PORT AUTHORITY OF GUAM

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND INTERNAL CONTROL

SEPTEMBER 30, 1999

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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED UPON THE AUDIT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board of Directors
Port Authority of Guam:

We have audited the financial statements of the Port Authority of Guam (the Authority) as of and for the year ended September 30, 1999, and have issued our report thereon dated March 26, 2001. We conducted our audit 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.

Compliance

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards* which is described in the accompanying Schedule of Findings and Questioned Costs as item number 99-07.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operations of the internal control over financial reporting that, in our judgment, could adversely affect the Authority's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as item numbers 99-01 though 99-08.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described above is a material weakness.

This report is intended for the information of the management and the Board of Directors of the Port Authority of Guam, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

Deloitte + Touche LLP

March 26, 2001

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Schedule of Findings and Questioned Costs
September 30, 1999

Finding Number 99-01 – Space Lease Income

Criteria: The provision of all space lease agreements should be reviewed and enforced.

Condition: The Unitek lease agreement requires additional rent of 3.5% of gross revenue of Unitek. The Authority has not billed the percentage rent portion of the Unitek lease since the effective date of the agreement.

Cause: The cause of this condition is unknown.

Effect: Additional income that the Authority could use is not being collected. The actual revenue that could be earned by enforcing the percentage rent portion of the lease cannot be determined, as no information regarding Unitek's gross revenue is available.

Recommendation: Management should thoroughly review lease agreements and ensure that all lease terms are enforced and that any rental income due the Authority is billed and collected.

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Schedule of Findings and Questioned Costs
September 30, 1999

Finding Number 99-02 – Parts, Materials and Supplies

Criteria: Parts, materials and supplies should be recorded as inventory until used.

Condition: Several parts, materials and supplies purchased within the facility maintenance and equipment maintenance department have been expensed upon purchase rather than capitalized.

Cause: When purchases are being recorded and paid for, items acquired are not being reviewed thoroughly to ensure proper classification.

Effect: Parts, materials, and supplies expense may be immaterially overstated.

Recommendation: Management should review disbursements to ensure that amounts are being properly recorded.

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Schedule of Findings and Questioned Costs
September 30, 1999

Finding Number 99-03 – Property, Plant and Equipment

Criteria: To ensure the validity of recorded fixed assets, the Authority must protect their existence by properly tagging and safeguarding them and maintaining updated location listings for all movable assets.

Condition: During fixed asset existence testing, the following 3 items out of 27 items tested could not be located by Authority personnel for verification of existence.

Class	Item	Section Assigned To	NBV @ 9/30/99
Communication Equip	Smartnet System	Port Police	$37,095
Office Equipment	Pedestal (furniture)	GM	$200 (approx.)
Office Equipment	Executive Chair	GM	$400 (approx.)

Cause: The cause of this condition is unknown.

Effect: Property, plant and equipment maybe immaterially misstated.

Recommendation: The Authority should ensure that all personnel are aware of a policy requiring significant events, such as relocations, damages, obsolescence, etc., to be reported to the fixed asset custodian for recording. The fixed asset register should be updated to reflect all changes.

Finding Number 99-04 – Audit Adjustments

Criteria: To ensure the accuracy of the accounting records, audit adjustments should be recorded in timely fashion before the closing of the fiscal year, if possible, or immediately after completion of the audit. Also, accounting personnel should understand the background of each audit adjustment to ensure that proposed adjustments are proper and that the affected subsidiary ledger can be properly adjusted, if necessary. This will ensure that correct and accurate financial records are maintained.

Condition: During our audit of fiscal year 1999, we discovered that none of the fiscal year 1998 audit adjustments had been posted.

Cause: The cause of this condition is unknown.

Effect: Preliminary balances of retained earnings and several other accounts, as provided to us at the start of the fiscal year 1999 audit, were significantly misstated. Internal financial statements produced since the completion of the fiscal year 1998 audit for management purposes were, therefore, also significantly misstated. Consequently, management decisions and analyses relied on inaccurate financial information.

Recommendation: The Authority should ensure that all audit adjustments are recorded in a timely manner. Authority personnel should concur with and understand the reason for all audit adjustments before accepting the audited financial statements.

Finding Number 99-05 – Retirement Expense

Criteria: The Authority's statutory payments to the GovGuam Retirement Fund for the Defined Benefit Retirement Plan should be adjusted to the actuarially determined expense rate less the effects of its recorded unfunded pension costs.

Condition: In 1999, the effect of the Authority's prior year accruals, for its share of pension underfunding, should have caused a reduction in the actuarially determined employer contribution rate from 16.37% to an effective rate of 9.56%, thereby reducing the retirement liability in the balance sheet and realizing a recovery of pension expense. For several years, it appears that the Authority has significantly over recorded pension expense.

Cause: The cause of this condition is unknown.

Effect: Preliminary balances of pension expense and consequently retained earnings, as provided to us at the start of the fiscal year 1999 audit, were misstated.

Recommendation: The Port should properly record its unfunded retirement liability based on the Government of Guam Retirement Fund's actuarial reports.

Finding Number 99-06 - Property, Plant and Equipment

Criteria: Property, plant and equipment purchased on credit should be recorded at either a) cash equivalent price or b) the present value of the future payments required by the debt agreement. In addition, the Authority should possess the means to accurately compute depreciation expense on property, plant and equipment on a monthly basis.

Condition:

(1) The Hitachi Crane (Subic) was recorded at the total of all future annual payments, or $3,371,989. This amount was not discounted at the stated interest rate (10%) at the time of acquisition (1/15/94), as required by accounting principles generally accepted in the United States of America. The equipment should have been recorded at approximately $2,595,000.

(2) In addition, 4 out of 32 items tested for reasonableness of depreciation expense produced an overstatement of expense for the current year of approximately $247,000.

Cause: The cause of the conditions noted above are unknown.

Effect: The error in recording the cost of the Hitachi Crane resulted in an overstatement of property, plant and equipment, of approximately $777,000. The miscalculation of depreciation expense, combined with the over-depreciation of the Hitachi Crane and the under-depreciation of other property, plant and equipment due to non-recording of prior periods' audit adjustments (see Finding Number 99-04), resulted in a net understatement of expense of approximately $166,000. These misstatements were corrected through adjustments during the audit.

Recommendation: Property, plant and equipment should be properly recorded at acquisition cost. Also, the fixed asset system should be reviewed on a regular basis for inaccuracies in its processes and computations.

Finding Number 99-07 – Single Audit

Criteria: The Authority is required under the Single Audit Act to have an audit performed in accordance with OMB Circular A-133 in any year in which it has more than $300,000 in Federal awards expenditures. The Authority is in noncompliance with the Act as long as the required audit is not performed.

Condition: The Authority expended in excess of $300,000 in fiscal year 1998 for its only major program, FEMA Disaster Relief. Consequently, a single or program audit was required for fiscal year 1998 for the FEMA Disaster Relief federal program. However, no single or program audit has been performed to date.

Cause: The cause of this condition is unknown.

Effect: To date, the Authority is not in compliance with the Single Audit Act.

Recommendation: The Authority should immediately contract for either a single audit or a program audit of the fiscal year 1998 FEMA Disaster Relief program.

Finding Number 99-8 – Timely Billings

Criteria: Billings for services provided to customers should be issued at the time the services are rendered.

Condition: The Authority issued a billing of $1.4 million to another government agency in fiscal year 2001 for services provided or paid for by the Authority in fiscal years 1995, 1998, 1999 and 2000.

Cause: The cause of this condition is unknown.

Effect: Revenues for fiscal years 1995, 1998 and 1999 are potentially understated. The collectibility of an invoice issued so late is questionable. The Authority's cash flow has been negatively impacted.

Recommendation: Billings for services should be issued when services are provided.