



EXECUTIVE SUMMARY
Government of Guam Use Tax on Air Cargo
OPA Report No. 20-01, January 2020

Our audit of the Government of Guam's (GovGuam) Use Tax data and processes from October 1, 2016 through December 31, 2018 found significant flaws and deficiencies in its processes, which were due to the inadequate oversight, monitoring, and coordination among its key players—Customs and Quarantine Agency (CQA), Department of Revenue and Taxation (DRT), and Department of Administration (DOA). In Calendar Year (CY) 2018, CQA's Air Cargo Operations received incoming cargoes worth \$1.6 billion (B). Without considering all exemptible cargoes, the 4% Use Tax rate, if collected upfront, could provide GovGuam approximately \$65.5 million (M) of Use Tax revenues. However, based on existing laws and CQA's professional judgement, GovGuam only collected \$136 thousand (K) (or 0.2%) from air cargo in CY 2018.

Manual Recording and Assessment of Incoming Air Cargo Prone to Errors

In CY 2018, CQA's Air Cargo Operations received and manually processed \$1.6 billion (B) worth of incoming cargoes. Our audit sample found errors, such as: (1) incoming cargoes not found in the E-Log records, (2) Master Airway Bill (MAWB) numbers off by one number, (3) assessment of cargoes 10 days after arrival, and (4) air cargo information inputted into the E-Log after its assessment. Without an effective system in place (preferably an electronic system) to collect, track, and record quantities and values of incoming air cargoes, CQA is exposed to risks of unaccounted, unrecorded, and unassessed incoming cargoes.

DRT Backlog in Processing Use Tax Forms Due to Non-Prioritization

As of February 2019, DRT received 16,777 Use Tax Forms from CQA for Use Taxes assessed, but not paid from Fiscal Year (FY) 2017 to FY 2018, of which 13,603 (or 81%) were not processed. The processing backlog was due to the lack of staff needed to process Use Taxes as DRT prioritizes processing and collecting other taxes such as Business Privilege Tax and Tobacco Tax. Consequently, DRT could not determine the Use Tax amount due from taxpayers and thus, cannot effectively pursue collection. If conditions persist, DRT risks its authority and ability to collect unpaid taxes due to the limiting provisions on the statute of limitations.

True Value of Use Taxes Assessed, Collected, and Receivables Unknown

Inability to Interface CQA and DRT's Systems Resulted in Unrecorded Receivables

DOA's AS400 reflected a Use Tax receivable of \$435K in FY 2018, a \$91K decrease from \$526K in FY 2017. The decrease from FY 2017 through FY 2018 may appear that collections have improved, however, Use Tax receivables were not booked by DOA or DRT since FY 2016. In comparison with CQA's Use Tax charge of \$1.6M, there is an undetermined amount of Use Taxes owed (receivable) due to DRT's backlog in processing of Use Tax Forms and the lack of interface of Use Tax data in DRT's AS400 System and CQA's Transaction Processing System (TPS). As of this report date, DRT and DOA have not established the true amount of Use Tax Receivable that should be recorded and consolidated in the GovGuam Financial Statements.

Use Tax Assessment Forms Not Pre-Numbered

CQA Use Tax Assessment Forms are not pre-numbered and thus could not be controlled and accounted for. Pre-numbered forms help to ensure that transactions are recorded and accounted for. As a result, the true amount of Use Tax revenues and receivables cannot be determined.

Discrepancies in Use Tax Assessment Data per CQA versus DRT

For FY 2017, CQA reported total Use Tax assessments of \$1.8M while DRT's record showed total assessments of \$1.4M, or a difference of \$417K. The discrepancy could be due to 5,608 unprocessed Use Tax Charge Forms as of February 2019.

Lack of Communication of Use Tax Payments

The CQA Administrative Clerk III accepted Use Tax payments up to 68 days, which is significantly beyond the seven-day grace period after assessment. Payments were accepted without validating against the original copies of the Use Tax Charge Form, issuing an official receipt, and communicating with DRT. Due to the lack of communication with DRT, Use Taxes owed could be overstated as TPS-recorded payments are not interfaced with DRT.

No Record of Use Tax Exemptions and Post-Supervisory Reviews

Although CQA has records of the incoming air cargoes, it has insufficient records to document how much of the daily total incoming cargoes were exempt from Use Tax. For August 2018, CQA's Use Tax Charge records showed 206 MAWBs with Use Tax assessments of \$75K for goods valued at \$1.9M. Only \$2.1M of the \$197.9M of incoming goods (or 1%) was assessed Use Taxes, resulting in about \$195.8M (or 99%) of cargoes exempt or not assessed for Use Tax. Although these cargoes could be exempt or non-exempt based on guidelines, this could not be determined due to insufficient records.

Manual to No-Tracking of Personal Exemptions

Since Use Tax assessments are dependent upon each CQA officer's professional judgment, personal exemptions could be manually tracked or not at all. CQA's Standard Operating Procedure does not outline a process on how to track or monitor the \$1,000 per month or \$5,000 per year of personal exemptions granted, nor does it define a threshold that should be considered in assessing Use Taxes. Without an electronic tracking system in place, the excess over exemptible amounts per taxpayer is difficult to determine.

CQA is currently in the process of procuring a Customs Management Information System (CMIS) that has various capabilities, including: receiving all AWBs and manifests electronically, automated assessments of Use Tax, tracking of exemptions, and more. CQA Management needs to aggressively pursue the acquisition of a CMIS (with appropriate funding) to minimize, if not eliminate, manual processes that may waste resources due to inefficient processes and solve all other relevant issues which deprive GovGuam of its true Use Tax revenue.

Lack of Independent Verification of Collections by DOA

For FY 2017, DOA reported total TPS collections of \$129K in contrast to CQA's recorded \$130K, or a difference of about \$1K. Our testing found three reported payments totaling \$8K without supporting documents, which further raises concerns on the completeness of remittances to the Treasurer of Guam (TOG). CQA Management should consider further investigating these matters as it increases the risk for potential fraud. We also learned that the total Use Tax collections

received by TOG per Depositor's Form were not verified against the total per TPS. Without an independent verification by DOA, there is a high probability of short or delayed deposits of Use Tax collections.

Conclusion and Recommendations

We commend CQA for its diligence in performing its primary task of inspecting incoming cargoes and assessing Use Taxes daily on the front end. However, GovGuam's Use Tax data and processes need significant improvements, especially in the automation of incoming air cargoes; recording of assessment, exemption, and collection; and the interface of Use Tax data. With the current manual processes, the voluminous and substantial value of incoming domestic and foreign goods could increase the risk of revenue leakage in Use Tax and other taxes resulting from escaped or incorrect assessments. Therefore, GovGuam needs to move towards the automation of these Use Tax processes and establish an efficient accounting infrastructure that could interface Use Tax data and information in CQA and DRT's systems. We recommend the following:

- **DRT Management:**
 - (1) Provide sufficient resources to prioritize processing of Use Tax Forms and reduce backlog.
 - (2) Meet with CQA on issues regarding taxpayer's information on Use Tax Assessment Forms.
 - (3) Provide updated training to CQA personnel.

- **CQA Management:**
 - (4) Maintain a record of exemptions and supervisory reviews.
 - (5) Update SOP to define threshold in assessing cargoes subject to personal exemption.
 - (6) Aggressively pursue the acquisition of a CMIS.
 - (7) Strengthen internal controls on Use Tax payments, collections, and deposits to prevent potential fraud.
 - (8) Separate Use Tax collections from other fees in the Depositor's Form for accountability.

- **TOG:**
 - (9) Verify Use Tax collections against TPS records.

- **DRT, DOA, and CQA:**
 - (10) DRT coordinate with DOA to establish and book the Use Tax Receivable for consolidation in the GovGuam Financial Statements.
 - (11) Consult with the Office of Technology on the interface of CQA and DRT's systems.
 - (12) Incorporate a control numbering sequence on the Use Tax Assessed Forms.

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