



December 26, 2002

Guam Education Policy Board
Government of Guam

Gentlemen:

We have been engaged to audit selected financial statements of the Guam Department of Education (DOE) during fiscal years 1998 through 2001. As part of this engagement, we are required to perform an auditability assessment of DOE and provide our findings and recommendations to DOE, the Office of the Public Auditor of Guam and affected federal agencies. This auditability assessment does not constitute an audit performed in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States. Accordingly, we do not express an opinion or any other assurance on the financial statements of DOE for the fiscal years 1998 through 2001.

Our assessment of the auditability of the Guam Department of Education for the years ended September 30, 1998, 1999, 2000 and 2001 consisted of performing the following procedures:

1. We obtained DOE balance sheets and statements of revenues and expenditures for the years ended September 30, 1998, 1999 and 2000. DOE has not closed 2001 but we were able to download the DOE general ledger.
2. We prepared and submitted listings of basic schedules that would be required for the financial audits for 1998, 1999 and 2000. We did not request that DOE prepare the requested schedules; we requested that DOE indicate whether or not they could provide the schedules.
3. We performed analytical reviews of the balance sheets and statements of revenue and expenditures for the years ended September 30, 1998, 1999 and 2000.
4. We performed high level walkthroughs of the major DOE accounting systems.

Findings

1. Analytical Reviews

In our review of the internal financial statements of DOE, we noted the following conditions:

- a. Balance sheets for several funds did not balance. In total, balance sheets for twenty-five (25) funds did not balance at September 30, 1998, 1999 and 2000. Out of balance amounts ranged from very small amounts (\$76) to an out-of-balance condition in one fund in two different years of almost \$12 million.

- b. Net fund equity plus or minus the excess of revenues over expenditures did not roll forward from year to year for the majority of funds in 1999 and 2000.
- c. There were several instances where account balances in funds simply do not make sense based on the nature of the account (i.e. large credit balances in cash accounts; debit balances in accounts payable and accrual accounts, etc.).
- d. Interfund cash account balances do not eliminate when combined. Variances exist of \$1.5 million at September 30, 1998, almost \$34 million at September 30, 1999 and almost \$36 million at September 30, 2000.

2. Schedule Requests

We have not received a formal response to our schedule request. However, we have informally discussed the availability of schedules with Mr. Ray Miranda, controller of DOE and other accounting personnel, and we have determined that one very key schedule, the bank reconciliation, has not been prepared over the entire four-year period from 1998 to 2001. Given the thousands of transactions and millions of dollars that flowed through DOE's bank accounts during the period, this condition represents a major obstacle in the audit process.

It appears that DOE may be able to provide schedules to support certain minor balance sheet accounts.

3. Systems Review

We walked through general ledger, revenue, expenditure and payroll systems.

Based on our discussions with accounting personnel, there appears to be a major problem with unrecorded transactions, particularly in the revenue/cash receipts cycle. Wire transfers for several years have not been recorded and DOE personnel have not been able to enter interbank transfers into the system. We have not determined if these problems are a result of system problems or an inability to properly administer the system.

It appears that the Financial Management System (FMS) in use at DOE has been significantly customized. If the customization was not performed by someone very knowledgeable in fund accounting, this could be the cause of some of the errors noted above.

Also, as noted above, reconciliation and other basic error detection control procedures are not regularly performed.

Suggested Audit Approach

In our opinion, the DOE financial statements for 1998, 1999 and 2000 are not auditable in their current state. The out-of-balance conditions appear to indicate concerns with basic computer systems or their administration. The lack of bank reconciliations and the significance of unrecorded transactions raises questions about the completeness of DOE's records.

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Given the state of DOE's records, we believe that the financial statements will need to be reconstructed. Portions of the reconstruction would need to be done prior to audit of reconstructed balances and some of the reconstruction work could be done as the account balances are being audited. Reconstruction of accounts would largely be performed using subsequent activity in the accounts and from records obtained from government agencies and other entities with whom DOE transacts business.

Reconstruction of all four years would be enormously time consuming. Adjustments for fiscal year 1998 would have been posted to 1999, 1999 adjustments posted to 2000, etc. Even with the reconstruction efforts, the opinion may be qualified on significant accounts and balances within the financial statements.

To complete this engagement in as timely a manner as possible, we propose foregoing the reconstruction of the 1998 and 1999 financial statements and beginning the reconstruction with the balance sheet at September 30, 2000. With this approach, we hope to be able to establish a good starting point at that date. All errors and misstatements discovered from the preceding three years would essentially be recorded through the various fund balance accounts at September 30, 2000. Because the general ledger is not yet closed for fiscal year 2001, all entries required to correct the balance sheet at September 30, 2000 could be recorded by DOE as adjustments to beginning balances. Fiscal year 2001 would then be subject to a full financial audit.

We believe that this appears to be the most plausible approach to (1) completing a financial audit of DOE for at least one fiscal year; and (2) providing DOE accounting personnel a fresh start. We note that several of the aforementioned out-of-balance conditions were in effect at September 30, 1998 and continued at the same relative amount at September 30, 1999 and 2000. We were also informed that one of the obstacles to completing bank reconciliations has been the large number of old uncleared reconciling items. This audit approach should reduce or eliminate the majority of these problems and allow DOE accounting personnel to concentrate on maintaining records on a more current basis.

Very truly yours,

A handwritten signature in cursive script that reads "Deloitte & Touche LLP". The signature is written in dark ink and is positioned below the "Very truly yours," text.