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August 31, 2004

CONFIDENTIAL

Mr. David Craddick
General Manager
Guam Waterworks Authority:

Dear Mr. Craddick:

In planning and performing our audit of the financial statements Guam Waterworks Authority (GWA) for the year ended September 30, 2003, on which we have issued our report dated August 31, 2004, we developed the following recommendations concerning matters related to its internal control. Our recommendations are summarized below:

Finding Number 1 – Safeguarding of Assets

Criteria:

Proper safeguarding of assets is necessary to circumvent the possibility of theft.

Condition:

While examining physical existence of certain general plant assets, we noted that a Tiyan storage facility was secured; however, keys for the building were kept in the front mailbox.

Cause:

There appears to be lack of protocol in securing assets.

Effect:

Lack of safeguarding fixed assets may lead to unnecessary losses.

Recommendation:

The Authority should ensure that all items are properly secured to avoid possible losses from theft.

Mr. David Craddick
General Manager
Guam Waterworks Authority
August 31, 2004

Page 2

Finding Number 2 – Promissory Notes

Criteria:

Promissory note account balances should accurately reflect customer activity.

Condition:

The September 30, 2003 promissory note balance included approximately \$122,000 in “missing deposits” within the account.

Cause:

There appears to be a lack of internal control over recording activity within this account.

Effect:

Errors in posting payments will lead to an overstatement of receivables. Inclusion of non-promissory note balances will also overstate this receivable balance. Moreover, as payments may be received and not posted, there is the possibility of misallocation of monies received.

Recommendation:

GWA should ensure all payments received are accurately reflected in the proper customer accounts.

Finding Number 3 – Recovered Revenue

Criteria:

Accounts receivable balances assigned to collection agencies should be properly tracked and reconciled.

Condition:

Cash remitted from collection agencies was not appropriately classified as recovered revenue. Moreover, as some of the balances were previously subject to a provision for doubtful accounts, corresponding amounts should be removed from the allowance for accounts receivable.

Cause:

There has been no clear assignment of duties and procedures with respect to the accounting treatment of recovered revenue.

Effect:

As a result of this condition, recovered revenue may be understated and the allowance for doubtful accounts may be overstated.

Recommendation:

The Authority should establish and implement procedure with respect to the recording and reconciliation of recovered revenue.

Mr. David Craddick
General Manager
Guam Waterworks Authority
August 31, 2004

Page 3

Finding Number 4 – Fixed Assets Maintenance

Criteria:

The acquisition of fixed assets should be with the understanding that the asset will perform the necessary functions for a reasonable time period after acquired.

Condition:

The following asset, identified in prior year as not being fully utilized, should be evaluated for impairment:

Asset #	Description	Year	Bus Unit	Cost	NBV at 9/30/03
109031	Truck Mounted Mobile Indust	2001	530	\$ 179,779.00	\$ 104,871

The item is just over three years old and has had repairs for both its vacuum and high-velocity functions. As a result, its normal functions have been outsourced to third parties. The top three vendors providing these types of services resulted in the following amounts of rental expense:

Vendor Number	Amount
15085	\$ 79,875
20268	164,875
17953	384,351

Cause:

The cause appears to be poor communication between departments to fully anticipate needs.

Effect:

As a result of this condition, assets may not be fully utilized. Because the damaged assets may be replaced years before the end of their useful life or because their related job-functions must be outsourced, cash outflow increases unnecessarily.

Recommendation:

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

Finding Number 5 – Accrued Expenses

Criteria:

Efforts should be made to ensure proper reversal of periodic expense accruals on a regular basis.

Condition:

Per review of accrued expenses, it was noted that reversal of accrued payroll expense of \$155,404 was not performed on a timely basis.

Mr. David Craddick
General Manager
Guam Waterworks Authority
August 31, 2004

Page 4

Finding Number 5 – Accrued Expenses, Continued

Cause:

There appears to be shortage of accounting manpower to adequately address systematic accruals and reversals.

Effect:

Liabilities at September 30, 2003 were overstated prior to the proposal of current year audit adjustments.

Recommendation:

The Authority should train and assign staff to properly accrue and reverse accruals on a regular basis.

Finding Number 6 – Salaries and Wages

Criteria:

The payment of employee salaries should be consistent with the policies of the Authority and in compliance with Government of Guam law.

Condition:

In our examination of other receivables, we discovered an employee with an outstanding payable to the Authority of approximately \$18,000. Current repayment terms are based on a \$72/pay period deduction (\$1,872 per year) with the amount to be fully paid by June 2013.

Cause:

This condition originally arose due to an error in the payment of accrued annual leave.

Effect:

There is no known material effect on the financial statements. However the underlying accounting balances may be questioned.

Recommendation:

GWA should ensure procedures are in place to identify employees that have agreed to decreased workweeks and ensure that the hours paid are consistent with Guam Public Law. All documentation related to shortened workweeks or other employment circumstances should be properly filed and safeguarded.

Finding Number 7 – Prior Period Adjustments

Criteria:

The Authority recorded certain adjustments at the beginning of the fiscal year that relate to prior periods.

Mr. David Craddick
General Manager
Guam Waterworks Authority
August 31, 2004

Page 5

Finding Number 7 – Prior Period Adjustments, Continued

Condition:

Approximately \$2 million in activity was improperly recorded against the beginning net assets prior to the proposal of current year audit adjustments.

Cause:

To better match activity, Accounting recorded items in the prior period.

Effect:

Because these adjustments were recorded directly to the prior period, it appears that management has been using internal financial information that differs materially from the audited financial statements.

Recommendation:

Management should work with outside vendors and customers to capture activity within the proper period. Management should further determine an expectation of normal activity to properly estimate items that may be received late.

Finding Number 8 – Budget Transfers

Criteria:

The Authority should adhere to the procedures in place with respect to budget transfers as mandated by the Guam Legislature and later adopted by the Consolidated Commission on Utilities (CCU).

Condition:

For the first quarter of fiscal year 2003, budget transfers were performed with the express authority from the Legislature. Budget authority was transferred to the CCU in January 2003. During fiscal year 2003, while the Authority was able to work within its allotted budget in total, the individual departments were out of balance.

Cause:

The cause appears to be a lack of oversight by management to properly document and record approved transfers.

Effect:

With the lack of a tracking mechanism in place with respect to budget movement, the Authority is more likely to operate beyond its means.

Recommendation:

The Authority should adhere to transfer procedures, requiring approval for transfers from the CCU and maintain a history of this activity.

Mr. David Craddick
General Manager
Guam Waterworks Authority
August 31, 2004

Page 6

Finding Number 9 – Disbursement Processing

Criteria:

Disbursements should be adequately supported by vendor invoices and have supervisor approval.

Condition:

Among rental equipment invoices tested, eight invoices were manually corrected by the accounts payable clerk based on time reported on trouble reports, amounting to overpayments as follows:

Invoice No.	Amount Billed	Amount Paid	Overpayment
21655	\$ 3,130	\$ 3,400	\$ 270
21613	6,975	6,995	20
21645	4,570	4,590	20
21649a,b	3,220	3,240	20
21656	5,200	5,220	20
21561a,b,c	1,910	1,920	10
21677	5,800	5,820	20
21690	8,100	8,130	30
		Total	\$ <u>410</u>

Cause:

Changes were made to invoices based on time reported on trouble reports to recognize appropriate amounts of expense.

Effect:

While there is no known material effect on the financial statements resulting from this condition, with changes being made to invoices already certified by vendor, there is a greater likelihood of potential issues with misappropriated assets.

Recommendation:

Should a billing error be encountered, a request for amended invoice should be made so that transactions are appropriately documented.

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This report is intended solely for the information and use of Board of Directors and management of Guam Waterworks Authority.

We wish to express our appreciation for the cooperation of the staff and management of GWA during the course of our audit. We would be available to discuss any questions that you may have concerning the above comments at your convenience.

Very truly yours,

