August 27, 2001

To the Board of Trustees and Management
Government of Guam Retirement Fund
424 Route 8
Maite, Guam 96927

In planning and performing our audit of the financial statements of Government of Guam Retirement Fund for the years ended September 30, 1999 and 1998, we considered the Fund's internal control in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on internal control.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions concerning those matters. A separate report dated August 27, 2001 contains our report on reportable conditions in the Fund's internal control. This letter does not affect our report dated August 27, 2001 on the financial statements of the Government of Guam Retirement Fund.

We have already discussed many of these comments and suggestions with various Fund personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Sincerely,

Controller

In performing this year's audit, we noted conditions that cause us to believe that the Fund is in need of a controller to be responsible for all of the day-to-day accounting, including accounting for investments, contributions, supervising accounting clerical personnel, and preparing monthly financial statements.

Specifically, there are general ledger accounts that include transactions that have not been properly identified. These accounts should be investigated to determine the nature of the items being posted. There are other accounts that need to be reconciled to the underlying details but have not been due to a lack of time.

The accounting manager's duties include creating original source documents (purchase orders, checks, etc.) generating checks, recording the entries into the general ledger, and making adjustments to the general ledger. Usually, there is no review of the accounting manager's work.

We believe that additional controls are needed over the accounting function. We recommend that a controller be retained to authorize accounting transactions, supervise the accounting manager's work, and review financial statements for accuracy. The addition of a controller would increase the controls over the Company's accounting functions and would also be an additional resource for management by providing them with budgets, analyses, and other reports that could be useful in making decisions.

The controllership function should include responsibility for the entire financial area, including implementation of new procedures and control over existing ones, and must include authority for all accounting functions in the following areas:

- Purchasing, accounts payable, and disbursements.
- Contributions and accounts receivable.
- Payroll
- Application of accounting procedures to data processing.
- Management reporting.

We recommend that a controller be hired who would report to the Director. The Controller's duties should be structured so that no one person in the Fund has total control over the accounting system.

Accounting Manager Duties

The Fund does not have a controller at present. The highest level person in the accounting department is an accounting manager. At present, the accounting manager is not provided with sufficient time during the day to carry out all of the required functions.

Based on our observations during the audit, the accounting manager spends a good deal of time answering questions from members, retirees, and government agencies regarding matters which would best be answered by personnel in members or benefits sections. There seems to be a culture within the Fund whereby incoming calls are routinely forwarded to the accounting manager, even if those calls really don't relate to accounting matters.

We recommend that members and benefits personnel try to avoid interrupting the accounting department to the greatest extent possible. Incoming questions that relate to routine non-accounting matters should be handled outside the accounting department.

Investment Section Staffing

The investment section consists of two people at the present time. These two people are responsible for keeping track of movements in the Fund's portfolio, communication with the Fund's consultant, reconciliation of money manager activities with the custodial statements, calculating amortization of premiums and discounts, accounting for securities lending transactions, and for generating all of the necessary correspondence to resolve any questions regarding the investments, among other functions.

Given the volume of activity relating to investments, it appears that this section is understaffed. If there is an excessive workload, employees may be tempted to take shortcuts and to circumvent necessary controls.

The Fund would be better served with the addition of one more qualified person in the investment section. The person should have an accounting background and should be familiar with various types of investment securities. Although this will add expenses to the Fund's operations, the overall performance of the investment section should improve. Reporting should be more timely and accurate, and the investment section will have more time to analyze investment activities and spot anomalies.

Accounting Department Training

In the accounting department, there are only two degreed accountants. Although the people in the department know their functions and perform their functions reasonably well, they don't always realize how their activities relate to the activities of others within the department.

We believe that ongoing training is essential for continuous improvement. We also believe that cross-training is a valuable tool for ensuring that work progresses even if unexpected events occur or if employees must take extended leaves of absence.

We recommend that the Fund should ensure that all employees in the accounting department are cross-trained in other employees' duties. Further, the Fund should institute a continuing education system to ensure that all accounting employees continuously upgrade their skills and knowledge.

These steps will result in more timely, accurate, and comprehensive financial reporting. They will also mitigate the impact of unexpected absences of accounting department employees.

Accounting Manual

We noted that the Fund does not have an accounting procedures manual. The existence of written procedures, instructions, and assignments of duties will prevent or reduce misunderstandings, errors, inefficient or wasted effort, duplicated or omitted procedures, and other situations that can result in inaccurate or untimely accounting records.

A well devised accounting manual can also help to ensure that all similar transactions are treated consistently, that accounting principles used are proper, and that records are produced in the form desired by management. A good accounting manual should aid in the training of new employees and possibly allow for delegation to other employees of some accounting functions management performs.

We recommend that management establish a standard accounting and operating procedures manual outlining policies to be followed. The preparation and maintenance of written standard procedures is very useful to do the following:

The manual should include, along with a chart of accounts, detailed explanations of account content, appropriate descriptions of all accounting procedures and routines, and definitions of job authority and responsibility.

It will take some time and effort for management to develop a manual; however, we believe this time will be more than offset by time saved later in training and supervising accounting personnel. Also, in the process of the comprehensive review of existing accounting procedures for the purpose of developing the manual, management might discover procedures that can be eliminated or improved to make the system more efficient and effective.

Bank Reconciliations

Bank reconciliations were not prepared in a timely manner during the period under audit. Not reconciling the accounts on a monthly basis means that errors or other problems might not be recognized and resolved on a timely basis. Also, it is generally easier and less time-consuming to reconcile accounts while transactions are fresh in mind. We recommend that all bank accounts be reconciled each month prior to preparation of the monthly financial statements.

File Organization

The member and retiree files are not organized in any consistent manner. In computing initial annuities, various documents have to be examined in order to perform the calculations. Given the number of members and retirees and the frequency with which files are accessed, much time could be saved when retrieving information from the files. The cause of this condition seems to be non-standardization of files since the inception of the Fund. We recommend that Fund personnel develop a standardized index system for member and retiree files. All documents in a person's file should be placed in the appropriate section of the file in either document number or chronological order.

Before embarking on this ambitious undertaking, Fund personnel should determine the average length of time needed to organize each file, estimate the time that will be saved by having organized files, and see if it is practical to implement the system.

Penalties on Late Contributions

The Plan document indicates that contributions shall be paid in cash to the Fund within five working days of the payroll issuance date for the salary related to such contributions. Failure to make timely payments by any employer shall cause the Board to invoke the penalties and conditions of GCA Section 8209, but there is no guidance on the rate to be used to calculate penalties. This could lead to disputes over any penalties imposed.

We believe the plan should be amended to include a statutory rate for failure to make timely payments.

DC Plan Administrative Fees

Title 4, Chapter VIII, Article 2, Section 8217 of the GCA allows for the Board to impose administrative fees to be paid by participants. Currently, all DC plan general and administrative costs are borne solely by the DB plan.

General and administrative expenses reflected in the financial statements as being related to the DB plan are overstated and conversely understated for the DC Plan.

We recommend imposing a fee on the DC plan participants to cover related general and administrative expenses. These fees can be used to reimburse the DB Plan.

Suspense Account for Forfeitures

Title 4, Chapter VIII, Article 2, Section 8210 provides that non-vested employer contributions be credited to a suspense account. The suspense account is to be maintained for a period of five years following the termination of the member contemplating a return to employment and reinstatement of the forfeited amount.

In the event that the forfeited amount is not reinstated, the amount attributable to such member will be released and used to offset future employer contributions in an amount proportionate to the respective employer's contributions in the preceding five years.

The plan is approaching the fifth year of existence. It is uncertain if the mechanism is in place to allocate forfeited amounts to the respective employer's future contributions.

DC Plan Duplication of Effort

Funds are transferred to the GGRF along with participant contribution reports. The reports are transmitted to the GGRF in a format that is compatible with the plan administrator's software. GGRF then uploads files to the plan administrator and wires funds. These activities can be easily and possibly more efficiently handled if transmittals occur directly between the various agencies and the plan administrator.

An additional step is created that may not be necessary. This additional procedure is inefficient and is a duplication of efforts. Additional handling increases the potential for errors.

Management should consider having the agencies transmit funds and participant data directly to the plan administrator.