# GUAM HOUSING CORPORATION

## SINGLE AUDIT

### FOR THE YEAR ENDED SEPTEMBER 30, 1998

## INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Directors
Guam Housing Corporation:

We have audited the financial statements of Guam Housing Corporation (GHC), a component unit of the Government of Guam, as of and for the year ended September 30, 1998 and have issued our report thereon dated February 25, 1999. We conducted our audit in accordance with generally accepted auditing standards 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 GHC'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 instances of noncompliance that are required to be reported under Government Auditing Standards and are described in the accompanying Schedule of Findings and Questioned Costs (pages 7 through 21) as item 98-13.

Internal Control over Financial Reporting

In planning and performing our audit, we considered GHC'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 operation of the internal control over financial reporting that, in our judgment, could adversely affect GHC'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 items 98-1 through 98-12.

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 the amount 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, of the reportable conditions described above, we consider items 98-2, 98-6, 98-10, and 98-12 to be material weaknesses.

This report is intended for the information of the management, and Board of Directors of the Guam Housing Corporation, the cognizant audit and other federal agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

February 25, 1999

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

To the Board of Commissioners
Guam Housing Corporation:

Compliance

We have audited the financial statements of Guam Housing Corporation (GHC), a component unit of the Government of Guam, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended September 30, 1998. GHC's major federal program is identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs (pages 6 and 7). Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of GHC's management. Our responsibility is to express an opinion on GHC's compliance based on our audit.

We conducted our audit of compliance in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about GHC's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of GHC's compliance with those requirements.

As described in item 98-13 in the accompanying Schedule of Findings and Questioned Costs, GHC did not comply with requirements regarding the Davis-Bacon Act that is applicable to its Community Development Block Grant federal program. Compliance with such requirements is necessary, in our opinion, for GHC to comply with requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, GHC complied, in all material respects, with the requirements referred to above that applicable to each of its major federal program for the year ended September 30, 1998.

Internal Control Over Compliance

The management of GHC is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered GHC's internal control over compliance with requirements that could have a direct and material effect on a major program in order to determine our auditing procedures for the purpose of expressing an opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance 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 operation of the internal control over compliance that, in our judgment, could adversely affect GHC's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 98-13.

A material weakness is a condition in which the design or operation one or more of the internal control components does not reduce to a relatively low level of risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program 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 compliance 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, of the reportable conditions described above, we consider item 97-9 to be a material weakness.

Schedule of Expenditures of Federal Awards

We have audited the basic financial statements of the Guam Housing Corporation as of and for the year ended September 30, 1998, and have issued our report thereon dated February 25, 1999. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards (page 6), is presented for additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. This schedule is the responsibility of the management of GHC. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended for the information of the management and Board of Directors, the cognizant audit and federal agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

February 25, 1999

**GUAM HOUSING AND URBAN RENEWAL AUTHORITY**

Schedule of Expenditures of Federal Awards
Year Ended September 30, 1998

| CFDA# | AGENCY/PROGRAM | Pass-Through Entity Identifying Number | 1998 Fiscal Year Expenditures |
|---|---|---|---|
| | **U. S. Department of Housing and Urban Development**: | | |
| | **Pass-Through Programs received from:** | | |
| | **Guam Housing and Urban Renewal Authority** | 96-0001279 | |
| 14.219 | Community Development Block Grant | | $ 592,578 |
| 14.239 | Home Investment Partnership | | 27,687 |
| | Total Expenditures of Federal Financial Awards | | $ 620,265 |
| | Total Expenditures of Federal Financial Awards Tested | | $ 592,578 |
| | Percentage of Federal Awards Tested | | 95.50% |

**Note 1. Basis of Presentation**

The accompanying schedule of expenditures of federal awards includes the grant activity of GHC and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, ***Audits of State and Local Governments, and Non-Profit Organizations***. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

**Note 2. Subrecipients**

The Guam Housing Corporation received federal Awards that were passed-through from the Guam Housing and Urban Renewal Authority from the CDBG and HOME programs totaling $592,578, as of September 30, 1998.

**Note 3. Major Programs**

Of the above programs, only the CDBG program met the criteria as major program and, accordingly, was subjected to applicable audit procedures as required by OMB Circular A-133.

**GUAM HOUSING CORPORATION**

Schedule of Findings and Questioned Costs
Year Ended September 30, 1998

**Part I – Summary of Audit Results**

Financial Statements

We have audited the basic financial statement of GHURA and issued an unqualified opinion.

Internal control over financial reporting:

- Material weaknesses were identified? ___x___yes ______ no

- Reportable conditions identified that are not considered to be material weaknesses? ___x___yes ______ none reported

Noncompliance material to financial statements noted? ______yes ___x___ no

Federal Awards

Internal control over financial reporting:

- Material weaknesses were identified? ___x___yes ______ no

- Reportable conditions identified that are not considered to be material weaknesses? ___x___yes ______ none reported

The auditor's report on major program compliance for GHC having three major programs included a qualified opinion on the Community Development Block Grant program based on identified reportable conditions, which, in our opinion, are not considered to be material weaknesses.

Any audit findings disclosed that are required to reported in accordance with section 510(a) of Circular A-133? ______yes ___x___ no

**GUAM HOUSING CORPORATION**

Schedule of Findings and Questioned Costs
Year Ended September 30, 1998

**Part I – Summary of Audit Results, continued**

Identification of major programs:

| CFDA# | PROGRAM |
|---|---|
| 14.219 | Community Development Block Grant |

Dollar threshold used to distinguish between type A and type B programs: $300,000

Auditee qualified as low-risk audit? ______ yes ___x___ no

**Part II - Financial Statement Findings Section**

There were no instances of noncompliance noted that should be reported in accordance with Government Auditing Standards.

**Part III - Federal Award Findings and Questioned Costs**

We noted certain reportable conditions, material weaknesses, and instances of noncompliance, including questions costs which are presented in the following pages as items 97-1 through 98-13

**Part II – Financial Statement Findings**

98-1 Criteria:

Financial lending institutions should design their lending activities to control and manage the lending risks e.g., credit risk, collateral risk, concentration risk, management or operational risk, and fraud risk. Those activities can generally be classified into the following categories:

a. Originating and disbursement
b. Servicing and accounting
c. Credit monitoring and collection
d. Internal loan review
e. Loan evaluation

Condition:

The Corporation recognizes what are referred to as Deferred Loans. These are loans whereby the borrower requests, in writing, that loan payments be deferred for a specified period of time. The President of the Corporation must approve deferred loans. At 9/30/98 there were 20 deferred loans outstanding with an aggregate accrued interest of approximately $130,100. There are no formal approved written underwriting policies and procedures for granting approval of deferred loans. Therefore, it appears that there is a lack of internal controls over loan credit monitoring and collection and internal loan review activities.

Cause:

The Corporation has not established and implemented approved written underwriting policies and procedures for granting deferred loans.

Effect:

There is no effect on the financial statements as a result of this condition.

98-1 Recommendation:

We recommend management establish written internal control loan underwriting policies and procedures for granting approval of deferred loans. Deferred loan policies and procedures should consider credit and collateral risk. Credit risk is the risk that the borrower will not repay the loan and the lender will not recover the amount of the loan. Collateral risk can be considered an aspect of credit risk because it can directly affect the risk of credit loss relating to the loan. Collateral risk is the risk that a loss will be incurred on secured loans because of circumstances such as the value of the collateral has declined significantly, among others.

The Board of Directors should approve all deferred loans until such time that adequate deferment loan policies and procedures are established and properly implemented.

98-2 Criteria:

Statement on Financial Accounting Standards No. 5, *Accounting for Contingencies*, (SFAS No. 5) and Statement on Financial Accounting Standards No. 114, *Accounting by Creditors for Impairment of a Loan* (SFAS No. 114), as amended, are the primary sources of guidance on accounting for the allowance for loan losses.

An allowance for loan losses should be maintained at a level which, in management's opinion, is adequate to absorb credit losses inherent in the loan portfolio. The amount of the allowance should be based on an evaluation of the collectibility of the loan portfolio, including the nature of the portfolio, credit concentrations, trends in historical loss experience, specific impaired loans, economic conditions, and other risks inherent to the loan portfolio. Allowances for impaired loans are generally determined based on collateral values or the present value of estimated cash flows. The allowance should be increased by a provision for loan losses, which is charged to expense and reduced by charge-offs, net of recoveries. Changes in the allowance relating to impaired loans should be charged or credited to the provision for loan losses.

Condition:

During our audit of the Corporation's loan portfolio and related allowance for loan loss, we noted that the allowance account approximating $30,805 had not been adjusted for over 6 years. Furthermore, we noted that the Corporation lacked written internal control policies and procedures to evaluate loans for potential loan loss. An audit adjustment of $80,000 was made to the allowance for loan losses to increase the reserve to approximately $110,000; this amount may not be sufficient for potential credit risk as of September 30, 1998.

98-2 Condition: (continued)

Additionally, we noted 60 loan approximating $3,889,588 that were delinquent and outstanding over 120 days as of September 30, 1998. Accordingly, accrued interest receivable on these loans approximated $301,150. Of these loans, $892,846 or 22% are outstanding in excess of 12 months. Management represented these loans had been reviewed and that the collateral value was higher than the potential loan loss, hence, there is no potential credit risk. However, based on review of the certain loan files, documentation was not available in the borrowers' file to evidence that a loan evaluation and review was conducted.

Cause:

The Corporation has not established written policies and procedures for determining the allowance for loan losses based on generally accepted requirements.

Effect:

The effect of the above condition is the possibility of an ineffective method for determining the allowance for loan losses.

Recommendation:

We recommend that management establish and implement written policies and procedures for determining loan losses and to ensure that an allowance for loan loss is adequate to absorb credit losses inherent in the loan portfolio and the components relating to impaired loans is adequate to provide for any losses computed in accordance with SFAS No. 114.

Loan evaluation is the process used to determine the allowance for loan losses. Therefore, we recommend that the Corporation establish an internal loan review function independent of origination, disbursement, servicing, accounting, monitoring, and collection functions. The loan review function may be performed by a committee of the board of directors or employees of another department. The objectives of internal loan reviews are to: 1) monitor compliance with established lending policies; 2) assess whether the payments due on the loan are likely to be received in accordance with the loan terms; and 3) identify weaknesses in the lending process or the lending officers' skills in originating, monitoring and collecting loans.

Efforts should be made to reduce delinquent loans, as such negatively impacts the Corporation's cash flow and its ability to generate new loans.

98-3 Criteria:

Loan files should be maintained in an orderly and systematic manner to ensure that all documentation is obtained and filed and can be independently verified.

Condition:

The Corporation utilizes a document checklist for obtaining borrower information and maintaining loan files. The loan checklist form is not being properly used. Documents are not being filed in loan files in accordance with the checklist index . Additionally, in 5 of 58 or 5% of loans tested, tasks were initialed as being completed or documents obtained when in fact, such had not been completed. Those loan files are as follows:

1. SRF – 19802549
2. R5 – 59802515
3. SRF – 19802542
4. SRF – 19802555
5. SRF – 19802561

Cause:

The cause of the above condition is the lack of internal controls to ensure that all loan files are reviewed for proper documentation prior to loan approval.

Effect:

The potential exist for loans to be improperly approved.

Recommendation:

Loan files should be properly reviewed to ensure all documents have been obtained prior to loan approval and disbursement of funds. All tasks performed should be initialed as completed by the responsible individual to ensure that the task was done. Additionally, filing the documents as scheduled on the Loan Checklist will not only save the Corporation time in locating documents but also reduce the likelihood of missing documents.

## GUAM HOUSING CORPORATION

Schedule of Findings and Questioned Costs
Year Ended September 30, 1998

98-4 Criteria:

In accordance with Federal regulations, lending institutions are required to disclose all loan terms and conditions to borrowers on the Truth-in Lending Disclosure Statement and obtain the borrower's signature for acknowledgement.

Condition:

On loan number SRF-19802549, the required borrowers signature was not present on the Federal Truth-in lending Disclosure Statement. The occurrence of this incident was 1 of 58 loans tested.

Cause:

The cause of the above condition is unknown.

Effect:

The Corporation is noncompliance with Federal regulations.

Recommendation

Greater care and responsibility needs to be taken so that employees will be accountable to the task performed. All borrower signatures should be obtained prior to loan approval. Additionally, the borrower must be contacted to sign the Federal Truth-in Lending Disclosure Statement.

98-5 Criteria:

Promissory notes should be obtained from all borrowers prior to loan disbursement.

Condition:

In two of fifty-eight loans tested the promissory notes were not present for SRF-19802431 and R5–69902574.

Additionally, approximately half of the other fifty-eight loans tested had the original promissory notes in the loan files.

98-5 Cause:

The cause of this condition is unknown.

Effect:

Loans are being approved and disbursed without obtaining executed promissory notes.

Recommendation:

Promissory notes should be obtained for the above loans. Greater care and responsibility should be taken in the maintenance of documents. Original promissory notes should be locked in the safe. Loan technicians should go through each loan file and replace original promissory notes with photocopies and file the original in the safe.

98-6 Criteria:

The loan-to-value ratios should be properly calculated and reviewed prior to loan origination.

Condition:

For loan R5–59802551, the building constructed differed from that in the plans for which the loan was obtained and approved. The appraiser valued the land and a two-story building of 3,474 square feet at $310,000. The building was to have on the first level 1 living room, 1 dining room, 1 family room, 1 bedroom, and 1 bathroom. The second floor was to have 3 bedrooms, three bathrooms and a study. According to the appraisal report, all construction was to be new. The construction contract was for $103,118.23 or $29.68 per square foot, an unreasonably low amount. The materials list also indicated there would be plumbing of 2 bathrooms. The original called for 1 bathroom on the first floor. There was also no documentation of any inspections on work performed for progress billings. It appears that had the reviewer calculated the cost of construction per square foot or reviewed the description of materials, they would have been alerted to a potential problem due to the inconsistencies. There is a high likelihood that the building constructed is not the building financed. This also includes the likelihood that the loan originated exceeded 80% of the appraised value.

98-6 Cause:

The cause of this condition is unknown.

Effect:

It appears that this loan was improperly approved and may be at risk as a result of this condition.

Recommendation:

Legal lending limits and loan-to-value ratios restrict the amount of funds that may be loaned to a single borrower. The purpose of those regulations is to limit the financial institution's exposure with respect to a single borrower. It also tends to limit the size of the loan that a single financial institution can make. Loan-to-value regulations establish the minimum collateral margins required for making certain types of loans. Management should adhere to existing lending policies to minimize its credit risk. Additionally, the contractor should be contacted to determine what is being built. If the building is found to differ than that financed, an appraisal will be required to determine if amount financed is within 80% of the new appraised value. Additionally, more care is required when reviewing contracts and construction loans.

98-7 Criteria:

Upon loan approval, all executed mortgages must be signed, notarized and recorded with the Government of Guam's Department of Land Management.

Condition:

In two of 58 new loans tested, the mortgage was not filed with the Government of Guam's Department of Land Management or loans SRF–19802542 and R5–59802574. The Corporation did not adequately secure its collateral ownership position on these loans.

Cause:

The Corporation has not established internal control procedures to ensure that all executed mortgages are properly recorded with the Government of Guam's Department of Land Management.

98-7 Effect:

The Corporation did not perfect its ownership interest in the property as a result of this condition.

Recommendation:

Management must investigate this condition and ensure that such executed mortgages are recorded with the Department of Land Management. The Corporation cannot be certain that it has a perfected interest in the title until such time. Should the borrower default on the loan, it may be possible that the Corporation will not have any legal remedy or recourse to recover any amounts outstanding and due on the loans.

The loan technicians should go through all loan files to gain assurance that all mortgages have been properly recorded with the Department of Land Management and immediately obtain any missing recorded mortgages.

Internal control policies and procedures must be established to ensure that all executed mortgages are properly recorded with Government of Guam's Department of Land Management.

98-8 Criteria:

Loans should be originated in accordance with the Corporation's lending underwriting policies and procedures. Additionally, all pertinent loan documents and amounts should be properly completed and calculated, respectively.

Condition:

For loan number R5–59802430, the finance charge was not properly computed on the Federal Truth-in Lending Statement. The amount shown on the Statement is $546,682.80. The amount that should be noted is $199,242.80.

The applicant's loan Review Sheet was not contained in the loan file, hence we could not determine eligibility for the loan. Additionally, there was no department clearance. It appears that this loan was not properly evaluated and approved in accordance the Corporation's underwriting policies and procedures.

98-8 Cause:

The cause of this condition is unknown.

Effect:

It appears that this loan was improperly approved.

Recommendation:

Loans should not be approved or disbursed until all documentation is complete. Internal control policies and procedures should be established to ensure that all loans are documented and approved in accordance with the Corporation's underwriting policies and procedures. Procedures should be established to ensure that upon loan approval, all documentation has been obtained, reviewed and properly evaluated to support such approval. Additionally, the Federal Truth-in Lending Statement should be corrected and signed by the borrower.

98-9 Criteria:

In accordance with Federal regulations, lending institutions are required to disclose all loan terms and conditions to borrowers on the Truth-in Lending Disclosure Statement and such information should be consistent on all pertinent loan documents.

Condition:

For one of 58 loans tested, the amount of the monthly loan payment of $1,321.74 shown on the promissory note for loan number R5-59802504 was incorrect. The correct amount is $1,079.19 resulting in a difference of $242.55.

Cause:

The cause of this condition is unknown.

98-9 Effect:

It appears that the signed and executed promissory note is incorrect.

Recommendation:

The promissory note should be corrected immediately and signed by the borrower. Greater care needs to take place in the preparation and review of loan documents.

98-10 Criteria:

Loans should be approved and originated in accordance with the Corporation's underwriting policies and procedures.

Condition:

For loan R5-59802430, the amount borrowed exceeded that authorized. The contract price for the property sets the base for determining the amount of the loan, which was $115,000. The amount of the loan should have been $92,000 ($115,000 x 80%). However, $172,000 or 80% of the appraised value of $215,000 was lent, thus exceeding that authorized. The appraisal also appears incorrect, as the dwelling appraised was for a wooden building.

Cause:

The cause of this condition is unknown.

Effect:

It appears that the loan was improperly approved as a result of this condition.

Recommendation:

Legal lending limits and loan-to-value ratios restrict the amount of funds that may be loaned to a single borrower. The purpose of those regulations is to limit the financial institution's exposure with respect to a single borrower. It also tends to limit the size of the loan that a single financial institution can make. Loan-to-value regulations establish the minimum collateral margins required for making certain types of loans. Management needs to establish stringent loan evaluation procedures and procedures to ensure that the Corporation adheres to existing lending policies to minimize its credit risk.

98-11 Criteria:

In accordance with Corporation's promissory note provisions, the borrower shall pay to the note holder a late charge of 5% of any monthly installment not received within fifteen (15) days after the installment is due.

Condition:

For 16 of 45 or 36% of cash receipts from loan payments tested, we noted that a late fee of only $5 was being charged to the borrower. This occurrence is pervasive and we were not able to project the cumulative potential loss in late charge revenues.

Cause:

The cause of this condition is unknown.

Effect:

The Corporation improperly applied late fee charges and has lost an undeterminable amount late fee revenues.

Recommendation:

We recommend that GHC begin charging the 5% late fee immediately. This will not only increase the amount of revenues GHC derives, but encourage borrowers to pay in a timely manner. We understand that management has implemented this policy.

98-12 Criteria:

Late payments received from borrowers should be allocated and applied to delinquent and outstanding balances in accordance with Corporation's policy manual Part 3, subpart A, Page 2, Section 3.5(b).

Condition:

In 10 of 45 (or 45%) of the cash receipts tested for loans payments, we noted that the principal, interest and other applications of payments was not being properly applied to borrowers outstanding loan balances. According to the policy manual, Part 3, Subpart A, Page 2, Section 3.5(b) (PF-9); the application of payments should be applied as follows:

98-12 Condition: (continued)

1. Fees
2. Recoverable costs, e.g. legal
3. Accrued interest
4. Trust fund
5. Principal

Cause:

It appears that a software program problem exists as a result of this condition. The software does not appear capable of calculating late payment allocations in accordance with the policies.

Effect:

As a result of this condition, it appears that borrower loan payments are improperly applied to outstanding loan balances and the Corporation may be losing revenues.

Recommendation:

GHC should investigate modifying the existing software on purchasing new software. Payments are currently being applied to principal, interest, and the other older payments. However, the costs and accrued interest should first be satisfied. If the payments were properly allocated first to accrued interest, more interest income would be realized.

Servicing and accounting activities cover the functions relating to initially recording the loan, collecting and recording payments, and reporting loan transactions and balances (including past due loan reports). Poorly designed or ineffective servicing and accounting activities can contribute to increased risk in areas such as credit risk, fraud, insider, operations or management risk. We recommend that management review existing loan servicing and accounting activities as well as policies and procedures to ensure that all delinquent loan payments are properly applied to borrower outstanding loan balances.

## GUAM HOUSING CORPORATION

Schedule of Findings and Questioned Costs
Year Ended September 30, 1998

**Part III – Federal Award Findings and Questioned Costs Section**

CFDA # 14.219
98-13 Criteria:

In accordance with Section V, C.2., of the Subrecipient Agreement between GHURA (grantee) and GHC (subrecipient), and OMB Circular A-133 General Requirements, the subrecipient agreed to and is required to comply with the Davis-Bacon Act. Furthermore, the subrecipient shall maintain documentation that demonstrates compliance with hour and wage requirements applicable to the requirement.

Condition

The subrecipient only had three (3) contracts of which, only one (1) was for actual construction related activities that required review for compliance. The project was awarded to a contractor in the amount of $501,969 (inclusive of change orders) for the renovation and rehabilitation of the Sagan Linahyan project. Based on review of the contractor's file and discussions with the subrecipient and the grantee, Corporation did not perform any compliance monitoring of the contractor nor did Grantee perform its compliance monitoring of the subrecipient to ensure that the contractor adhered to the Davis-Bacon Act requirements. Correspondingly, based on a review of the contract between GHC and Sea Star Group, Inc., it did not contain a prevailing wage rate provision or clause requiring such to be paid to the contractor's laborers.

Cause:

The cause of this condition is unknown.

Effect:

The Corporation is in noncompliance with the Davis-Bacon Act as a result of this condition. There is no effect on the financial statements as a result of this noncompliance finding.

Recommendation:

We recommend that management conduct wage compliance monitoring of its construction contractor to ensure compliance with the Davis-Bacon Act.

Auditee Response/Correction Action Plan:

We concur with the auditor's recommendation and we will implement procedures to ensure compliance with the Davis-Bacon Act requirements.