



OFFICE OF THE PUBLIC AUDITOR

**Guam Waterworks Authority
Fiscal Year 2006 Financial Highlights**

May 25, 2007

After closing its books with positive net assets of \$1.5 million in 2005, Guam Waterworks Authority (GWA) posted an \$8.1 million decrease in net assets in 2006.

In January 2006, GWA issued a \$101,175,000 bond for the purpose of funding capital improvements to GWA's water and wastewater systems, refinancing certain outstanding obligations of GWA, and financing new water meters. Though GWA's bond ratings of Ba2 from Moody's Investors Service, Inc. and BB rating from Fitch, Inc. is not of investment grade, it is GWA's first time to receive a rating from a nationally recognized credit rating agency and borrow from the financial markets. The bond indenture agreements require the establishment of special funds to be held and administered by trustees and GWA. Proceeds from borrowings to fund capital improvements are maintained in construction accounts, which are required by loan agreement or public law to be used for capital improvements. At September 30, 2006, \$67.9 million is held by GWA in the construction fund. Construction work in progress was \$26.7 million at the end of 2006.

All gross revenues of GWA have been pledged to repay the bond principal and interest. Principal and mandatory sinking fund payments will commence with a \$1,865,000 payment in July 2008 and will variably increase to \$6,810,000 in July 2035. The bond matures on July 1, 2035.

Operating revenues decreased by \$855,866 from \$42.3 million in 2005 to \$41.4 million in 2006, while total operating and maintenance expenses increased by \$5.4 million from \$42.7 million in 2005 to \$48 million in 2006. The loss of \$9.2 million was offset by \$1.1 million in capital contributions: \$849,207 in grants from the United States Government; and \$300,000 from the government of Guam. The \$8.1 million decrease in net assets in 2006 was due to several factors to include:

- Increase in salaries and wages from \$11.6 million in 2005 to \$14.5 million in 2006. This increase is the largest contributing factor in the increase in operating and maintenance expenses. Although the net change in GWA personnel was only 10,¹ the increase in salaries and wages is largely due to a \$1.6 million adjustment in fiscal year 2005 pension costs and the hiring of new employees and replacement of employees who have separated from GWA. As employees separate from GWA, new professionals, particularly engineers, are hired at higher salary levels. Additionally, a court-stipulated order required GWA to hire Direct Responsible Charges (DRCs) to operate the wastewater facilities. The DRCs are primarily off-island hires thereby making the recruitment-related costs relatively high;
- Increase in contractual expenses from \$2.3 million in 2005 to \$4 million in 2006 to include rental, testing, and accounting; and
- Increase in interest expense from \$353,613 in 2005 to \$5.6 million in 2006. The interest expense of \$5.6 million was partially offset by interest income of \$3.2 million earned by monies in the construction fund.

¹ GWA personnel numbered 235 in 2005 and 245 in 2006.

Additionally, the Public Utility Commission of Guam (PUC) only approved a 3% increase in rate as opposed to the 8% requested by GWA. Future rate increases will be inevitable to fund incremental increases in debt services obligations and the need for capital improvement projects to sustain and improve operations.

Although it appears that accounts receivables improved from \$9.9 million in 2005 to \$7.7 million in 2006, the reduction is due to a higher allowance for doubtful accounts. The allowance for private accounts increased from \$5.2 million in 2005 to \$8.1 million in 2006, while the allowance for government accounts increased from \$6.6 million in 2005 to \$6.9 million in 2006. A larger portion of GWA's receivables is largely from private accounts as opposed to government customers. To date, GWA continues to experience high levels of receivables. As of September 30, 2006, total receivables amount to \$22.7 million, of which \$14.5 million or 64% is 120 days and over.

GWA is mandated to provide water to fire hydrants in Guam and classifies the services as government water revenue. However, no government of Guam agency is tasked to pay for the services; therefore, GWA has historically provided for a full allowance of the billings. Fire hydrant revenue was \$755,245 in 2005, and due to a rate adjustment, significantly declined to \$259,020 in 2006. Fire hydrant receivables were \$6 million in 2006 and \$5.8 million in 2005. GWA is currently in communication with PUC as to the billing of such services.

The Independent Auditors' Reports on Compliance and On Internal Control identified seven findings, of which two are repeat findings. Of the seven findings, the auditors noted three reportable conditions involving areas of cash management, procurement, and reporting. Reportable conditions are defined as matters "relating to significant deficiencies in the design or operation of the internal control over compliance ... that could adversely affect the Authority's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants." This year, questioned costs amount to \$330,931 compared to \$115,000 in 2005. Total unresolved questioned costs at the end of 2006 were \$445,931.

Other findings include not performing independent checks and reviews for adherence to Federal compliance requirements and Standard Operating Procedures. The auditors also found that procedures were not performed and adequate documentation was not maintained to comply with procurement regulations. GWA persistently procures in the \$14,000 range, which is just below the \$15,000 threshold that would require advertisement and competitive bidding. The auditors noted the absence of supporting documentations and the awards of blanket purchase agreements after soliciting from only one vendor.

OPA received a Hotline tip concerning the amounts expended at Consolidated Commission on Utilities (CCU)² meetings. The CCU Board is the only paid Board in the government of Guam where members are provided with a monthly stipend of \$1,000, equally paid for by GPA and GWA. GWA expenditures for board meetings were \$6,159 in 2006 as opposed to \$967 in 2005.

For a detailed commentary of GWA's operations, see the Management Discussion and Analysis portion of the audit report.

² The governing body for GPA and GWA.