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April 23, 2009

Consolidated Commission on Utilities (CCU)

In planning and performing our audit of the financial statements of the Guam Waterworks Authority (GWA) as of and for the year ended September 30, 2008 (on which we have issued our report dated April 23, 2009), 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 the GWA'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 the GWA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the GWA'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 the GWA's internal control over financial reporting and other matters as of September 30, 2008 that we wish to bring to your attention.

We have also issued a separate report to the management, also dated April 23, 2009, on our consideration of the GWA'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 Consolidated Commission on Utilities, the management of Guam Waterworks Authority and the Office of the Public Auditor of Guam 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 GWA for their cooperation and assistance during the course of this engagement.

Very truly yours,

Deloitte & Touche LLP

APPENDIX I

SECTION I – CONTROL DEFICIENCIES

We identified no control deficiencies involving the GWA's internal control over financial reporting as of September 30, 2008.

SECTION II – OTHER MATTERS

We identified, and have included below, other matters involving the GWA's internal control over financial reporting as of September 30, 2008 that we wish to bring to your attention:

Finding Number 1 - Promissory Note

Comment: A negotiation was initiated with customer # W0800006 to settle an outstanding account. However, no promissory note was formalized. This may create exposure to the Authority and may increase the likelihood of disputes and disagreements.

Recommendation: All promissory notes should be formally documented and be duly executed. Documentation should include settlement amounts, terms, date of settlement and authorization of both parties accepting the final settlement.

Finding Number 2 - Proper Valuation of Final Inventory Listing

Comment: Per examination of the final inventory listing, we noted the following:

1. Inventory items were over recorded

Description	Quantity	Cost
Valve Gate FX – FX 8"	1	$ 820
Valve Gate MJ – FX to FX 6"	3	$ 5,940

2. Inventory item was under recorded

Description	Quantity	Cost
Uni Flange 3"	30	$ 1,350

Recommendation: We recommend that review procedures be implemented to ensure that all transferred count sheets are reviewed. Such procedures would include reviewers initialing sheets checked and another supervisor randomly inspecting sheets to ascertain whether actual counts have been transferred to the final inventory listing.

Finding Number 3 - Inefficiencies in Physical Count

Comment: We were scheduled to complete our inventory observation at the location on September 28, 2008. However, the Authority was not able to finalize counts as scheduled. The cause of the delay was due to a combination of problems relating to the inventory count procedures as noted below:

Finding Number 3 - Inefficiencies in Physical Count, Continued

1. Segregation of Inventory Items

   The entire case goods inventory is generally stacked in an organized manner. However, we noticed that different inventory items were comingled during the count. Since the Authority did not segregate inventory items, it became very time consuming to perform the count. In fact, the Authority omitted or miscounted certain inventory in their initial counts and had to recount several times to ensure an accurate count.

2. Lack of Tag Control

   The Authority utilized tag control in counting inventory. However, inventories counted in other locations were recorded on scratch paper. As there are multiple personnel involved, the Authority runs the risk of omitting or double counting inventories, which was evident by the need to perform the recount.

3. Personnel and Time Management

   Due to the counter not being familiar with inventory items and the lack of advance preparation, the Authority was not able to complete inventory counts and reconciliations by the scheduled time. The length of time and manpower required to complete the inventory count was significantly more than necessary.

Recommendation: We recommend the following to avoid the matters noted above:

1) Segregate inventory items
2) Implement tag control
3) Ensure employees participating in the counts are familiar with the inventories
4) Schedule the count to start in advance and allow a realistic amount of time to complete both the inventory count and the reconciliation process.

Finding Number 4 - Inventoried Capitalized Items

Comment: The following capitalized items were not correctly reflected in the final item listing. However, the exceptions have no effect on the financial statements.

1. Item not properly recorded in the final listing

Description	Final Count	Actual Count	Difference
Coupling 2” FIP	865	864	1

2. Item not included in the final listing

Description	Final Count	Actual Count	Difference
Coupling 1” CTS PJ x ¾”	0	1,300	1,300

Recommendation: We recommend correctly recording capitalized items counted.

Finding Number 5 – Asset Dispositions

Comment: A 1 million gallon water tank was demolished and disposed of during the year. However, the asset and related amortization has not been removed from the general ledger account.

Recommendation: We recommend that the Authority perform a physical inventory of capital assets. As part of this inventory, all capital assets should be assigned an identification number and be tagged. The related detailed accounting records should be adjusted for the results of these procedures. Both cost and accumulated amortization should be removed from the general ledger upon disposal.

Finding Number 6 – Allowance for Inventory Obsolescence

Comment: The Authority could not provide the basis for its estimation of the inventory allowance as of September 30, 2008.

Recommendation: The Authority should document the basis of its obsolescence reserve.

Finding Number 7 – Recording of Transactions in Proper Period

Comment: One invoice of $14,120 from vendor # 22121 was not recorded in the correct period.

Recommendation: Liabilities should be recognized upon receipt of goods or services.

Finding Number 8 – Timesheet Approval

Comment: The January 5, 2008 time sheet for employee #714 did not contain the required sign-offs of the supervisor or department head.

Recommendation: Supervisors and department heads should be reminded that their approval should be annotated on employee timesheets prior to submission to the payroll department.

Finding Number 9 – Delay in Processing of Terminated/Resigned Employee

Comment: For one of fifty samples tested, the paperwork clearance for employee #603 was not processed in a timely manner.

Recommendation: Prior to the employee departure, the Authority should obtain completed clearance forms and timely submit to human resources for processing.

Finding Number 10 – Customer Refunds

Comment: Certain customer accounts appear to have resulted in overpayments which resulted in an increase of customer credit balances of $80,991 during the year. However, the customer credits were not refunded on a timely basis.

Recommendation: The Authority should ensure that customer overpayments are timely refunded.

Finding Number 11 – Non-Registering Meter

Comment: In six of one hundred fifty transactions tested, the meter did not register water consumption.

Recommendation: 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 most likely causes a substantial percentage of the abnormal readings.

Finding Number 12 – Exception in Meter Readings

Comment: In sixteen of one hundred fifty (10%) transactions tested, the estimated readings, which are based on a 6-month average billing, if available or the previous month's billing, were not adjusted to reflect actual readings.

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 is already addressing the concern of defective, non-registering meters, which most likely causes a substantial percentage of abnormal readings.

Finding Number 13 – Erroneous Use of Water Rate

Comment: Of one hundred fifty revenue accounts examined, one account was charged an old rate for the current estimated bill and one account was charged a current rate for back billed charges.

Recommendation: We recommend that the Authority apply applicable water rates to billings.

Finding Number 14 – Processing Job Order

Comment: In one of one hundred fifty revenue accounts examined, bills were sent four months after contract termination, and in one account, GWA back billed pending charges from August 2004 to March 2005 which resulted from an unprocessed job order.

Recommendation: The Authority should weigh the benefit of reducing the likely misstatement of revenue against the cost of paying additional people to process pending job requests.

Finding Number 15 – Bid Invitation/Price Solicitation With No Response

Comment: For two of forty-four procurement transactions examined, the buyer did not follow up or contact the nonresponsive bidders or vendors. Therefore, there was no assurance that the vendor actually received the solicitation.

Recommendation: We recommend that the Authority contact non-responsive bidders or solicited vendors and document such procedure in file to provide documentation that bidders were provided an opportunity to respond prior to the awarding of the bid, contract, or purchase order.

Finding Number 16 – Percentage Completion of Construction in Progress

Comment: The Authority could not provide the percentage of completion of certain projects carried in construction in progress (CIP).

Recommendation: The Authority should ensure that the responsible department maintains and updates the percentage of completion schedule on a timely basis.

Finding Number 17 - Reconciliation of Account Balance With Collection Agency

Comment: The collection agency remits collected amounts to GWA. The remitted amount is verified and is applied to respective customer accounts. However, GWA does not perform a reconciliation of the ending account balance, which resulted in an unremitted amount of $7,964 to GWA.

Recommendation: GWA should perform regular reconciliation of the collection agency's account balance to ensure that collected amounts are appropriately remitted to GWA. Discrepancies noted should be addressed in a timely manner.

Finding Number 18 – Bid Security

Comment: Under certain conditions, a bid security may be required on bids exceeding a certain value and must accompany a bid as a part of, among other requirements, a bid or proposal package. Depending on the form of the bid security, the security maybe deposited in GWA's bank account. In the last quarter of fiscal year 2008, the security is now secured in a safe deposit box at GWA. Unsuccessful bidders are entitled to the return of their bid deposit upon the award of the procurement. In one instance, we noted no reasonable attempt was made to notify an unsuccessful bidder and the delay resulted in the untimely refund of a bid security.

Recommendation: GWA should develop procedures for receiving, depositing, and refunding of bid securities and proper notice is given to appropriate departments upon conclusion of a procurement to ensure timely refund of bid securities.

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

GWA'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.