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March 25, 2010

Mr. Lenard Olive
General Manager
Guam Waterworks Authority
P.O. Box 3010
Hagatna, Guam 96932

Dear Mr. Olive:

In planning and performing our audit of the financial statements of Guam Waterworks Authority (GWA) as of and for the year ended September 30, 2009 (on which we have issued our report dated March 25, 2010), 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 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 GWA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of 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 GWA's internal control over financial reporting and other matters as of September 30, 2009 that we wish to bring to your attention.

We have also issued a separate report to the Consolidated Commission on Utilities, also dated March 25, 2010, on our consideration of 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, management, others within the organization, the Office of Public Accountability – Guam, federal awarding agencies, pass-through entities, and the cognizant audit and other federal agencies 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

SECTION I – CONTROL DEFICIENCIES

We identified, and have included below, control deficiencies involving GWA's internal control over financial reporting as of September 30, 2009 that we wish to bring to your attention:

Inefficiencies in Physical Count

Comment: We noted the following exceptions during physical count observation.

1. Proper Segregation of Inventory Items

   The entire case goods inventory is generally stacked in an organized manner. However, inventory items were comingled with non-inventory items during the count. Since the Authority did not segregate non inventory items from inventory items, it became very time consuming to count the inventories. The Authority, as a result, included non-inventory items in the final inventory schedule.

2. Lack of Tag Control

   The Authority utilized tag control in counting the 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 the inventories which were evident by the number of counts that were reperformed.

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

Allowance for Inventory Obsolescence

Comment: The Authority has not established a formal methodology for establishing its inventory allowance.

Recommendation: The Authority should establish a formal basis for its obsolescence reserve.

Proper Valuation of Final Inventory Listing

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

1. Inventory item was over recorded

Description	Quantity	Cost
Valve Gate FX – FX 8"	3	$ 3
Nipple, Brass 1 1/4" x 4"	10	$ 64

2. Inventory item was under recorded

Description	Quantity	Cost
Valve, Gate FX-FX 3”	1	$ 405
2” Ball Valve	1	$ 21

3. The wrong unit cost was used for the inventory item resulting in an overstatement of $353,340. However, GWA adjusted and corrected the ending inventory balance.

Description	Quantity	Unit Cost	Amount
Coupling, PVC S/S 3/4”	2,125	$168.00	$ 357,000
Coupling, PVC S/S 3/4”	2,125	1.68	3,570
Overstatement			$ 353,340

4. Automated meter reading items are capitalized upon receipt. The capitalized item was included in the final item listing which resulted in an overstatement of inventory. However, GWA adjusted and corrected the ending inventory balance.

Description	Final Count	Cost
Valve, Check ¾”	3,714	$352,830

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

Collection Effort

Comment: In previous years, collections on written-off accounts were performed by collection agencies. Due to contract expiration, the accounts were returned to GWA. Collections are only performed on inactive accounts because of staff shortages. No collection effort is being done on the written-off accounts.

Recommendation: We recommend that written-off accounts be followed up on and collection efforts be diligently pursued.

Capitalization of Fixed Assets in Proper Period

Comment: Certain capital assets were not recorded in the correct period. This resulted in an overstatement of operating expenses and an understatement of net assets.

Recommendation: We recommend that capitalizable assets be captured in the correct period.

Non-Registering Meter

Comment: In six (8%) of seventy five 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 abnormal readings.

Recording of Transactions in Proper Period

Comment: Two invoices amounting to $68,921 from vendor #22058 were not recorded in the correct period.

Recommendation: We recommend that liabilities be captured upon receipt of goods or services in the correct period.

Bid Invitation/Price Solicitation with No Response

Comment: For seven of twenty six expenditures tested, the buyer represented that follow up or contact occurred with the nonresponsive bidders or vendors. However, there was no assurance that the vendor was actually contacted because there was no indication in the solicitation document of when the buyer contacted the vendor.

Recommendation: We recommend that the Authority document this procedure in file to ensure that vendors were provided the opportunity to respond prior to awarding of bids, contracts, or purchase orders.

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 project percentage of completion on a timely basis.

Bidding Time

Comment: In accordance with GAR section 3109 (d), a minimum 15 days of bidding time shall be provided for Invitation for Bid (IFB). For one of thirteen bids tested, IFB GWA 2009-01 did not comply with the requirement.

Recommendation: GWA should publish IFB's in a manner consistent with established policy.

Contract Agreement

Comment: The contract agreement with a collection agency expired in July 2009. The contract contains a provision to extend for an additional year if the extension is formalized in writing. GWA extended the contract for another year but no written agreement was formalized.

Recommendation: GWA should formalize the extension in writing.

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 the respective customer accounts. However, GWA does not perform a monthly reconciliation of the ending account balance which may result in not capturing remitted amounts in GWA's books.

Recommendation: GWA should perform monthly reconciliations of the collection agency's account balance to monitor if collected amounts are appropriately remitted to GWA. In addition, discrepancies noted should be addressed in a timely manner.

SECTION II – OTHER MATTERS

We identified no other matters involving GWA's internal control over financial reporting as of September 30, 2009.

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.