendor’s invoices, procurement documents, receipts, approved timecards, and approved annual leave forms could not be provided for examination.

A: Fixed Asset Acquisition (vendor invoice):

Asset #	P.O. #	Vendor #	Amount
11509	250371	21633	\$ 8,832

B: Employee approved timecards:

	Emp #	PPE
1	246	04/17/04
2	395	11/15/03
3	488	11/29/03
4	646	09/18/04
5	603	07/10/04
6	438	05/01/04
7	136	11/01/03
8	453	07/24/04
9	509	02/21/04

C: Employee approved annual leave forms:

	Emp #	PPE
1	182	06/26/04
2	136	11/01/03
3	509	02/21/04

D: Procurement documents (i.e. RFP, Invitation to Bid, Bid abstract, price quotes, etc.)

P.O. #	Amount
250177	\$ 90,400
250206	59,902
250650	160,825
251227	53,730

E: Documentation on selection process (lowest bidder):

P.O. #	Amount
250011	\$14,790
250985	14,999
RFP 2004-04	N/A

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-04 –Supporting Documents, Continued

Condition, Continued:

F: No other price quotation from other vendors:

P.O. #	Amount
250124	\$14,999

G: Account reconciliation for vendor #18892.

H: Minutes of the Board of Directors 2004 section and October 2004 to the report date.

I: Journal entry explanations for the following:

<u>G/L Date</u>	<u>Reference</u>	<u>Amount</u>
9/30/04	JE	\$ 180,140
9/30/04	JE	33,880
9/30/04	JE	38,011
9/30/04	JE	439,608
9/30/04	JE	70,238
9/30/04	JE	64,454

Cause:

There appears to be lack of internal control over safekeeping of accounting and administrative documents.

Effect:

No known material effect on the financial statements results from this condition. However, the propriety of underlying account balances may be questioned.

Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

Recommendation:

The Authority should ensure proper safekeeping of supporting documents.

Auditee Response:

GWA has been working to address problems related to the safeguarding of documents. GWA believes a great deal of improvement has been made in the last couple of years and that based on measures already taken, many of these instances will be reduced in the future. GWA recognizes the improvements have not been sufficient and need to continue.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-05 – Construction Contract Management and Accounting

Criteria:

An accurate construction work in progress (CWIP) subsidiary ledger should be properly maintained through constant coordination between the engineering and accounting departments. The contract management system should be designed to provide for accurate flow of significant information. At any point in time, the CWIP subledger total should agree with the amount in the general ledger.

Condition:

While many CWIP projects were closed during fiscal year 2004, the following projects should have been closed, but were not.

<u>Project Name</u>	<u>Projects Total</u>
Vulnerability Assessment Plan	\$ 115,000
CPE for Agat, Baza Gardens	<u>187,226</u>
TOTAL	\$ <u>302,226</u>

Cause:

The cause of this condition is the lack of coordination between the engineering and accounting departments, compounded by the shortage of knowledgeable personnel to whom the duties of recording capital purchases and maintaining CWIP listings could be assigned.

Effect:

The propriety of underlying account balances may be questioned. Depreciation expense is understated by an immaterial amount as projects remain in CWIP, and are not depreciated. Furthermore, the control procedure of attempting to reconcile ongoing and completed projects with accounting records is rendered ineffective.

Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

Recommendation:

The Authority should define and implement a system of construction contract management involving both qualified and knowledgeable personnel from the engineering and accounting departments. The JDEdwards system should be utilized to the fullest extent possible to limit human error and to optimize efficiency.

Auditee Response:

GWA has a knowledgeable plant accountant who has been tasked with reviewing open projects during the year to ensure this type of finding does not recur.

## GUAM WATERWORKS AUTHORITY

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2004

#### Finding Number 2004-06 – Exception in Meter Readings

##### Criteria:

Abnormal readings (those appearing on exception reports) should be verified by the Authority's Task Force. Adjustments made should be reflected on all applicable billings before delivery to customers.

##### Condition:

For five out of sixty-two (8%) transactions tested, the readings were not comparable with previous and subsequent billings.

##### Cause:

GWA had little to no control over ensuring adequate efforts were made by readers. Consequently, the Authority cannot ensure exceptions are kept as low as possible. The Authority's Task Force is therefore overwhelmed with investigating a disproportionately large number of exceptions.

##### Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

##### Effect:

Revenue may be misstated due to the absence of adjustments to unverified accounts. Non-registering meters left unidentified will result in unbilled consumption and thus increased water loss.

##### Recommendation:

All readings appearing on the exception report should be verified. The Authority should weigh the benefit of reducing the likely misstatement of revenue against the cost of paying additional people to verify abnormal readings. The Authority has already addressed the concern of defective, non-registering meters, which are most likely causing a substantial percentage of abnormal readings.

##### Auditee Response:

GWA has recognized for a long time that there are significant problems resulting from outdated meters. GWA has had a project underway for the last two years to purchase a completely new inventory of radio read meters for each of GWA's customers. GWA believes the implementation of these meters will greatly reduce the number of exceptions appearing on GWA's billing exception reports.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-07 – Disconnection Policies

Criteria:

Pursuant to the provisions of Guam Waterworks Authority's Rules and Regulations of Water and Sewer Services, delinquent accounts shall be subject to discontinuation of services.

Condition:

Of sixty-two revenue accounts reviewed, nine were still classified as "active" while delinquent and were incurring additional monthly charges. These accounts should have been disconnected per GWA's disconnection policies, but had not as of year end.

Cause:

Guam Waterworks Authority represents that it does not have the manpower on both the customer service side to track the account and on the operations side to remove or have the knowledge of the exact location of the meter to disconnect the non-paying customers.

Effect:

Due to lack of enforcement of collection of outstanding water charges billed to customers, the collectibility of accounts receivable balances is questionable.

Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

Recommendation:

The Authority should ensure that nonpaying customers are disconnected in accordance with applicable policies and procedures.

Auditee Response:

GWA believes great improvement has been made in this area as opposed to previous years. The Consolidated Commission on Utilities has requested that GWA management enter into a contract with a private company to assist in the overload of disconnections that are required.

## GUAM WATERWORKS AUTHORITY

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2004

#### Finding Number 2004-08 – Policies and Procedures, Systems Control Over New Accounts

##### Criteria:

The Guam Waterworks Authority should ensure that policies and procedures and systems controls exist that prevent customers from opening another account (in the same physical location) if the original account outstanding balance is significant and remains outstanding.

##### Condition:

It appears the IBM/JD Edwards System does not prevent customers from applying for a new account even though the application for a new account is for an exact location where an outstanding balance exists. We further noted that disconnected customers with outstanding balances request family members to open a new account in the same physical location.

##### Cause:

Currently, the Authority's services rules and regulations do not allow the agency to refuse service under these circumstances.

##### Effect:

Due to lack of internal policies and procedures, the collection of accounts receivable may be in question.

##### Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

##### Recommendation:

The Authority should implement policies and procedures and computer system controls relating to application for a new account in the same physical location where a prior account with an outstanding balance already exists. Further, documents such as new renter agreements, deeds of sale or other items should be reviewed to deter family members from opening new accounts at the same location.

##### Auditee Response:

GWA disagrees with this finding. GWA's customer rules and regulations do not allow GWA to prevent family members from applying at a residence where another family member has an outstanding bill. This results from a defect in GWA's customer rules and regulations. GWA intends to correct this problem, but it cannot be achieved without going through the Administrative Adjudication process with the Guam Legislature.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-09 – Fixed Assets Existence

Criteria:

Fixed assets should be properly tagged and safeguarded against loss and should not be subject to misuse. Fixed asset accountability should be vested in a Fixed Asset Accountant. Any impairment, loss or damage of fixed assets should be reflected on the books.

Condition:

Eight of seventeen (17) fixed assets tested, with a total sample cost of \$585,833 and a net book value of \$201,541, could not be located.

	<u>Asset #</u>	<u>Description</u>	<u>Year</u>	<u>Cost</u>	<u>NBV at 9/30/04</u>
1	85892	Airconditioning 12000 BTU	1999	\$ 4,400	\$ 2,237
2	11114	Backhoe Loader	2001	47,999	15,999
3	94596	40" Foot Aluminum High Cube	2000	3,900	2,210
4	10997	Air Compressor w/ Accessories	2002	2,395	1,198
5	107617	Water Blaster w/ Accessories	2001	3,395	962
6	74350	Pump & Motor Submersible 8"	1996	15,874	3,307
7	74376	Pump & Motor US 50HP Frame 3	1997	<u>16,907</u>	<u>4,931</u>
				<u>\$93,870</u>	<u>\$30,934</u>

Cause:

The Authority has no formal policy creating accountability over fixed assets.

Effect:

As a result of this condition, assets are susceptible to loss and/or misuse. Because the lost, damaged or stolen assets must be replaced years before the end of their useful lives, cash outflows increase unnecessarily. The failure to write-down impaired assets to fair market value or to increase depreciation when required results in the overstatement of fixed assets. The expense for non-capitalized tools and equipment increases, thereby lowering net income.

Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

Recommendation:

The Authority should establish, implement and monitor a firm policy for the accountability over fixed assets and equipment purchases. A qualified, trained person should be appointed as a fixed asset (plant) accountant, and should perform duties stated in the policy to ensure assets are safeguarded from loss and/or misuse.

Auditee Response:

GWA concurs with the finding.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-10 – Fixed Assets: Capitalization Policy

Criteria:

Additions to fixed assets should represent actual utility plant in service or general plant additions, and should not include parts and materials. The duty to ensure that this occurs should be assigned to a Fixed Asset Accountant, a person in charge solely of additions, issues, receipts, and disposals of fixed assets. The impairment, loss or damage of fixed assets should be reflected on the books via write-down entries.

Condition:

During our review of fixed asset additions, the following assets appear to be more appropriately categorized as materials inventory than fixed assets.

<u>Item #</u>	<u>Description</u>	<u>Amount</u>
11589	A/B Pressure Switch 5 Amps	\$ 2,665
11674	10" Plug Valve	5,691
11676	Safety Switch 100 Amps	2,720
11491	Anthracitefil Anthracite Filter	6,450
11492	Silicasanfil Silica Sand Filter	2,414
11493	Garnetsandfil Garnet Sand Filter	965
11510	Pin Shear 6.25 Diameter	72
11508	Chain H Mill	1,350
11507	Sprocket Drive	250
11506	Segment Sprocket	720
11505	Shoe Wear	810
11504	Shoe Wear	900
11503	Block Spacer	50

Cause:

The Authority has no formal policy defining distinctions between fixed assets and inventory.

Effect:

As a result of this condition, assets may be overstated. Given the double counting of items as both inventory and fixed assets, there is a possibility that other account balances may be questionable as the expense for non-capitalized tools and equipment is not recorded, thereby inflating net income.

Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

Recommendation:

The Authority should establish, implement and monitor accountability over fixed asset and equipment purchases. A qualified, trained person should be appointed as fixed asset (plant) accountant, and should perform duties stated in the policy to ensure assets are safeguarded from loss and/or misuse.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-10 – Fixed Assets: Capitalization Policy, Continued

Auditee Response:

This has been an ongoing problem and GWA believes there has been great improvement in this area over prior years. GWA will continue to work on its review process for purchases to ensure these are appropriately categorized in the future.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-11 – Internal Audit

Criteria:

The Authority should consider establishing a qualified Internal Audit function to perform, among other duties, check and review procedures on transaction processing, revenue protection, and ensuring departmental adherence to Standard Operating Procedures.

Condition:

There are no checks and review procedures performed independently of the specific department adherence to Standard Operating Procedures.

Cause:

The Authority does not have an internal auditor in place to perform this function.

Effect:

With the lack of an Internal Audit Department, the Authority faces a greater risk of loss, misuse of assets and a potential misstatement of account balances.

Prior Year Status:

The above condition is reiterative of conditions identified in the prior year audit of the Guam Waterworks Authority.

Recommendation:

The Authority should consider creating an Internal Audit department and should continue its efforts to avail itself of services of the Guam Power Authority internal audit department.

Auditee Response:

The Consolidated Commission on Utilities has determined that a single Internal Auditor should be utilized by the Guam Power Authority and the Guam Waterworks Authority. There has been some turnover in this position which has delayed implementation of the extended scope of services, however, it is believed this function will be active by the end of the current fiscal year.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-12 – Monthly Bank Reconciliation

Criteria:

Bank accounts should be reconciled in a timely manner.

Condition:

Certain bank accounts are not reconciled on a monthly basis.

<u>Bank</u>	<u>Account #</u>
Community First Credit Union	132355
Oceanic Bank	2116901
First Hawaiian Bank	3064476
Citibank	310336
Bank of Hawaii	0038095390
Citizens Security Bank	2200004844
BankPacific	700800313
Bank of Guam	0601014149
Bank of Guam	0101191373
First Hawaiian Bank	03918424

The above accounts were only reconciled as of September 30, 2004.

Cause:

There appears to be lack of manpower to ensure bank accounts are reconciled on a monthly basis.

Effect:

No known material effect results from this condition. However, cash shortages and overages may not be identified in a timely manner. Furthermore, the control procedure of regularly reconciling bank statements is rendered ineffective.

Recommendation:

The Authority should delegate a responsible staff to ensure bank accounts are reconciled timely.

Auditee Response:

GWA concurs with this finding.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-13 – Federal Compliance Administrator

Criteria:

The Authority should consider establishing a Federal Compliance Administrator function, to perform, among other duties, check and review procedures on transaction processing, revenue protection, and ensuring adherence with federal requirements.

Condition:

There are no checks and review procedures performed independently of a specific department to ensure adherence to Federal compliance requirements.

Cause:

The Authority does not have a federal compliance administrator.

Effect:

With the lack of Federal compliance administrator, the Authority faces a greater risk of loss, misuse of federal funds and a potential misstatement of account balances.

Recommendation:

The Authority should consider creating federal compliance administrator position.

Auditee Response:

GWA does not believe that a new senior financial officer position is prudent or necessary to ensure proper accountability of federal funds.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-14 – Disbursement Processing

Criteria:

Disbursements should only be made to pay for the Authority’s related expenditures.

Condition:

The Northern District Sewage Treatment Plant project is financially supported by the Department of Public Works (DPW). However, GWA’s engineering department is in charge of the construction. At the end of the project, it will be turned over to GWA.

Consequently, the Authority paid a vendor for an expenditure not directly charged to the Authority, which was already paid by DPW.

<u>Vendor #</u>	<u>Amount Paid</u>
20726	\$ 164,880

Cause:

The Authority was advised to make payment to ensure continuation of the project.

Effect:

There is no known effect to the financial statements as the Authority had already recorded a receivable from the vendor. However, there appears to be lack of internal control procedures over ensuring that processed disbursements are legitimate.

Recommendation:

The management should ensure that disbursements are processed specifically for Authority’s related expenditures.

Auditee Response:

This finding should be removed. This is a project that GWA needs to complete in order for its wastewater systems to function. DPW agreed to allow GWA to utilize their funding source, but if their funding source was not available, GWA would need to fund the project using its own funds. There is no inappropriate expenditure here.

Auditor’s Response:

At issue is that the vendor was paid twice, once by DPW and once by GWA. Hence, a receivable exists that should be repaid.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-15 – Redundant AS/400 Users

Criteria:

AS/400 system users should be audited to determine if users are still employed and/or require access to the system.

Condition:

GWA has not performed procedures to delete system users who are no longer employed.

Cause:

There appears to be a weakness in controls relating to the addition and deletion of users of the AS/400 system.

Effect:

Inappropriate access to the system from users no longer employed with GWA results from this condition.

Recommendation:

User's names that are no longer employed with GWA should be removed from AS/400 authorized user list.

Auditee Response:

GWA has changed its employee clearance procedure to ensure that user IDs are deleted as an employee processes out of the agency.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-16 – System Values

Criteria:

System values that control security on the AS400 systems should be established at the proper settings.

Condition:

Current settings create weakness in system controls.

Cause:

Incorrect settings increase the risk of unauthorized system access.

Effect:

The condition may result in unauthorized access

Recommendation:

System Value (Usage and Implication)	Current Setting	Recommended Setting	Management Response
QINACTITV Specifies, in minutes, how long the system allows a job to be inactive before taking action.	120	30	Value changed to 30 as recommended.
QLMTDEVSSN Determines if a user can have more than one device session occurring at one time. Accessing the same account from more than one terminal indicates that more than one user uses the account. This might lead to accountability issues.	0	1	Change pending interface for multiple 3rd party software issues (kronos, JDE, DMR) and group discussion in preparation for system value change.
QDSCJOBITV Specifies if and when the system ends a disconnected job.	120	30	Value changed to 30 as recommended.
QLMTSECOFR Limits the security officer to one device.	0	1	Security functions performed by one person which still requires more than one device in order to perform functions outside of normal working hours and separate locations.
QMAXSIGN Assigns the number of user signon attempts before the system takes action.	10	3	Value changed to 3 as recommended.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-16 – System Values, Continued

Recommendation, Continued:

System Value (Usage and Implication)	Current Setting	Recommended Setting	Management Response
QMAXSGNACN  Action the system takes when the maximum number of signon attempts is exhausted.	2	3	Change pending evaluation of user performance due to password expiration from 120 to 30.
QPWDEXPITV  Specifies the amount of time (in days) users must change their password	120	30	Value changed to 30 as recommended.
QPWDMINLEN  Specifies the minimum length a password must be	4	6	Value changed to 6 as recommended.
QPWDMAXLEN  Specifies the max length the password can be	8	10	Value changed to 10 as recommended.
QPWDRQDDGT  Specifies a required digit within the user's password.	0	1	Value changed to 1 as recommended.

Auditee Response:

GWA is grateful for the input in this finding. Some of the recommended changes have been implemented. Others are currently being evaluated for their impact on existing processes.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-17 – Proper User Class Settings

Criteria:

Proper User Class Settings must be properly set to restrict users from changing initial menus and assigning new special authorities.

Condition:

GWA has not correctly set initial menus and limited capabilities correctly for users in the User Class.

Cause:

Improper Initial Menu Settings and Limited Capability settings for users within the \*USER class can allow talented users to change system values without the consent of System Administrators.

Effect:

The condition may result in unauthorized system value changes.

Recommendation:

The following settings are needed to prevent users within the \*USER Class from changing system values:

User Class	Proper Initial Menu Setting	Proper Limited Capability Setting	Management Response
*USER	*SIGNOFF	*YES	Review of all profiles with *user class will be reviewed and Changes to be made as recommended.

We recommend changing the \*USER Class Initial Menu Setting to \*SIGNOFF to force the user to sign-off the system after use. For the \*SIGNOFF Initial Menu to mitigate the risk of users changing system values, the Limited Capability setting must be set to \*YES for all users.

Auditee Response:

GWA is grateful for the input in this finding. GWA believes this recommendation will be implemented in the immediate future.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-18 – User Class Special Authorities and Limited Capabilities

Criteria:

Proper settings of the AS/400 Special Authorities and Limited Capabilities are used for segregation of duties within the operating system.

Condition:

Some settings were inappropriately set.

Cause:

Inappropriate assignment of Special Authorities and Limited Capabilities can create risk due to the lack of segregation of duties within the AS/400 System. Certain User Classes have inappropriate system settings.

Effect:

Weak segregation of duties and inappropriate special authorities within the system increases the risk of unauthorized system changes.

Recommendation:

Special Authorities:

User Class	Current Special Authority Setting	Recommended Special Authority Setting	Management Response
*PGMR	*ALLOBJ, *JOBCTL, *SPLCTL, *SAVSYS, *SECADM, *SPLCTL, *IOSYSCFG	Remove: *ALLOBJ, *SECADM, *JOBCTL	Value to be changed to recommended.
*SYSOPR	*ALLOBJ, *IOSYSCFG, *JOBCTL, *SAVSYS, *SPLCTL	Remove: *ALLOBJ	Value to be changed to recommended.
*USER	*NONE, *JOBCTL, *SPLCTL, *SAVSYS	Remove: *JOBCTL, *SPLCTL, *SAVSYS	Value to be changed to recommended.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-18 – User Class Special Authorities and Limited Capabilities, Continued

Recommendation, Continued:

Limited Capability

User Class	Current Limited Capability Setting	Recommended Capability Setting	Management Response
*PGMR	*NO	*PARTIAL	Value to be changed to recommended.
*SYSOPR	*NO	*PARTIAL	Value to be changed to recommended.
*USER	*YES, *NO, & *PARTIAL	*YES	Value to be changed to recommended.

We recommend setting Special Authorities to the above settings to reduce the risk of unauthorized system changes.

Auditee Response:

GWA is grateful for the input in this finding. GWA is currently evaluating the impact of implementing this finding.

**GUAM WATERWORKS AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding Number 2004-19 – Accounts Payable: Delayed Resolution of Disputed Charges

Criteria:

Disputed charges should be addressed in a timely manner.

Condition:

Of twenty-two accounts tested, one had long standing disputed charges because of overcharging, unapproved job order, etc. The disputes dated to prior years. Currently, the Authority has not addressed the disputed charges.

Vendor #	Disputed Amount
17953	\$ 66,015

Cause:

The Authority did not follow up or address the dispute in a timely manner.

Effect:

Expenditures may be misstated due to the absence of adjustments to disputed charges. This condition could result in an overstatement of expenditures as the Authority may pay more than what has been actually incurred.

Recommendation:

The Authority should ensure disputes are adequately addressed in a timely manner to prevent overpayment of vendors and an overstatement of expenditures.

Auditee Response:

GWA has a lot of these types of issues and is slowly addressing them.