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April 8, 2013

Mr. Joaquin C. Flores  
General Manager  
Guam Power Authority  
1911 Route 16  
Harmon, Guam 96913

Dear Mr. Flores:

In planning and performing our audit of the financial statements of Guam Power Authority (GPA) as of and for the year ended September 30, 2012 (on which we have issued our report dated April 8, 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 GPA'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 GPA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of GPA'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 that might be significant deficiencies or material weaknesses and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, in connection with our audit, we identified, and included in the attached Appendix I, deficiencies related to GPA's internal control over financial reporting and other matters as of September 30, 2012 that we wish to bring to your attention. We have also separately reported in a letter dated April 8, 2013 addressed to GPA's management certain deficiencies involving GPA's information technology environment.

We have also issued a separate report to the Consolidated Commission on Utilities, also dated April 8, 2013, on our consideration of GPA's internal control over financial reporting and 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 and the Federal cognizant agency and is not intended to be and should not be used by anyone other than these specified parties.

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 GPA for their cooperation and assistance during the course of this engagement.

Very truly yours,

*Deloitte & Touche LLP*

**SECTION I –DEFICIENCIES**

We identified the following deficiencies involving GPA's internal control over financial reporting as of September 30, 2012 that we wish to bring to your attention:

**1. Electricity Sales**

Comment: Our tests of electricity sales disclosed the following:

- a. Reconciliations between PayPal and merchant accounts are not being performed.
- b. Of seventy-five accounts tested:
  - One account (account/service address nos. 124381/150826) was erroneously reclassified from Schedule K to Schedule S. Based on the rate schedule, "A Small Government Demand (Schedule K) customer will be transferred to Small Government NonDemand (Schedule S) service if the customer's monthly consumption in each of the customer's last twelve billing months is less than 5,000 kWh". Our examination of the account's monthly consumption history for the last twelve months indicated that monthly power consumption exceeded 5,000 kWh for the majority of the past twelve months; as such, the customer should have not been reclassified to Schedule S. We were informed that Utiligy is not capable of detecting consumption trends in the customers' accounts to prompt a change in rate class when consumption reaches certain levels; therefore, manual analysis of the account was performed. However, the manual analysis performed was based on a criterion which does not apply to the account tested.
  - One account (account/service address nos. 211944/109262) was erroneously reclassified from Schedule J to Schedule G. Based on the rate schedule, "A Small General Demand (Schedule J) customer will be transferred to Small General NonDemand (Schedule G) service, if the customer's average daily kWh consumption is less than 200 kWh per day in each of the customer's last twelve billing months." Our examination of the customer's average daily consumption for the past 12 months indicated that the customer exceeded daily consumption of 200kWh for the month of November 2011; as such, the customer should not have been reclassified to Schedule G. We were informed that Utiligy is not capable of detecting consumption trends in the customers' accounts to prompt a change in rate class when consumption reaches certain levels; therefore, manual analysis of the account was performed. However, the manual analysis performed was based on a criterion which does not apply to the account tested.
  - One account (account no. 291378) was not properly assessed for late fees. We were informed that Utiligy does not properly age transferred balances. Balances transferred from other accounts are excluded from the late fee calculation generated by Utiligy resulting in under charges in late fees for accounts with unpaid transferred balances.
  - One account (account no. D100121239) was overcharged because the estimate usage generated in Utiligy is not based on the previous 3-months consumption. We were informed that Utiligy is experiencing issues with the base load calculation affecting estimates.

SECTION I –DEFICIENCIES, CONTINUED

1. Electricity Sales, Continued

Recommendation: In line with GPA’s effort in streamlining errors and account misclassifications, the following may be considered:

- a. Reconciliation between PayPal and merchant accounts should be performed on a monthly basis and an investigation should be conducted for differences above an established threshold.
- b. Perform further analysis of rate class changes.
- c. Devise a method to allow for accurate calculation of late fees considering Utiligy’s limitations.

2. Cancellation and Rebills

Comment: Of five customer accounts tested, one account (Service Agreement No. 276762) was subject to multiple cancellations due to an improper termination of the account. The customer’s meter was not timely terminated by the Connect/Reconnect crew; therefore, charges were generated after the requested termination date. The error was discovered when the customer disputed the charges.

Recommendation: We recommend that timely termination of meters and cross review of termination requests occur.

3. Allowance for Doubtful Accounts

Comment: GPA has long outstanding receivables from the Department of Public Works (DPW) and Guam Waterworks Authority (GWA) of \$390,377 and \$216,993, respectively. However, both DPW and GWA dispute the balances. No allowance for doubtful accounts had been recognized for these accounts.

Further, our analysis of the allowance for doubtful accounts provided for other receivables indicated that the provision is understated by approximately \$230,000 representing accounts that are dated 2011 and prior.

Prior Year Status: This condition is reiterative of conditions identified in our prior year audit of GPA.

Recommendation: We recommend that GPA discuss the DPW and GWA accounts with the CCU for appropriate action. Further, we recommend that all long outstanding receivables be considered in the analysis of the provision for doubtful accounts.

4. Utility Plant

Comment: One item under the general plant account (Code # 2727422, Altec 80486-33 EISA System) was obsolete and no longer supported. Although the item is already fully depreciated and appears to have been retired, such has not been adjusted in the general plant assets ledger.

Recommendation: We recommend that obsolete or retired assets be adjusted from the fixed assets register.

**SECTION I –DEFICIENCIES, CONTINUED**

5. Water and Sewer Billings

Comment: Beginning January 2012, GWA billed GPA for water and sewer charges previously handled through the Navy. Absent an agreement or a contract, GPA remitted payments to GWA based on the Navy rates which were lower than those billed by GWA. GPA recorded a payable to GWA covering the difference in GWA billing and the Navy rates.

Recommendation: GPA should clarify billing rates with GWA and enter into a service agreement to minimize the potential for disputes.

6. Bid Deposits

Comment: Bid deposits totaling \$111,288 dated 2005 to 2011 remain outstanding at September 30, 2012. We were informed that outstanding bid deposits from prior years may be due to unclaimed bid deposits or improper posting of salvage bids. Currently, GPA does not have a policy for recognizing unclaimed bid deposits as revenue; therefore the deposits remain as a liability. Salvage bids should be recognized as revenue rather than a liability immediately upon collection.

Recommendation: A policy for recognizing unclaimed bid deposits should be established. Further, GPA should regularly monitor the bid deposit account to reclassify salvage bids timely.

7. Customer Deposits

Comment: Our tests of customer deposits disclosed the following:

- a. Account number 294508 was assessed a guarantee deposit of \$500 on June 30, 2012 and there was no documentation of the basis of the amount assessed.
- b. The Utiligy system improperly applied credits to various customer accounts with guarantee deposits. Deposits made by customers in fiscal year 2012 were not properly captured in the guarantee deposit schedule resulting in an overpayment of refunds claimed. For one account (account#166890), the customer made a guarantee deposit of \$300; however a \$364.83 refund was applied to the customer's last bill.
- c. At September 30, 2012, customer deposit subsidiary details contained negative balances totaling \$18,325. Furthermore, no regular review of related accrued interest occurs.

Recommendation: Consistent documentation of the basis for the customer deposit should be assessed in accordance with GPA's policy. Further, Utiligy calculations should be checked and negative balances in customer deposits should be investigated.

**SECTION I – DEFICIENCIES, CONTINUED**

8. Annual Leave

Comment: Beginning in 2010, the JD Edwards system included a module that allows for monitoring of annual leave. However, monitoring is still being performed through the use of manual records and excel spreadsheets. Further, reconciliation of annual leave schedules to the general ledger is only performed at year-end. As of September 30, 2012, annual leave accrual has the following balances:

General ledger balance	\$3,144,583
Subsidiary ledger – JD Edwards module	\$3,146,012
Subsidiary ledger – Manual monitoring	\$3,056,194

An adjustment was not proposed as the differences are not considered material.

Recommendation: We recommend that the leave monitoring module in the JD Edwards system be utilized in order to minimize the time spent by the Payroll Department in manually tracking leave credits. Further, we recommend that reconciliations of annual leave accruals be performed at least quarterly.

**SECTION II – OTHER MATTERS**

Other matters related to our observations concerning operations, compliance with laws and regulations, and best practices involving internal control over financial reporting that we wish to bring to your attention are as follows:

1. Liquidated Damages

Comment: The Guam Procurement Law (the Law) requires that when a contractor is given notice of delay or nonperformance and fails to cure in the time specified, the contract shall be liable for damages for delay of one-fourth of 1% of the outstanding order per calendar day from the date set for cure until either similar supplies or services are reasonably obtained if the contractor is terminated for default, or until the contractor provides the supplies or services if not terminated for default. The Law also provides forbearance for nonperformance or delayed performance if the contractor has notified the Procurement Officer within 15 days after the cause of the delay and the failure arises out of causes such as: acts of God, fires, floods, epidemics, unusually severe weather and other reasons that are beyond the control of the contractor.

Our examination of expenses noted that liquidated damages are not uniformly assessed. Further, waivers of liquidated damages for one contractor’s delayed performance did not appear to qualify under the above criteria.

Recommendation: GPA should comply with the requirements of the Law and reasons for exceptions should be documented.

**SECTION II – OTHER MATTERS, CONTINUED**2. Defective Fuel Auto Gauges

Comment: Fuel auto gauges are devices used to record fuel consumption and issuance. During the fuel inventory observation, we noted the following tanks with defective fuel auto gauges:

<u>No.</u>	<u>Location</u>	<u>Tank No.</u>
1	Piti (MEC) #6 & #7 (Old Tanks)	Tank 1
2	Piti (MEC) #6 & #7 (Old Tanks)	Tank 2
3	Piti Power Plant 8 & 9 (MEC)	TA-FO-01
4	Piti Power Plant 8 & 9 (MEC)	TA-FO-03
5	Piti Power Plant 8 & 9 (MEC)	TA-FO-26

Recommendation: We recommend that auto gauges be maintained or replaced so that accurate measurement of fuel consumption and issuance are achieved.

**SECTION III – DEFINITIONS**

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.

The definition of a deficiency is as follows:

A *deficiency* in internal control over financial reporting 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**

GPA'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.