

**STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION
HARBORS DIVISION**

REPORTS ON THE AUDIT OF FEDERAL AWARDS

Fiscal Year Ended June 30, 2002



NISHIHAMA & KISHIDA, C.P.A.'S, INC.

**STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION
HARBORS DIVISION**

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PART I

**AUDITORS' REPORT ON THE SCHEDULE OF
EXPENDITURES OF FEDERAL AWARDS**



NISHIHAMA & KISHIDA, CPA's, INC.
CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITORS' REPORT ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

To the Director
Department of Transportation
State of Hawaii

We have audited the financial statements of the Harbors Division, Department of Transportation of the State of Hawaii relating to the Public Undertaking (Harbors Division) as of and for the fiscal year ended June 30, 2002, and have issued our report thereon dated November 25, 2002. These financial statements are the responsibility of the management of the Harbors Division. Our responsibility is to express an opinion on these financial statements based on our audit.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 25, 2002, on our consideration of the Harbors Division's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audit was performed for the purpose of forming an opinion on the basic financial statements of the Harbors Division taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. 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.

Nishihama & Kishida, CPA's, Inc.

Honolulu, Hawaii
November 25, 2002

State of Hawaii
Department of Transportation
Harbors Division
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Fiscal Year Ended June 30, 2002

<u>Federal Grantor/Pass-through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Federal Expenditures</u>
U.S. Department of Transportation - Federal Highways Administration			
Pass-through from State of Hawaii, Department of Transportation-Highways Division			
Highway Planning and Construction	20.205	FB-0300 NH-0700(42)	\$ 612,543 <u>14,928</u>
TOTAL FEDERAL EXPENDITURES			\$ <u>627,471</u>

Note: The accompanying schedule of expenditures of federal awards is prepared on the cash basis of accounting.

PART II

**AUDITORS' REPORT ON COMPLIANCE AND ON
INTERNAL CONTROL OVER FINANCIAL REPORTING**



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**INDEPENDENT AUDITORS' 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 Director
Department of Transportation
State of Hawaii

We have audited the financial statements of the Harbors Division, Department of Transportation of the State of Hawaii relating to the Public Undertaking (Harbors Division), as of and for the fiscal year ended June 30, 2002, and have issued our report thereon dated November 25, 2002. 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 Harbors Division's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, including applicable provisions of the Hawaii Public Procurement Code (Chapter 103D of the Hawaii Revised Statutes) and procurement rules, directives and circulars, 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 no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Harbors Division'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 judgement, could adversely affect the Harbors Division'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 02-1 through 02-2.

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, of the reportable conditions described above, we consider item 02-1 to be a material weakness.

This report is intended solely for the information and use of management and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Nishihama & Kishida, CPAs, Inc.

Honolulu, Hawaii
November 25, 2002

PART III

**AUDITORS' REPORT ON COMPLIANCE WITH
REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND
INTERNAL CONTROL OVER COMPLIANCE**



NISHIHAMA & KISHIDA, CPA's, INC.
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**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

To the Director
Department of Transportation
State of Hawaii

Compliance

We have audited the compliance of the Harbors Division, Department of Transportation of the State of Hawaii relating to the Public Undertaking (Harbors Division), 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 its major federal program for the fiscal year ended June 30, 2002. The Harbors Division's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of the Harbors Division's management. Our responsibility is to express an opinion on the Harbors Division's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; 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 the Harbors Division'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 on the Harbors Division's compliance with those requirements.

In our opinion, the Harbors Division complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the fiscal year ended June 30, 2002.

Internal Control Over Compliance

The management of the Harbors Division 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 the Harbors Division's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. 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 noncompliance with 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. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Nishihama & Kishida, CPA's Inc.

Honolulu, Hawaii
November 25, 2002

PART IV
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

**Department of Transportation
Harbors Division
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Fiscal Year Ended June 30, 2002**

SECTION I - SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued:	Unqualified
Internal control over financial reporting:	
Material weakness(es) identified?	<input checked="" type="checkbox"/> yes <input type="checkbox"/> no
Reportable condition(s) identified not considered to be material weaknesses?	<input checked="" type="checkbox"/> yes <input type="checkbox"/> none reported
Noncompliance material to the financial statements noted?	<input type="checkbox"/> yes <input checked="" type="checkbox"/> no

Federal Awards

Internal control over major program:	
Material weakness(es) identified?	<input type="checkbox"/> yes <input checked="" type="checkbox"/> no
Reportable condition(s) identified not considered to be material weaknesses?	<input type="checkbox"/> yes <input checked="" type="checkbox"/> none reported

Type of auditors' report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with OMB Circular A-133, Section.510(a)?	<input type="checkbox"/> yes <input checked="" type="checkbox"/> no

Identification of major programs:

CFDA Number

20.205

Name of Federal Program or Cluster

Highway Planning and Construction

Dollar threshold used to distinguish between Type A and Type B programs:	\$300,000
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Auditee qualified as a low-risk auditee?	<input type="checkbox"/> yes <input checked="" type="checkbox"/> no
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**Department of Transportation
Harbors Division
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Fiscal Year Ended June 30, 2002**

SECTION II - FINANCIAL STATEMENT FINDINGS

Ref.

No. Internal Control Findings

02-1 DEVELOP AN INTEGRATED COMPUTERIZED ACCOUNTING SYSTEM

The Harbors Division did not record transactions and close its general ledger for the entire fiscal year ended June 30, 2002 until October 2002. The Harbors Division also relied on a third party to determine depreciation and amortization expense amounts, adjust its general ledger for recurring accrual journal entries, and provide advice on the correct accounting treatment for new bond issues although these accounting issues are common to the Harbors Division. The Harbors Division had encumbrance balances outstanding for several contracts which services were completed many years ago.

In addition, the Harbors Division did not reconcile the accounts receivable and security deposit subsidiary ledgers to the general ledger accounts and did not reconcile the general ledger to the State of Hawaii Financial Accounting and Management Information System's reports for cash and temporary deposits as of June 30, 2002.

The Harbors Division's inability to perform standard accounting procedures such as recording transactions, clearing long outstanding balances, and preparing account reconciliations on a timely basis is primarily due to an inadequate accounting system and staffing problems which have been occurring since January 2001. Although much of the data processing to prepare summary reports for recording in the general ledger and to prepare special reports for management use is done electronically, the process is essentially manual and time-consuming. In addition, inadequate training and vacant positions continued to aggravate the situation.

The Harbors Division is in the process of designing a new computerized accounting system and filling vacant positions to ensure adequate resources are provided and appropriate assignments of responsibilities are completed so that timely and accurate financial information can be prepared.

Recommendation

In designing its new computerized accounting system, the Harbors Division should automate as many routine accounting tasks and integrate the various accounting modules for efficiency where it is feasible, without compromising the adequacy of internal controls. At a minimum, the new computerized accounting system should be able to efficiently record common transactions and accounting entries in the general ledger and perform the necessary calculations needed for recording transactions. The new computerized accounting system should also allow users to easily develop new reports as the need arises. In addition, the Harbors Division should continue to fill vacant positions and provide adequate training to its staff as part of the development of the new computerized accounting system.

**Department of Transportation
Harbors Division
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Fiscal Year Ended June 30, 2002**

**Ref.
No. Internal Control Findings (Continued)**

02-2 RECORD COMPLETED CONSTRUCTION PROJECTS IN THE STATE PROPERTY INVENTORY RECORDS

In previous fiscal years, we noted that the Harbors Division did not record completed construction projects in the state property inventory records since the fiscal year ended June 30, 1995. To date, the Harbors Division has recorded approximately \$25 million of the completed projects but as of June 30, 2002, approximately \$222 million of such assets completed prior to the fiscal year have not been recorded in the state property inventory records.

In addition, several constructed or acquired fixed assets that were demolished were not removed from the state property inventory records because the Harbors Division did not know how to value the disposed assets that were a portion of a larger acquired or constructed asset.

Section 103D-1206 of the Hawaii Revised Statutes states in part, "...the administrative heads of the executive departments, and all other persons, offices, and boards of public character... shall prepare and file with the administrator of the state procurement office an annual inventory return of all state property in the possession, custody, control, or use of the officer making the return, or of the department or office of the government over which the officer presides...."

Recommendation

The Harbors Division should record completed construction projects and remove the disposed assets from the state property inventory records, as appropriate. For the purpose of recording disposed assets, the Harbors Division should consider estimating the value of the demolished fixed asset by discounting the replacement value of such asset.

**Department of Transportation
Harbors Division
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Fiscal Year Ended June 30, 2002**

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

None

PART V
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

STATUS REPORT

This section contains the current status of the prior audit recommendations. The recommendations are referenced to the pages of the previous audit report for the fiscal year ended June 30, 2001, dated November 16, 2001.

Recommendations	Status
<p>01-1 FILL VACANT POSITIONS AND PROVIDE ADEQUATE TRAINING (page 5)</p> <p>The Harbors Division should fill its vacant positions as soon as possible. Adequate training should also be provided for its personnel.</p> <p>In addition, once the new computerized accounting system is operational, the Harbors Division should create an accounting manual so that employees have a reference source on how they should be performing any newly assigned task.</p>	<p>Not accomplished. See Internal Control Finding 02-1.</p>
<p>01-2 RECORD COMPLETED CONSTRUCTION PROJECTS IN THE STATE PROPERTY INVENTORY RECORDS (page 7)</p> <p>The Harbors Division should record completed construction projects in the state property inventory records.</p>	<p>Partially accomplished. However, see Internal Control Finding 02-2 relating to completed construction projects.</p>

PART VI
RESPONSE OF THE AFFECTED AGENCY

LINDA LINGLE
GOVERNOR



RODNEY K. HARAGA
DIRECTOR

Response of the Harbors Division, Department of Transportation.

GLENN M. OKIMOTO
Acting Deputy Director

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION
HARBORS DIVISION
79 SO. NIMITZ HWY. • HONOLULU, HAWAII 96813-4898

IN REPLY REFER TO:

HAR-SF 6011.03

March 11, 2003

Mr. Ronald Shiigi
Nishihama & Kishida, CPA's, Inc.
Pacific Tower
1001 Bishop Street, Suite 1760
Honolulu, Hawaii 96813-3696

Dear Mr. Shiigi:

We have reviewed the draft of the reports on the audit of Federal Awards for the fiscal year ended June 30, 2002. Attached is the corrective action plan.

Very truly yours,

A handwritten signature in cursive script that reads "Gerald Morita".

Gerald Morita
Fiscal Officer

Att.

This is our response to the reportable conditions 02-1 and 02-2.

02-1 Develop an integrated computerized accounting system

Completion and implementation of a new fully automated accounting system will correct many of the problems mentioned in this finding. One of the many modules in this package is a fully integrated general ledger. The revenue transactions in summary will be automatically posted to the general ledger from the accounts receivable module. Other modules will automatically post transactions to the accounts receivable module. These modules include vessel management (dockage, port entry, electricity, water and cleaning charges), property management (rents and leases), parking management (parking fees), and agent accounts receivable (wharfage fees). The expenditures will be automatically posted to the general ledger from the download from the State of Hawaii Financial Accounting Management Information System. Also, the General Ledger Module will have a depreciation and amortization program, which will allow the Harbors Division to determine its own depreciation and amortization expense. The new system will generate accrual accounting reports and audit work papers. The Consultant firm who is developing and implementing this computer system is also providing training. The Harbors employee who is responsible for the module will be responsible for future training. Also, the Division has a vacant position, which will assist in the reconciliation of accounts and the closing of the general ledger on a timely basis. The Division believes that the completion of this accounting system and the filling of their vacant position will correct the reportable conditions.

02-2 Record completed construction projects in the state property inventory records

The Financial Management Section will be coordinating with the Engineering Branch to formally provide all necessary information to properly record fixed asset additions. We will consider estimating the value of the demolished fixed asset for the purpose of recording disposed assets.