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September 9, 2013

Ms. Benita Manglona
Director
Department of Administration
Government of Guam
P.O. Box 884
Hagatna, GU 96910

Dear Ms. Manglona:

In planning and performing our audit of the financial statements of the Solid Waste Fund and of those funds related to the Government of Guam Limited Obligation (Section 30) Bonds, 2009 Series A (Solid Waste Funds or the Funds) as of and for the year ended September 30, 2012 (on which we have issued our report dated September 9, 2013), 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 Funds' 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 Funds' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Funds' 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 Funds' internal control over financial reporting and other matters as of September 30, 2012 that we wish to bring to your attention.

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.

The Funds' responses to the deficiencies identified in our audit are set forth in the attached Appendix I. We did not audit the Funds' responses, and accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of the Solid Waste Funds' management, others within the organization and the Office of Public Accountability – 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 the Solid Waste Operations Fund for their cooperation and assistance during the course of this engagement.

Very truly yours,

SECTION I – DEFICIENCIES

We identified, and have included below, deficiencies involving the Solid Waste Funds’ internal control over financial reporting as of September 30, 2012 that we wish to bring to your attention:

1. Allowance for Doubtful Accounts

A formal policy for the recognition of the allowance for doubtful accounts is not currently in place.

We recommend that a formal policy relative to the recognition of an allowance for doubtful accounts be established.

Auditee Response: GSWA management concurs.

2. Encumbrances

During tests of encumbrances, the following were noted:

- a. Of five encumbrances aggregating \$938,669 tested under Fund 416, all were expired or invalid as of September 30, 2012. An audit reclassification was proposed to decrease the reserve.
- b. Twenty two encumbrances aggregating \$5,316,138 under the Capital Project Fund related to operations. An audit reclassification was proposed to transfer these encumbrances from Capital Projects Fund to Operations Fund.
- c. Of seven encumbrances aggregating \$9,363,903 under Fund 254 as of September 30, 2012, five items did not agree to audit expectations by \$2,536,616 either due to expired or invalid items. An audit reclassification was proposed to correct the reserve.
- d. Encumbrances associated with two contracts were understated by \$27,678,910. An audit reclassification was proposed to correct the reserve.

<u>Contract#</u>	<u>Particulars</u>	<u>Understatement</u>
C110601722	Waste hauling services	\$ 13,320,506
C110601741	Landfill operations	<u>14,358,404</u>
		<u>\$ 27,678,910</u>

We recommend that encumbrances be approved and reviewed for ongoing pertinence. Further, we recommend that reserves be recorded based on contract amounts.

Auditee Response:

- a. DOA will coordinate with Guam Solid Waste Authority to identify which encumbrances are no longer active and will liquidate which will decrease reserve.
- b. DOA will de-encumber all encumbrances from Capital fund account and re-encumber accordingly to created accounts for all operation vendors.
- c. DOA will coordinate with Guam Solid Waste Authority and Receiver to submit all amendments on existing contracts or purchase orders timely to avoid direct recording of expenditures to appropriation account instead of encumbrances.

SECTION I – DEFICIENCIES, CONTINUED

2. Encumbrances, Continued

- d. Corrective measures are made for FY2013 to increase encumbrances for both waste hauling services and Landfill operation contracts for the duration of contract time.

3. Other Revenue Transactions

GSWA prepares a monthly report of billings and collections and provides that to the Department of Administration (DOA). During fiscal year 2012, DOA utilized this report to record revenue transactions. However, certain revenue related transactions (i.e. credits applied to customers' accounts, discounts, payment reversal and invoice reversals) posted to the billing system were not captured in the monthly revenue report, and as such were not recorded in the general ledger.

Since the billing system is currently not interfaced to the general ledger, we recommend that other revenue related transactions be summarized and provided to DOA for recording to the general ledger.

Auditee Response: GSWA management concurs. GSWA will begin incorporating credits, payment reversal and invoice reversals into the monthly revenue report.

4. Payroll Expenditures

Of five employees tested, the overtime work authorization for one employee (employee #3892 for overtime hours from 10/10/11 thru 10/14/11) was not signed by the Administrator.

We recommend that approval of overtime work authorization be documented.

Auditee Response: GSWA management concurs. It is the policy of GSWA to maintain the report. The report in question was misplaced. New procedures have been put into place to assure that these reports are properly maintained.

SECTION II – 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

Management is responsible for the overall accuracy of the financial statements and their conformity with accounting principles used to prepare the financial statements. 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 accounting principles used to prepare the financial statements).

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.