



CERTIFIED PUBLIC ACCOUNTANTS

State of Hawaii
Department of Health
Financial and Compliance Audit
June 30, 2007

Submitted by
The Auditor
State of Hawaii

Quality

Integrity

Insight

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 Department of Health
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Report of Independent Auditors

The Auditor
State of Hawaii

In our opinion, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Hawaii, Department of Health (the "Department") which collectively comprise the Department's basic financial statements as listed in the index, present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Department at June 30, 2007, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Department's management. Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit of these statements 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1 to the basic financial statements, the basic financial statements of the Department are intended to present the financial position and the changes in financial position and cash flows, where applicable, of only that portion of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Hawaii that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State of Hawaii as of June 30, 2007, and the changes in its financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 8 to the basic financial statements, certain errors resulting in understatement of the previously reported governmental activities net assets and governmental funds fund balance as of June 30, 2006, were discovered by management of the Department during the current year. Accordingly, the fiscal year 2006 financial statements have been restated and an adjustment has been made to department-wide net assets and governmental funds fund balance as of July 1, 2006 to correct the error.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 28, 2008 on our consideration of the Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The accompanying management's discussion and analysis and budgetary comparison information on pages 3 through 13 and 37 through 41 are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by the 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. As described in Note 1 to the Schedule of Expenditures of Federal Awards, the accompanying schedule of expenditures of federal awards was prepared on the cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. 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 on the basis of accounting described in Note 1, in relation to the basic financial statements taken as a whole.

Accuity LLP

Honolulu, Hawaii
March 28, 2008

State of Hawaii
Department of Health
Management's Discussion and Analysis (Unaudited)
June 30, 2007

This Management Discussion and Analysis ("MD&A") presents a narrative overview and analysis of the financial activities and performance of the State of Hawaii Department of Health (the "Department") during the fiscal year that ended on June 30, 2007. Please read it in conjunction with the Department's Financial Statements including its related notes (which follow this section) as well as the following subsequent two sections which are: Required Supplementary Information Other than MD&A; and a Schedule of Expenditures of Federal Awards ("SEFA"). The following is a brief description of the contents of those three sections:

Overview of the Financial Statements

This MD&A serves as an introduction to the Department's basic financial statements. The basic financial statements are comprised of three components: (1) department-wide financial statements; (2) fund financial statements; and (3) notes to the basic financial statements.

Department-wide Financial Statements

The department-wide financial statements provide information about the Department's overall financial position and results of operations. These statements, which are presented on an accrual basis of accounting, consist of the Statement of Net Assets and the Statement of Activities.

The department-wide statements report information about the Department as a whole using accounting methods similar to those used by private sector companies. The statement of net assets provides both short-term and long-term information about the Department's financial position, which assists in assessing the Department's economic condition at the end of the fiscal year. All of the current year revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid. The department-wide financial statements include two statements:

- The *Statement of Net Assets* presents all of the Department's assets and liabilities, with the difference between the two reported as "net assets." Over time, increases and decreases in the Department's net assets may serve as a useful indicator of whether the financial position of the Department is improving or deteriorating.
- The *Statement of Activities* presents information showing how the Department's net assets changed during the most recent fiscal year.

The department-wide financial statements of the Department are further divided into two categories:

- *Governmental activities* –The activities in this section are primarily supported by State of Hawaii appropriations, funds from the tobacco settlement, beverage container deposit administrative fees, federal grants, and fees.
- *Business-type activities* –These functions normally are intended to recover all or a significant portion of their costs through user's fees and charges to external users. These activities include the Department's two revolving loan funds.

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Fund Financial Statements

The fund financial statements include the Department's: (1) governmental funds, for which activities are funded primarily from appropriations from the State of Hawaii, by revenues from the tobacco settlement agreement, beverage container deposit program and federal grants; (2) proprietary funds, which consist of revolving loan funds and are reported similar to business activities; and (3) fiduciary funds. The governmental funds are presented on a modified accrual basis of accounting. The proprietary and the fiduciary funds are presented on an accrual basis of accounting.

The fund financial statements provide more detailed information about the Department's most significant funds and not the Department as a whole. In these statements, the financial activities of the Department are recorded in individual funds. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Department uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. Funds are reported as a major fund or a non-major (other) fund. The Governmental Accounting Standards Board ("GASB") issued Statement 34, *Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments*, which sets forth the minimum criteria for the determination of major funds. The non-major funds are combined in a column in the fund financial statements.

To reiterate, the Department has three types of funds:

- *Governmental funds* – Governmental funds are used to account for essentially the same functions reported in the governmental activities in the department-wide financial statements. However, unlike the department-wide financial statements, governmental financial statements focus on near-term inflows and outflows of expendable resources as well as on the balances of expendable resources available at the end of the fiscal year.

Because the focus of governmental funds is narrower than that of the department-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the department-wide financial statements. Both the governmental fund balance sheet and statement of revenues, expenditures, and changes in fund balance provide a reconciliation to facilitate comparison between governmental funds and governmental activities in the department-wide financial statements.

- *Proprietary funds* – Proprietary funds are used to report activities that operate more like those of commercial enterprises. They are known as enterprise funds because they charge fees for services provided to outsiders. They are used to report the same functions presented as business-type activities in the department-wide financial statements. The Department uses enterprise funds to account for the operations of its two revolving loan funds each of which are considered to be major funds of the Department.
- *Fiduciary funds* – The fiduciary funds account for net assets held in a trustee or agent capacity for others. These funds are not reflected in the department-wide financial statements since these resources are not available to support the Department's programs.

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Notes to Financial Statements

The *Notes to Financial Statements* section provides additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements follow the basic financial statements.

Required Supplementary Information

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information. This section includes a budgetary comparison schedule, which includes reconciliations for the general fund, tobacco settlement fund, and deposit beverage container fund, comparing the excess of revenues over expenditures presented on a budgetary basis to the excess (deficiency) of revenues over expenditures presented in conformity with generally accepted accounting principles ("GAAP") as presented in the governmental fund financial statements. This management's discussion and analysis is also Required Supplementary Information that is required to be presented preceding the financial statements.

Schedule of Expenditures of Federal Awards

Other information consists of the Schedule of Expenditures of Federal Awards and the Notes to the Schedule of Expenditures of Federal Awards. The SEFA reports federal awards to the Department expended on the cash basis of accounting for the year ended June 30, 2007.

Financial Highlights

- The financial information for fiscal year ("FY") 2006 has been restated to correct the Department's appropriations and receivables reported in the Department's FY 2006 financial statements. The FY 2006 amounts in the MD&A are the restated balances (see Note 8).
- The Department's total net assets increased from \$524.4 million as of June 30, 2006 to \$604.0 million as of June 30, 2007, or by approximately \$79.6 million. The total increase in net assets was attributed to an increase in the Department's business type activities' net assets of \$83.6 million and a decrease in governmental activities' net assets of \$4.0 million during the year.
- The Department's governmental funds reported an aggregate increase in fund balance of \$6.4 million during the year totaling \$134.4 million at June 30, 2007. Note that this is based on the adjusted fund balance at June 30, 2006 of \$128.0 million.
- The Department's proprietary funds, consisting of two revolving loan funds, reported an increase in net assets of \$83.7 million for FY 2007. Total net assets were \$407.0 million at June 30, 2007 compared to the FY 2006 year end total of \$323.3 million.

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Department-Wide Financial Analysis

This section includes condensed Department-wide financial information and analysis.

Statement of Net Assets
June 30,
(\$000)

| | Governmental Activities | | Business-Type Activities | | Total | |
|---|--------------------------------|----------------------------|---------------------------------|-------------------|-------------------|----------------------------|
| | 2007 | 2006 (restated) | 2007 | 2006 | 2007 | 2006 (restated) |
| Current assets | \$ 276,373 | \$ 257,143 | \$ 196,486 | \$ 182,060 | \$ 472,859 | \$ 439,203 |
| Capital assets | 67,285 | 68,792 | 287 | 302 | 67,572 | 69,094 |
| Loans receivable, noncurrent | - | - | 210,621 | 141,048 | 210,621 | 141,048 |
| Total assets | \$ 343,658 | \$ 325,935 | \$ 407,394 | \$ 323,410 | \$ 751,052 | \$ 649,345 |
| Current liabilities | \$ 130,144 | \$ 109,274 | \$ 204 | \$ 89 | \$ 130,348 | \$ 109,363 |
| Long term liabilities | 16,481 | 15,588 | 215 | - | 16,696 | 15,588 |
| Total liabilities | 146,625 | 124,862 | 419 | 89 | 147,044 | 124,951 |
| Net assets | | | | | | |
| Invested in capital assets | 67,285 | 68,792 | 287 | 302 | 67,572 | 69,094 |
| Restricted | 128,138 | 131,809 | 406,688 | 323,019 | 534,826 | 454,828 |
| Unrestricted | 1,610 | 472 | - | - | 1,610 | 472 |
| Total net assets | 197,033 | 201,073 | 406,975 | 323,321 | 604,008 | 524,394 |
| Total liabilities and net assets | \$ 343,658 | \$ 325,935 | \$ 407,394 | \$ 323,410 | \$ 751,052 | \$ 649,345 |

As noted earlier, changes in net assets may serve over time as a useful indicator of the Department's financial position. As of June 30, 2007, the Department's total net assets were approximately \$604.0 million.

At June 30, 2007, in addition to cash in the state treasury approximating \$313.3 million, the Department had total loan receivables from county governments in the amount of \$229.9 million arising from its two revolving loan funds. The Department had total liabilities of \$147.0 million at June 30, 2007 of which \$10.3 million relates to accrued wages and employee benefits payable. Approximately \$74.4 million in liabilities relate to vouchers and contracts payable. At June 30, 2007, restricted net assets were \$534.8 million. The restrictions arise from legal and contractual agreements.

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Statement of Activities
June 30,
(\$000)

| | Governmental Activities | | Business-Type Activities | | Total | |
|--------------------------------------|------------------------------------|----------------------------|-------------------------------------|---------------|----------------|----------------------------|
| | 2007 | 2006 (restated) | 2007 | 2006 | 2007 | 2006 (restated) |
| Revenue | | | | | | |
| Program revenues | | | | | | |
| Charges for services | \$ 43,616 | \$ 41,556 | \$ 6,008 | \$ 5,643 | \$ 49,624 | \$ 47,199 |
| Operating grants and contributions | 118,923 | 110,083 | 76,400 | 11,497 | 195,323 | 121,580 |
| General revenues | | | | | | |
| State appropriated funds | 445,079 | 407,547 | - | - | 445,079 | 407,547 |
| No imposed fringe benefits | 47,303 | 44,722 | - | - | 47,303 | 44,722 |
| Tobacco settlement funds | 45,507 | 34,063 | - | - | 45,507 | 34,063 |
| Environmental fees and taxes | 25,011 | 24,365 | - | - | 25,011 | 24,365 |
| Total revenues | 725,439 | 662,336 | 82,408 | 17,140 | 807,847 | 679,476 |
| Expenses | | | | | | |
| General administration | 34,729 | 29,953 | - | - | 34,729 | 29,953 |
| Environmental health | 65,692 | 59,487 | 2,468 | 2,152 | 68,160 | 61,639 |
| Behavior health | 273,790 | 244,245 | - | - | 273,790 | 244,245 |
| Health resources | 368,892 | 290,760 | - | - | 368,892 | 290,760 |
| Total expenses | 743,103 | 624,445 | 2,468 | 2,152 | 745,571 | 626,597 |
| Excess (deficiency) before transfers | (17,664) | 37,891 | 79,940 | 14,988 | 62,276 | 52,879 |
| Transfers | 13,624 | (4,048) | 3,714 | 3,714 | 17,338 | (334) |
| Change in net assets | (4,040) | 33,843 | 83,654 | 18,702 | 79,614 | 52,545 |
| Net assets | | | | | | |
| Beginning of year, as restated | 201,073 | 167,230 | 323,321 | 304,619 | 524,394 | 471,849 |
| End of year | \$ 197,033 | \$ 201,073 | \$ 406,975 | \$ 323,321 | \$ 604,008 | \$ 524,394 |

Governmental activities decreased the Department's net assets by \$4.0 million in FY 2007. There was an increase in the State appropriated funds of \$37.5 from FY 2006 to FY 2007 because of a significant increase in expenses for the Department. The increase was partially due to a \$7.1 million increase in the expenditures of the Tobacco Settlement Special Fund related to contracts executed and expended in FY 2007 which had been delayed from FY 2006. Also in FY 2007 the Department received emergency appropriations in the amount of \$4.4 million for the Early Intervention Services, \$1.4 million for Emergency Medical Services and \$5.0 million for the Developmental Disabilities programs which also contributed to the increase in expenditures.

Revenues of the Department's business-type activities, which increased by \$65.3 million from 2006, consist of the Department's environmental loan programs — one for water pollution control and the other for drinking water treatment — were generated from charges for services, program investment income, and federal assistance program funds as well as state matching funds. Charges for services consist primarily of administration loan fees and interest income on loans related to the Department's two revolving loan programs. The majority of the program investment income is from income earned from participation in the State Treasury Investment Pool System. In FY 2007, there was a significant increase

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in revenue from the environment health loan programs due to an increase in Federal contributions which provided funding for new loans.

For the fiscal year ending June 30, 2007, business-type activities increased the Department's net assets by \$79.9 million before transfers whereas in FY 2006, the increase was only approximately \$15.0 million before transfers. The key element this fiscal year over FY 2006 was due in large part to the increase of \$64.9 million in operating grants and contributions over FY 2006.

Total Department-wide expenses for FY 2007 were \$745.6 million of which \$743.1 million was for governmental activities. Overall the Department is organized into four major administrations.

Financially, the largest administration is the Health Resources Administration that expended approximately 49.7% of all expenses. FY 2007 expenditures for this Administration increased \$78.1 million over FY 2006. Major programs included in this administration include:

- Developmental Disabilities Division that services disabled clients in the State while addressing the conditions of the Makin Settlement;
- Family Health Services Division ("FHSD") that administers the State's Healthy Start and Early Intervention programs for children zero to three in compliance with the Federal Individual with Disabilities Education Act, Part C as well as serving children, youth and families through its three branches;
- Community Health Division that provides Public Health Nursing Services and in concern with the two programs of the FHSD continuing to provide services necessary to meet the requirements of the settled Felix lawsuit;
- Emergency Medical Services and Injury Prevention Control System Branch that includes the State's mandated Emergency Medical Services funds, the majority of which is used to operate the State's emergency ambulance service in the four major counties;
- Tobacco Settlement Project/Healthy Hawaii Initiative entity which seeks to prevent chronic diseases such as heart disease, cancer and diabetes utilizing tobacco settlement funds for programs that work to decrease tobacco use, improve nutrition and promote physical activities;
- Communicable Disease Division which provides tuberculosis control, Hansen's disease control programs in the community and at Kalaupapa, and STD/AIDS prevention services;
- Disease Outbreak Control Division which utilizes State and Federal bioterrorism funds for emergency response to disease outbreaks; and
- Dental Health Division which is the smallest division in this administration and implements a dental hygiene program in the public schools and provides public health dental services to the State's disabled clientele.

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This administration provides a wide array of public health services in addition to meeting the court settlement conditions, which results in the expenditure of a high percentage of departmental funds. In addition, the increase in expenditures is due to a change in the accounting procedures for the Developmental Disabilities Division Title XIX (aka Medicaid) Waiver Home & Community Based Services ("HCBS") Program. In FY 2006, a U fund account was established to track the Department of Human Service's ("DHS") portion of the total expenditures for the Title XIX HCBS Program. In FY 2007, the expenditures for the Department of Human Service's portion was \$46 million. Their portion was established at 58%, of the total expenditures with the Department of Health's portion being 42%.

The Behavioral Health Services Administration expended a significant 36.8% of departmental funds with an increase of \$29.5 million over FY 2006. This administration is responsible for providing available and coordinated mental health and substance abuse treatment and prevention programs. Programs within this administration are:

- Adult Mental Health Division ("AMHD") that includes the Hawaii State Hospital and Community Mental Health Center Branches;
- Child and Adolescent Mental Health Division ("CAMHD") which includes seven Family Guidance Centers and the Family Court Liaison Branches; and
- Alcohol and Drug Abuse Division ("ADAD") which plans for and purchases substance abuse prevention and treatment services for adolescents and adults.

A portion of the increase in expenditures is attributed to the AMHD's continuing efforts to identify, place and treat eligible clients. In FY 2007, AMHD serviced 13545 clients as compared to the 12,245 clients serviced in FY 2006. AMHD's Access Line continues to provide the community with a resource site for information as well as a referral point for possible clients. CAMHD continues to respond to the ongoing requirements of the settled Felix case, while ADAD is responsible to the "Ice" (nickname for methamphetamine) initiative and the expenditure of the additional appropriated funds.

The Environmental Health Administration is responsible for the management of the clean air, clean water, solid and hazardous waste, public sanitation, vector control, and purity of food and drugs. It expended approximately 8.8% of the departmental funds with an increase of \$6.2 million expended over FY 2006. This increase in expenditures is mainly due to the public's continued acceptance and participation of the Beverage Container Deposit Program. This program continues to expand every year with increasing amounts being recycled resulting in related costs increasing. Other programs in this administration are heavily federally funded through the Environmental Protection Agency. This administration also manages both the Water Pollution Control Revolving and the Drinking Water Treatment Revolving Loan Funds.

Finally, General Administration provides the overall leadership and oversight for the Department. It includes administrative support staff, three district health offices, and five administratively attached agencies. This administration expends approximately 4.7% of the departmental funds.

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The following table presents revenues and expenditures of the governmental funds for FY 2007 and FY 2006 (\$000):

| | 2007 | 2006 (restated) |
|---|-------------|----------------------------|
| Revenues | | |
| State general fund allotments | \$ 445,079 | \$ 407,547 |
| Nonimposed fringe benefits | 47,303 | 44,722 |
| Tobacco settlement funds | 36,507 | 34,863 |
| Deposit beverage container program | 22,588 | 21,868 |
| Intergovernmental | 108,768 | 111,792 |
| Taxes, fees, fines and other | 50,844 | 46,547 |
| Investment income | 5,431 | 3,992 |
| Total revenues | 716,520 | 671,331 |
| Expenditures | | |
| General administration | 35,032 | 28,933 |
| Environmental health | 65,129 | 58,550 |
| Behavioral health | 270,926 | 242,232 |
| Health resources | 367,820 | 301,319 |
| Total expenditures | 738,907 | 631,034 |
| Excess (deficiency) revenues over expenditures before transfers | \$ (22,387) | \$ 40,297 |

The governmental funds revenue consist of the Department's general fund, tobacco settlement funds, deposit beverage container funds, intergovernmental (federal) funds, taxes, fees, fines and investment income.

During the fiscal year ended June 30, 2007, general fund revenues were \$486.3 million, including \$47.3 million for fringe benefits paid directly from the State General Fund. General fund expenditures were \$479.7 million, including the \$47.3 million for fringe benefits discussed above.

For FY 2007, the tobacco settlement fund earned revenues of \$37.8 million, including investment income of \$1.3 million. \$22.1 million was transferred to other State departments and agencies of which \$8.3 million was for the State's Emergency and Budget Reserve Fund (a.k.a. Rainy Day Fund), and \$9.6 million was for the University of Hawaii to assist in financing the construction of the new medical school facility in Kakaako.

In FY 2007, the deposit beverage container fund collected \$22.6 million in beverage container deposit administrative fees. Of this amount received, \$20.1 million was paid to recycling centers, or utilized to fund the program. The bottle bill fund collected \$34.8 million in deposits from distributors and repaid \$30.5 million in deposits to consumers during FY 2007.

The proprietary funds consist of two funds: Water Pollution Control Revolving Fund and Drinking Water Treatment Revolving Loan Fund and are reported in the statement of net assets and statement of activities as business-type activities.

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The Water Pollution Control Revolving Fund accounts for federal and state funds used to provide loans to county governments for the construction of wastewater treatment facilities and the repayment of principal, interest and fees from such loans and investment of such moneys. During FY 2007, this fund received \$49.3 million and \$2.1 million of federal and state funds, respectively. The fund also disbursed \$63.5 million in loan proceeds and collected \$13.1 million in principal repayments in 2007. As compared to 2006, the fund disbursed \$3.6 million in loan proceeds and collected \$11.4 million in principal payments.

The Drinking Water Treatment Revolving Loan Fund accounts for federal and state match funds used to provide loans and other types of financial assistance to public water systems for drinking water infrastructure and the repayment of principal interest and fees from such loans and the investment of such moneys. During FY 2007, this fund received \$21.4 million and \$1.7 million of federal and state funds, respectively. The fund also disbursed \$25.1 million in loan proceeds and collected \$1.2 million in principal repayments in 2007. As compared to 2006, the fund disbursed \$4.0 million in loan proceeds and collected \$0.8 million in principal payments.

The Department accounts for funds held as an agent and/or trustee for certain individuals in the fiduciary funds.

Budgetary Analysis

The following budget information relates to the general fund, tobacco settlement fund, and deposit beverage container fund for 2007.

| | Budgeted Amounts (\$000) | | Actual on a Budgetary Basis (\$000) |
|--|-------------------------------------|--------------|--|
| | Original | Final | |
| General fund | | | |
| Revenues | \$ 431,383 | \$ 440,104 | \$ 438,051 |
| Expenditures | | | |
| General administration | 23,231 | 24,903 | 24,682 |
| Environmental health | 18,584 | 18,726 | 18,505 |
| Behavioral health | 197,829 | 201,519 | 200,678 |
| Health resources | 191,739 | 194,956 | 194,186 |
| Tobacco settlement fund | | | |
| Revenues | 43,143 | 43,184 | 37,733 |
| Expenditures | 43,143 | 43,184 | 39,023 |
| Deposit beverage container fund | | | |
| Revenues | 62,187 | 62,201 | 57,770 |
| Expenditures | 62,187 | 62,201 | 59,572 |

The differences between the original budget and final expenditures for the general fund were primarily due to the delay in hiring on vacant positions of many programs throughout the Department. Other differences occurred due to contracts being delayed, and lower than expected caseloads for services. The actual expenditures of the general fund were approximately \$2.1 million less than the final budgeted expenditures.

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For the tobacco settlement fund, the \$39.0 million expended in FY 2007 on a budgetary basis was \$1.3 million more than the actual revenues received. This was primarily due to using the "excess" revenues from FY 2006 to execute and expend contracts delayed in FY 2006.

The deposit beverage container program was fully implemented in January 2005 with the public's redemption of empty containers. It received revenues from the program's administrative fees of \$22.5 million, \$0.7 million more than in 2006 due to an increase in the number of deposit beverage containers actually sold. In fiscal year 2006, 930,353,658 containers were sold. This amount rose to 936,412,347 in fiscal year 2007.

Capital Assets

As of June 30, 2007, the Department's governmental activities had invested approximately \$67.3 million (net of accumulated depreciation) in a broad range of capital assets. This amount represents a decrease of about \$1.5 million. The decrease is primarily related to depreciation expense which approximated \$5.6 million, offset by the \$4.3 million in additions purchased in the current year. See Note 3 to the Department's financial statements for a description of capital assets activities for the fiscal year ended June 30, 2007.

Capital Assets
Governmental Activities
June 30,
(\$000)

| | 2007 | 2006 |
|--------------------------------|------------------|------------------|
| Land | \$ 1,018 | \$ 1,018 |
| Land and building improvements | 134,145 | 134,031 |
| Furniture and equipment | <u>19,454</u> | <u>16,239</u> |
| Total | 154,617 | 151,288 |
| Accumulated depreciation | <u>87,332</u> | <u>82,496</u> |
| Total capital assets, net | <u>\$ 67,285</u> | <u>\$ 68,792</u> |

Currently Known Facts, Decisions, or Conditions

The Department continues to face numerous challenges in mental health, developmental disabilities and emergency preparedness and has worked hard to meet these challenges to improve the overall health of the people of our state and to prepare the State for various emergency situations.

Much has been accomplished in improving the adult mental health system statewide. However, the number of consumers with severe and persistent mental illness continues to increase. The number of adult consumers increased from 12,200 in FY 2006 to 14,492 in FY 2007. Continued evaluation of the service delivery system and program operations will be made to achieve operational efficiencies.

Similarly, in the developmental disabilities program, the number of clients continues to increase by about 200 clients each year. Further, the Federal Matching Assistance Percentage ("FMAP") decreased from 57.55% to 56.50% effective October 1, 2007. This means that the state match requirement increases by 1.05%. Also, the FY 2007 end Average Cost per Client ("APC") increased from \$38,414 to \$39,188. These factors all contribute to the need for additional resources to serve the developmentally disabled.

State of Hawaii
Department of Health
Management's Discussion and Analysis (Unaudited)
June 30, 2007

Preparedness response is also an integral part of maintaining a safe and healthy environment for our communities throughout the State. The Department has worked hard to develop and implement response plans to ensure that our state will be ready to respond to any and all types of emergency situations. Recently, Hawaii scored 9 out of 10 in a national report rating each state's level of preparedness to handle disease outbreaks, bioterrorism attacks or other public health emergencies. Our state was one of sixteen states that were rated adequate in 9 out of 10 categories. Only seven states were rated adequate in all 10 categories.

And lastly, the Water Pollution Control Revolving Fund and the Drinking Water Treatment Revolving Loan Fund expect to execute a total of 13 loan agreements in the amount of \$58.7 million and 11 loan agreements for \$29.2 million respectively during FY 2008.

State of Hawaii
Department of Health
Statement of Net Assets
June 30, 2007

| | Governmental Activities | Business-Type Activities | Total |
|---|----------------------------|-----------------------------|-----------------------|
| Assets | | | |
| Current assets | | | |
| Equity in cash and cash equivalents in State Treasury | \$ 140,716,622 | \$ 172,599,947 | \$ 313,316,569 |
| Receivables | | | |
| Due from State Treasury | 66,771,558 | - | 66,771,558 |
| Due from other State agencies | 32,273,422 | - | 32,273,422 |
| Accrued interest and loan fees | 1,230,480 | 3,682,256 | 4,912,736 |
| Accounts receivable | 1,776,075 | - | 1,776,075 |
| Due from Federal government | 7,097,963 | 486,487 | 7,584,450 |
| Internal balances | (392,700) | 392,700 | - |
| Tobacco settlement receivable | 26,900,000 | - | 26,900,000 |
| Current maturities of loans receivable | - | 19,324,985 | 19,324,985 |
| | <u>135,656,798</u> | <u>23,886,428</u> | <u>159,543,226</u> |
| Total current assets | 276,373,420 | 196,486,375 | 472,859,795 |
| Loans receivable, net of current maturities | - | 210,620,901 | 210,620,901 |
| Capital assets, net of accumulated depreciation | 67,284,555 | 287,154 | 67,571,709 |
| Total assets | <u>\$ 343,657,975</u> | <u>\$ 407,394,430</u> | <u>\$ 751,052,405</u> |
| Liabilities and Net Assets | | | |
| Current liabilities | | | |
| Vouchers and contracts payable | \$ 74,298,211 | \$ 89,258 | \$ 74,387,469 |
| Accrued wages and employee benefits payable | 10,168,600 | 92,158 | 10,260,758 |
| Accrued vacation, current portion | 8,600,296 | 22,700 | 8,622,996 |
| Workers' compensation liability | 601,540 | - | 601,540 |
| Deferred income | 254,096 | - | 254,096 |
| Due to State of Hawaii | 23,198,882 | - | 23,198,882 |
| Beverage container deposits | 13,022,901 | - | 13,022,901 |
| Total current liabilities | <u>130,144,526</u> | <u>204,116</u> | <u>130,348,642</u> |
| Accrued vacation, net of current portion | 16,480,765 | 214,936 | 16,695,701 |
| Commitments and contingencies | | | |
| Net assets | | | |
| Investment in capital assets | 67,284,555 | 287,154 | 67,571,709 |
| Restricted for | | | |
| Loans | - | 406,688,224 | 406,688,224 |
| Tobacco prevention and control | 31,022,207 | - | 31,022,207 |
| Capital projects | 8,496,848 | - | 8,496,848 |
| Other purposes | 88,618,675 | - | 88,618,675 |
| Unrestricted | 1,610,399 | - | 1,610,399 |
| Total net assets | <u>197,032,684</u> | <u>406,975,378</u> | <u>604,008,062</u> |
| Total liabilities and net assets | <u>\$ 343,657,975</u> | <u>\$ 407,394,430</u> | <u>\$ 751,052,405</u> |

The accompanying notes are an integral part of this statement.

**State of Hawaii
Department of Health
Statement of Activities
Year Ended June 30, 2007**

| Functions/Programs | Program Revenues | | | Net (Expense) Revenue and Changes in Net Assets | | |
|--|------------------|----------------------|------------------------------------|---|--------------------------|-----------------|
| | Expenses | Charges for Services | Operating Grants and Contributions | Primary Government | | |
| | | | | Governmental Activities | Business-Type Activities | Total |
| Primary government | | | | | | |
| Governmental activities | | | | | | |
| General administration | \$ 34,729,633 | \$ 280,699 | \$ 8,762,899 | \$ (25,686,035) | \$ - | \$ (25,686,035) |
| Environmental health administration | 65,692,129 | 6,336,379 | 13,247,074 | (46,108,676) | - | (46,108,676) |
| Behavioral health services administration | 273,790,294 | 28,191,320 | 16,110,855 | (229,488,119) | - | (229,488,119) |
| Health resources administration | 368,891,652 | 8,807,308 | 80,801,959 | (279,282,385) | - | (279,282,385) |
| Total governmental activities | 743,103,708 | 43,615,706 | 118,922,787 | (580,565,215) | - | (580,565,215) |
| Business-type activities | | | | | | |
| Environmental health loan programs | 2,468,422 | 6,007,563 | 76,401,292 | - | 79,940,433 | 79,940,433 |
| Total business-type activities | 2,468,422 | 6,007,563 | 76,401,292 | - | 79,940,433 | 79,940,433 |
| Total primary government | \$ 745,572,130 | \$ 49,623,269 | \$ 195,324,079 | (580,565,215) | 79,940,433 | (500,624,782) |
| General revenues | | | | | | |
| State general fund allotments, net | | | | 445,078,814 | - | 445,078,814 |
| Nonimposed employee fringe benefits | | | | 47,303,098 | - | 47,303,098 |
| Environmental response tax | | | | 1,741,311 | - | 1,741,311 |
| Deposit beverage container fee | | | | 22,588,027 | - | 22,588,027 |
| Advance glass disposal fee | | | | 681,466 | - | 681,466 |
| Tobacco settlement funds | | | | 45,507,167 | - | 45,507,167 |
| Transfers | | | | 13,624,658 | 3,714,000 | 17,338,658 |
| Total general revenues and transfers | | | | 576,524,541 | 3,714,000 | 580,238,541 |
| Change in net assets | | | | (4,040,674) | 83,654,433 | 79,613,759 |
| Net assets at July 1, 2006, as previously reported | | | | 175,207,506 | 323,320,945 | 498,528,451 |
| Prior period adjustment | | | | 25,865,852 | - | 25,865,852 |
| Net assets at July 1, 2006, as restated | | | | 201,073,358 | 323,320,945 | 524,394,303 |
| Net assets at June 30, 2007 | | | | \$ 197,032,684 | \$ 406,975,378 | \$ 604,008,062 |

The accompanying notes are an integral part of this statement.

**State of Hawaii
Department of Health
Governmental Funds
Balance Sheet
June 30, 2007**

| | General | Tobacco Settlement | Deposit Beverage Container | Other Funds | Total Governmental |
|---|---------------|--------------------|----------------------------|---------------|--------------------|
| Assets | | | | | |
| Equity in cash and cash equivalents in State Treasury | \$ - | \$ 35,992,053 | \$ 37,173,519 | \$ 67,551,050 | \$ 140,716,622 |
| Due from State Treasury | 56,868,192 | - | - | 9,903,366 | 66,771,558 |
| Due from other State agencies | - | - | - | 17,954,472 | 17,954,472 |
| Internal balances | 17,954,472 | - | - | (17,954,472) | - |
| Accrued interest receivable | - | 373,113 | 293,474 | 563,893 | 1,230,480 |
| Accounts receivable | - | - | 1,776,075 | - | 1,776,075 |
| Due from Federal government | - | - | - | 7,097,963 | 7,097,963 |
| Total assets | \$ 74,822,664 | \$ 36,365,166 | \$ 39,243,068 | \$ 85,116,272 | \$ 235,547,170 |
| Liabilities and Fund Balances | | | | | |
| Liabilities | | | | | |
| Vouchers and contracts payable | \$ 46,219,719 | \$ 5,628,186 | \$ 4,447,904 | \$ 14,639,902 | \$ 70,935,711 |
| Accrued wages and employee benefits | 7,807,652 | 90,191 | 30,433 | 2,240,324 | 10,168,600 |
| Deferred income | - | - | - | 254,096 | 254,096 |
| Due to State of Hawaii | 36,800 | 6,349,582 | - | - | 6,386,382 |
| Due to other funds | - | - | - | 392,700 | 392,700 |
| Beverage container deposits | - | - | 13,022,901 | - | 13,022,901 |
| Total liabilities | 54,064,171 | 12,067,959 | 17,501,238 | 17,527,022 | 101,160,390 |
| Fund balance | | | | | |
| Reserved for encumbrances | 35,839,310 | 9,534,543 | 9,560,102 | 33,631,849 | 88,565,804 |
| Unreserved, reported in | | | | | |
| General fund | (15,080,817) | - | - | - | (15,080,817) |
| Tobacco settlement fund | - | 14,762,664 | - | - | 14,762,664 |
| Deposit beverage container fund | - | - | 12,181,728 | - | 12,181,728 |
| Special revenue funds | - | - | - | 33,957,401 | 33,957,401 |
| Total fund balance | 20,758,493 | 24,297,207 | 21,741,830 | 67,589,250 | 134,386,780 |
| Total liabilities and fund balance | \$ 74,822,664 | \$ 36,365,166 | \$ 39,243,068 | \$ 85,116,272 | \$ 235,547,170 |

State of Hawaii
Department of Health
Reconciliation of the Governmental Fund Balance to the
Statement of Net Assets
June 30, 2007

| | |
|--|-----------------------|
| Total fund balance – governmental funds | \$ 134,386,780 |
| Amounts reported for governmental activities in the statement of net assets are different because | |
| Tobacco settlement receivable (net of vouchers payable and Due to State of Hawaii amounts) is not available for current financial resources and therefore is not reported as an asset in the governmental funds. | 6,725,000 |
| Capital assets used in governmental activities are not financial resources and therefore not reported in the funds. | 67,284,555 |
| Compensated absences reported in the statement of net assets do not require the use of current financial resources and therefore are not reported as liabilities in the governmental funds. | (25,081,061) |
| Workers' compensation liability reported in the statement of net assets does not require the use of current financial resources and therefore is not reported as a liability in the governmental funds. | (601,540) |
| Receivables not available to pay for current-period expenditures and therefore, are not recognized in the funds. | <u>14,318,950</u> |
| Net assets of governmental activities | <u>\$ 197,032,684</u> |

The accompanying notes are an integral part of this statement.

**State of Hawaii
Department of Health
Governmental Funds
Statement of Revenues, Expenditures and Changes in Fund Balance
Year Ended June 30, 2007**

| | General | Tobacco Settlement | Deposit Beverage Container | Other Funds | Total |
|--|----------------------|-----------------------|----------------------------------|----------------------|-----------------------|
| Revenues | | | | | |
| State allotment, net | \$ 439,044,641 | - | - | \$ 6,034,173 | \$ 445,078,814 |
| Intergovernmental | - | - | - | 108,767,481 | 108,767,481 |
| Tobacco settlement | - | 36,507,187 | - | - | 36,507,187 |
| Deposit beverage container program | - | - | 22,588,027 | - | 22,588,027 |
| Nonimposed employee fringe benefits | 47,303,098 | - | - | - | 47,303,098 |
| Taxes, fees, fines and other | - | - | - | 50,844,261 | 50,844,261 |
| Interest income | - | 1,304,467 | 1,323,352 | 2,803,453 | 5,431,272 |
| Total revenues | <u>486,347,739</u> | <u>37,811,654</u> | <u>23,911,379</u> | <u>168,449,368</u> | <u>716,520,140</u> |
| Expenditures | | | | | |
| General administration | 25,862,239 | - | - | 9,169,569 | 35,031,808 |
| Environmental health | 24,045,768 | - | 20,123,840 | 20,959,809 | 65,129,417 |
| Behavioral health services | 216,162,240 | - | - | 54,763,721 | 270,925,961 |
| Health resources | 213,591,271 | 15,161,587 | - | 139,067,003 | 367,819,861 |
| Total expenditures | <u>479,661,518</u> | <u>15,161,587</u> | <u>20,123,840</u> | <u>223,960,102</u> | <u>738,907,047</u> |
| Excess (deficiency) of revenues over expenditures | 6,686,221 | 22,650,067 | 3,787,539 | (55,510,734) | (22,386,907) |
| Other financing sources (uses) | | | | | |
| Transfers in | (983,261) | - | - | 55,616,773 | 55,616,773 |
| Transfers out | (983,261) | (22,119,291) | - | (3,756,498) | (26,859,050) |
| Total other financing sources (uses) | <u>(1,966,522)</u> | <u>(22,119,291)</u> | <u>-</u> | <u>51,860,275</u> | <u>28,757,233</u> |
| Net change in fund balance | 5,702,960 | 530,776 | 3,787,539 | (3,650,459) | 6,370,816 |
| Fund balance at July 1, 2006, as previously reported | 7,333,197 | 23,766,431 | 17,954,291 | 76,923,208 | 125,977,127 |
| Prior period adjustment | 7,722,336 | - | - | (5,683,499) | 2,038,837 |
| Fund balance at July 1, 2006, as restated | <u>15,055,533</u> | <u>23,766,431</u> | <u>17,954,291</u> | <u>71,239,709</u> | <u>128,015,964</u> |
| Fund balance at June 30, 2007 | <u>\$ 20,758,493</u> | <u>\$ 24,297,207</u> | <u>\$ 21,741,830</u> | <u>\$ 67,589,250</u> | <u>\$ 134,386,780</u> |

The accompanying notes are an integral part of this statement.

State of Hawaii
Department of Health
Reconciliation of the Statement of Revenues, Expenditures and
Changes in Fund Balance of Governmental Funds to the
Statement of Activities
Year Ended June 30, 2007

| | |
|--|-----------------------|
| Net change in fund balance – total governmental funds | \$ 6,370,816 |
| Amounts reported for governmental activities in the statement of activities are different because | |
| Accrual of tobacco settlement receivable is reported in the statement of activities but not as revenue in the governmental funds as it was not available at June 30, 2007. | 2,250,000 |
| Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation exceeded capital outlays for the year. | (1,507,051) |
| Compensated absences reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. | (1,580,830) |
| Decrease in the noncurrent portion of workers' compensation liability reported in the statement of activities do not require the use of current financials resources and therefore is not reported as an expenditure in governmental funds. | (65,544) |
| Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds. | <u>(9,508,065)</u> |
| Change in net assets of governmental activities | <u>\$ (4,040,674)</u> |

The accompanying notes are an integral part of this statement.

State of Hawaii
Department of Health
Statement of Net Assets — Proprietary Funds
June 30, 2007

| | Water Pollution Control Revolving Fund | Drinking Water Treatment Revolving Loan Fund | Total |
|---|---|---|-----------------------|
| Assets | | | |
| Current assets | | | |
| Equity in cash and cash equivalents in State Treasury | \$ 154,516,160 | \$ 18,083,787 | \$ 172,599,947 |
| Loan fees receivable | 591,529 | 285,105 | 876,634 |
| Accrued interest receivable | 1,210,635 | 51,263 | 1,261,898 |
| Other accrued interest | 1,381,632 | 162,092 | 1,543,724 |
| Due from other funds | - | 392,700 | 392,700 |
| Due from federal government | - | 486,487 | 486,487 |
| Current portion of loans receivable | 17,246,964 | 2,078,021 | 19,324,985 |
| Total current assets | 174,946,920 | 21,539,455 | 196,486,375 |
| Loans receivable, net of current portion | 171,819,443 | 38,801,458 | 210,620,901 |
| Capital assets, net of accumulated depreciation, at cost | 17,051 | 270,103 | 287,154 |
| Total assets | <u>\$ 346,783,414</u> | <u>\$ 60,611,016</u> | <u>\$ 407,394,430</u> |
| Liabilities | | | |
| Current liabilities | | | |
| Accounts payable and other accrued liabilities | \$ 75,683 | \$ 128,433 | \$ 204,116 |
| Total current liabilities | 75,683 | 128,433 | 204,116 |
| Accrued vacation, net of current portion | 195,258 | 19,678 | 214,936 |
| Net Assets | | | |
| Invested in capital assets | 17,051 | 270,103 | 287,154 |
| Restricted – expendable | 346,495,422 | 60,192,802 | 406,688,224 |
| Total net assets | <u>346,512,473</u> | <u>60,462,905</u> | <u>406,975,378</u> |
| Total liabilities and net assets | <u>\$ 346,783,414</u> | <u>\$ 60,611,016</u> | <u>\$ 407,394,430</u> |

The accompanying notes are an integral part of this statement.

State of Hawaii
Department of Health
Statement of Revenues, Expenses and Changes in Fund Net Assets –
Proprietary Funds
Year Ended June 30, 2007

| | Water Pollution Control Revolving Fund | Drinking Water Treatment Revolving Loan Fund | Total |
|------------------------------|---|---|-----------------------|
| Operating revenues | | | |
| Interest income from loans | \$ 3,443,195 | \$ 197,018 | \$ 3,640,213 |
| Administrative loan fee | 1,577,060 | 790,290 | 2,367,350 |
| Total revenues | <u>5,020,255</u> | <u>987,308</u> | <u>6,007,563</u> |
| Expenses | | | |
| Administrative | 1,580,570 | 270,214 | 1,850,784 |
| State program management | - | 324,398 | 324,398 |
| Water protection | - | 65,740 | 65,740 |
| Small systems | - | 227,500 | 227,500 |
| Total expenses | <u>1,580,570</u> | <u>887,852</u> | <u>2,468,422</u> |
| Operating income | 3,439,685 | 99,456 | 3,539,141 |
| Nonoperating revenues | | | |
| State contributions | 2,053,000 | 1,661,000 | 3,714,000 |
| Federal contributions | 47,792,849 | 21,353,757 | 69,146,606 |
| Other interest income | 6,476,357 | 777,242 | 7,253,599 |
| Other | - | 1,087 | 1,087 |
| Total nonoperating revenues | <u>56,322,206</u> | <u>23,793,086</u> | <u>80,115,292</u> |
| Change in net assets | 59,761,891 | 23,892,542 | 83,654,433 |
| Net assets at July 1, 2006 | <u>286,750,582</u> | <u>36,570,363</u> | <u>323,320,945</u> |
| Net assets at June 30, 2007 | <u>\$ 346,512,473</u> | <u>\$ 60,462,905</u> | <u>\$ 406,975,378</u> |

The accompanying notes are an integral part of this statement.

State of Hawaii
Department of Health
Statement of Cash Flows — Proprietary Funds
Year Ended June 30, 2007

| | Water Pollution Control Revolving Fund | Drinking Water Treatment Revolving Loan Fund | Total |
|---|---|---|----------------|
| Cash flows from operating activities | | | |
| Interest income from loans | \$ 3,429,702 | \$ 187,637 | \$ 3,617,339 |
| Administrative loan fees | 1,523,712 | 632,869 | 2,156,581 |
| Principal repayments on loans | 13,119,252 | 1,157,968 | 14,277,220 |
| Disbursement of loan proceeds | (63,509,828) | (25,068,775) | (88,578,603) |
| Payments to employees | (1,218,817) | (198,504) | (1,417,321) |
| Payments to vendors | (142,888) | (474,117) | (617,005) |
| Net cash flows used in operating activities | (46,798,867) | (23,762,922) | (70,561,789) |
| Cash flows from noncapital financing activities | | | |
| State contributions | 2,053,000 | 1,661,000 | 3,714,000 |
| Federal contributions | 49,309,531 | 21,404,046 | 70,713,577 |
| Net advances to other funds | - | (27,700) | (27,700) |
| Net cash flows provided by noncapital financing activities | 51,362,531 | 23,037,346 | 74,399,877 |
| Cash flows from capital and related financing activities | | | |
| Purchase of equipment | (9,827) | (72,670) | (82,497) |
| Net cash flows used in capital and related financing activities | (9,827) | (72,670) | (82,497) |
| Cash flows from investing activities | | | |
| Other interest | 6,252,010 | 745,359 | 6,997,369 |
| Net cash flows provided by investing activities | 6,252,010 | 745,359 | 6,997,369 |
| Net increase (decrease) in cash and cash equivalents | 10,805,847 | (52,887) | 10,752,960 |
| Cash and cash equivalents at July 1, 2006 | 143,710,313 | 18,136,674 | 161,846,987 |
| Cash and cash equivalents at June 30, 2007 | \$ 154,516,160 | \$ 18,083,787 | \$ 172,599,947 |

The accompanying notes are an integral part of this statement.

State of Hawaii
Department of Health
Statement of Cash Flows — Proprietary Funds
Year Ended June 30, 2007

| | Water Pollution Control Revolving Fund | Drinking Water Treatment Revolving Loan Fund | Total |
|--|---|---|------------------------|
| Reconciliation of operating income to net cash used in operating activities | | | |
| Operating income | \$ 3,439,685 | \$ 99,456 | \$ 3,539,141 |
| Adjustments to reconcile operating income to net cash used in operating activities | | | |
| Depreciation expense | 9,575 | 88,307 | 97,882 |
| Other nonoperating income | - | 1,087 | 1,087 |
| Change in assets and liabilities | | | |
| Accounts receivable | 5,574 | - | 5,574 |
| Loans receivable | (50,390,576) | (23,910,808) | (74,301,384) |
| Accrued interest on loans receivables | (13,493) | (9,381) | (22,874) |
| Loan fees receivable | (53,348) | (157,422) | (210,770) |
| Accounts payable and other accrued liabilities | 203,716 | 125,839 | 329,555 |
| Net cash used in operating activities | <u>\$ (46,798,867)</u> | <u>\$ (23,762,922)</u> | <u>\$ (70,561,789)</u> |

The accompanying notes are an integral part of this statement.

State of Hawaii
Department of Health
Statement of Fiduciary Net Assets — Fiduciary Funds
June 30, 2007

| | Agency Funds |
|---------------------------|-------------------------|
| Assets | |
| Cash and cash equivalents | \$ 364,442 |
| Total assets | <u>\$ 364,442</u> |
| Liabilities | |
| Due to others | \$ 364,442 |
| Total liabilities | <u>\$ 364,442</u> |

The accompanying notes are an integral part of this statement.

State of Hawaii
Department of Health
Notes to Financial Statements
June 30, 2007

1. Organization and Summary of Significant Accounting Policies

Financial Reporting Entity

The State of Hawaii, Department of Health (the "Department"), administers and oversees statewide personal health services, health promotion and disease prevention, mental health programs, monitoring of the environment, and the enforcement of environmental health laws. Federal grants received to support the State's health services and programs are administered by the Department.

The accompanying financial statements of the Department have been prepared in conformity with accounting principles generally accepted in the United States of America prescribed by the Governmental Accounting Standards Board ("GASB").

The Department is part of the executive branch of the State of Hawaii (the "State"). The financial statements of the Department are intended to present the financial position and the changes in financial position and cash flows, where applicable, of only that portion of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2007, and the changes in its financial position and cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America. The State Comptroller maintains the central accounts for all State funds and publishes a comprehensive annual financial report for the State annually, which includes the Department's financial activities.

Act 262, Session Laws of Hawaii of 1996, established the Hawaii Health Systems Corporation ("HHSC") as a public body corporate and politic and an instrumentality and agency of the State. HHSC consists of the state hospitals and was created to provide quality health care for all of the people in the state. HHSC commenced operations on July 1, 1996 and is administratively attached to the Department. However, HHSC is a component unit of the State and not the Department. HHSC's stand-alone financial statements are included in the State's comprehensive annual financial report but are not included in the Department's basic financial statements.

Department-wide Financial Statements

The Department-wide financial statements, the statement of net assets and the statement of activities, are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Certain eliminations have been made as prescribed by GASB Statement No. 34 related to interfund activities, receivables, and payables. All internal balances have been eliminated except those representing balances between governmental and business-type activities, which are presented as internal balances and eliminated in the total department column. In the statement of activities, those transactions between governmental and business-type activities have not been eliminated. In addition, the fiduciary funds account for net assets held in a trustee or agent capacity for others. These funds are not reflected in the department-wide financial statements since these resources are not available to support the Department's programs.

Fund Financial Statements

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when

State of Hawaii
Department of Health
Notes to Financial Statements
June 30, 2007

they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Department considers revenues to be available if they are collected within 60 days of the end of the current fiscal year end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, expenditures related to compensated absences and claims and judgments are recorded only when payment is due.

The proprietary funds and fiduciary funds financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the department-wide financial statements described above.

The Department has the option under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, to elect to apply all Financial Accounting Standards Board ("FASB") pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. The Department's enterprise funds have elected not to apply FASB statements after the applicable date.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

A description of the funds administered by the Department is as follows:

Governmental Funds (Governmental Activities):

- *General Fund* – The General Fund is the general operating fund of the Department. It is used to account for all financial resources except those required to be accounted for in another fund. The General Fund presented is a part of the State's General Fund and is limited to only those appropriations and obligations of the Department.
- *Special Revenue Funds* – Special revenue funds are used to account for the proceeds of specific revenue sources (other than major capital projects) that are legally restricted to expenditures for specified purposes.
- *Capital Projects Funds* – Capital projects funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary fund type) and are included in Other Funds in the fund financial statements.

Proprietary Funds (Business-Type Activities):

- *Enterprise Funds* – Enterprise funds are used to account for the activities for which the intent of management is to recover, primarily through user charges, the cost of providing goods or services to customers, or where sound financial management dictates that periodic determination of results of operations are appropriate.

Fiduciary Funds:

- *Agency Funds* – Agency funds are used to account for cash collected and expended by the Department in a custodial capacity.

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Equity in Cash and Cash Equivalents in State Treasury

The State Director of Finance is responsible for the safekeeping of cash in the State Treasury in accordance with State laws. The Director of Finance may invest any monies of the State which, in the Director's judgment, are in excess of the amounts necessary for meeting the immediate requirements of the State. Effective August 1, 1999, cash is pooled with funds from other State agencies and departments and deposited into approved financial institutions or in the State Treasury Investment Pool System. Funds in the investment pool accrue interest based on the average weighted cash balances of each account.

The State requires that depository banks pledge as collateral, government securities held in the name of the State for deposits not covered by federal deposit insurance.

GASB Statement No. 40, *Deposit and Investment Risk Disclosures* ("Statement No. 40") requires disclosures over common deposit and investment risks related to credit risk, interest rate risk, and foreign currency risk. Investments can be categorized by type, maturity and custodian to determine the level of interest rate, credit, and custodial risk assumed by the Department. However, as all of the Department's monies are held in the State cash pool, the Department does not manage its own investments and the types of investments and related interest rate, credit, and custodial risks are not determinable at the Department level. The risk disclosures of the State's cash pool are included in the State's Comprehensive Annual Financial Report ("CAFR") for the fiscal year ended June 30, 2007 which may be obtained from the following address:

Department of Accounting and General Services
Accounting Division
P.O. Box 119
Honolulu, Hawaii 96810-0119

Due from State Treasury

The State Director of Finance is responsible for the safekeeping of all cash in the State Treasury in accordance with State laws. Currently, separate accounts are not maintained in the State Treasury for the Department's general operating and capital appropriations. Although these appropriations are available to the Department to expend, custody and ownership of the funds remains with the State. Unspent general and capital appropriations that continue to be available to the Department for expenditure at the end of the fiscal year are reported as Due from State Treasury in the accompanying fund and department-wide financial statements.

Due from Other State Agencies

Receivables due from other State Agencies consist of reimbursements from the Department of Human Services ("DHS") for Medicaid payments that the Department makes to the providers. The Department is responsible to pay the State portion of the Medicaid claims, and DHS reimburses them for the Federal portion of the claims. The receivable of \$32.3 million is comprised of \$15.7 million receivable for the Developmental Disabilities/Mental Retardation ("DD/MR") Waiver program and \$16.6 for other Medicaid rehabilitation option claims.

Tobacco Settlement

In November 1998, the State settled its tobacco lawsuit as part of a nationwide settlement involving 46 other states and various tobacco industry defendants. Under the settlement, those tobacco companies that have joined in the Master Settlement Agreement will pay the State approximately \$1.3 billion over a 25-year period. The Department is responsible for administering the Hawaii Tobacco Settlement Special Fund. The Department receives all tobacco settlement monies and then allocates and appropriates 75% of the funds to other State agencies and other entities in

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accordance with Hawaii Revised Statutes (“HRS”) 328L-2. The Department receives annual payments on April 15 of each year for tobacco settlements earned for the preceding calendar year.

The Department received approximately \$36,500,000 in tobacco settlement proceeds during the year ended June 30, 2007 for the calendar year ended December 31, 2006. In accordance with GASB Technical Bulletin No. 04-01, *Tobacco Settlement Recognition and Financial Reporting Entity Issues*, the Department has recorded a tobacco settlement receivable for \$26,900,000 in the statement of net assets representing tobacco settlements earned for the period January 1, 2007 through June 30, 2007.

Reserved for Encumbrances

Encumbrance accounting, under which purchase orders and contractual commitments for the expenditure of funds are recorded in order to reserve that portion of the applicable appropriation, is employed in the governmental funds. Although appropriations lapse at year end, open encumbrances are reported as reservations of fund balances because the commitments will be honored when the goods or services are received. Encumbrances do not constitute expenditures or liabilities.

Capital Assets

Capital assets, which include buildings, furniture, and equipment, are reported in the applicable governmental or business-type activities in the department-wide financial statements and in the proprietary funds’ financial statements. Capital assets are defined by the Department as those assets with estimated useful lives greater than one year and with an acquisition cost greater than:

| | |
|------------------------------------|-----------------|
| Land | All capitalized |
| Land improvements | \$100,000 |
| Building and building improvements | \$100,000 |
| Equipment | \$5,000 |

Such assets are recorded at historical cost if purchased or constructed. Donated assets are recorded at estimated fair market value at the time received. Depreciation expense is recorded in the department-wide financial statements using the straight-line method over the estimated useful lives of the assets. Generally, the useful lives are as follows:

| | Governmental- Type Activities | Business- Type Activities |
|------------------------------------|--|--------------------------------------|
| Land improvements | 15 | Not applicable |
| Building and building improvements | 30 | Not applicable |
| Furniture and equipment | 5–7 | 5–7 |

Deferred Income

Deferred income at the fund level and department-wide level arise when the Department receives resources before it has a legal claim to them. In subsequent periods, when the revenue recognition criteria is met, or when the Department has a legal claim to the resources, the liability for deferred income is removed from the statement of net assets and balance sheet, and revenue

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is recognized. Deferred income at June 30, 2007 consisted primarily of Federal grant funds for which all eligibility requirements have not yet been met.

Accrued Vacation

Vacation pay is accrued as earned by employees. Vacation pay can accumulate at the rate of one and three-quarters working days for each month of service up to 720 hours at calendar year-end and is convertible to pay upon termination of employment. As accrued vacation does not require the use of current financial resources, it is not reported in the governmental funds balance sheet.

Intrafund and Interfund Transactions

Significant transfers of financial resources between activities included within the same fund are offset within that fund. Transfers of revenues from funds authorized to receive them to funds authorized to expend them are recorded as operating transfers in the basic financial statements.

Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Use of Restricted and Unrestricted Net Assets

When an expense is incurred for which both restricted and unrestricted net assets are available, the Department's policy is to apply restricted net assets first.

New Accounting Pronouncements

In June 2004, the GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postretirement Benefits Other Than Pensions*. This Statement establishes standards for the measurement, recognition and display of other postretirement benefits expense/expenditures and related liabilities (assets), note disclosures and required supplementary information in the financial reports of state and local governmental employers. The provisions of this Statement are effective for periods beginning after December 15, 2006. Management has not yet determined the effect this Statement will have on its financial statements.

In June 2005, the GASB issued Statement No. 47, *Accounting for Termination Benefits*. This Statement establishes standards for accounting for termination benefits that affect an employer's obligations. For defined benefit OPEB plans, the provisions of this Statement are effective for the fiscal year beginning after December 15, 2006. For all other termination benefits, the provisions of this Statement are effective in fiscal 2007. Management does not expect this Statement to have a material effect on the Department's financial statements.

In September 2006, the GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*. This Statement establishes criteria that governments will use to ascertain whether the proceeds received should be reported as revenue or as a liability. The provisions of this Statement are effective for the fiscal year beginning after December 15, 2006. Management does not expect this Statement to have a material effect on the Department's financial statements.

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In November 2006, the GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. This Statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. The provisions of this Statement are effective for the fiscal year beginning after December 15, 2007. Management has not yet determined the effect this Statement will have on its financial statements.

In May 2007, The GASB issued Statement No. 50, *Pension Disclosures – An Amendment of GASB Statements No. 25 and 27*. This Statement is to amend note disclosure and required supplementary information (“RSI”) standards of Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 27, *Accounting for Pensions by State and Local Governmental Employers*, to conform with applicable changes adopted in Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The provisions of this Statement are effective for periods beginning after June 15, 2007, except for requirements related to the use of the entry age actuarial cost method for the purpose of reporting a surrogate funded status and funding progress of plans that use the aggregate actuarial cost method, which are effective for periods for which the financial statements and RSI contain information resulting from actuarial valuations as of June 15, 2007, or later. Management has not yet determined the effect this Statement will have on the Department’s financial statements.

In June 2007, the GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. The provisions of this Statement establish accounting and financial reporting requirements for intangible assets to reduce inconsistencies, thereby enhancing the comparability of the accounting and financial reporting of such assets among state and local governments. This Statement also results in a more faithful representation of the service capacity of intangible assets – and therefore the financial position of governments – and of the periodic cost associated with the usage of such service capacity in governmental financial statements. The provisions of this Statement are effective for periods beginning after June 15, 2009. Management does not expect this statement to have a material effect on the Department’s financial statements.

In November 2007, the GASB issued Statement No. 52, *Land and Other Real Estate Held As Investments by Endowments*, effective for the Department’s fiscal year beginning July 1, 2008. Statement No. 52 requires that land and other real estate held as investments by endowments be reported at fair value at the reporting date. Changes in fair value during the period should be reported as investment income. Management is currently evaluating the effect that this statement will have on its financial statements.

2. Loans Receivable

At June 30, 2007, the proprietary funds loans receivable consisted of loans to county governmental units for the water pollution control and drinking water treatment programs. The loans require annual, semi-annual or quarterly payments, including interest at 0.00% to 3.02%, commencing not later than one year after project completion, notice to proceed, or loan agreement date. Final payment is due not later than twenty years after project completion. Accrued interest receivable on the loans amounted to approximately \$1,262,000 at June 30, 2007.

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The following is a schedule of principal payments due on loans for projects completed or in progress as of June 30, 2007:

| | |
|-----------------------------|-----------------------|
| Year ending June 30, | |
| 2008 | \$ 19,324,985 |
| 2009 | 18,045,676 |
| 2010 | 18,384,206 |
| 2011 | 18,732,598 |
| 2012 | 19,062,484 |
| Thereafter | <u>136,395,937</u> |
| | <u>\$ 229,945,886</u> |

3. Capital Assets

Capital asset activity for the year ended June 30, 2007 was as follows:

| | Beginning Balance | Additions | Dispositions | Ending Balance |
|---|----------------------|-----------------------|---------------------|----------------------|
| Governmental activities | | | | |
| Capital assets, not being depreciated | | | | |
| Land | \$ 1,018,080 | \$ - | \$ - | \$ 1,018,080 |
| Total capital assets not being depreciated | 1,018,080 | - | - | 1,018,080 |
| Capital assets, being depreciated | | | | |
| Land improvements | 1,862,927 | - | - | 1,862,927 |
| Building and improvements | 132,168,484 | 113,028 | - | 132,281,512 |
| Furniture and equipment | 16,238,836 | 4,205,220 | (989,618) | 19,454,438 |
| Total capital assets being depreciated | 150,270,247 | 4,318,248 | (989,618) | 153,598,877 |
| Less: Accumulated depreciation | | | | |
| Land improvements | 1,819,259 | 22,818 | - | 1,842,077 |
| Building and improvements | 68,764,346 | 3,973,849 | (958) | 72,737,237 |
| Furniture and equipment | 11,913,116 | 1,644,356 | (804,384) | 12,753,088 |
| Total accumulated depreciation | 82,496,721 | 5,641,023 | (805,342) | 87,332,402 |
| Governmental activities, net | <u>\$ 68,791,606</u> | <u>\$ (1,322,775)</u> | <u>\$ (184,276)</u> | <u>\$ 67,284,555</u> |
| Business-type activities | | | | |
| Capital assets being depreciated | | | | |
| Equipment | \$ 930,099 | \$ 82,497 | \$ (2,815) | \$ 1,009,781 |
| Total capital assets being depreciated | 930,099 | 82,497 | (2,815) | 1,009,781 |
| Less: Accumulated depreciation for equipment | 627,560 | 97,882 | (2,815) | 722,627 |
| Total accumulated depreciation | 627,560 | 97,882 | (2,815) | 722,627 |
| Business-type activities capital assets, net | <u>\$ 302,539</u> | <u>\$ (15,385)</u> | <u>\$ -</u> | <u>\$ 287,154</u> |

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Current period depreciation expense was charged to functions as follows:

| | |
|---|---------------------|
| Governmental activities | |
| General administration | \$ 463,597 |
| Environmental health | 1,888,360 |
| Behavioral health | 1,797,019 |
| Health resources | 1,492,047 |
| Total depreciation expense – governmental activities | <u>\$ 5,641,023</u> |
| Business-type activities | |
| Environmental health | \$ 97,882 |
| Total depreciation expense – business-type activities | <u>\$ 97,882</u> |

4. Long-Term Obligation – Governmental Activities

The changes to the accrued vacation liability as of June 30, 2007 were as follows:

| | |
|--------------------------|----------------------|
| Balance at July 1, 2006 | \$ 23,500,231 |
| Increase | 11,324,857 |
| Decrease | 9,744,027 |
| Balance at June 30, 2007 | <u>25,081,061</u> |
| Less: Current portion | <u>8,600,296</u> |
| Noncurrent portion | <u>\$ 16,480,765</u> |

5. Non-Imposed Employee Fringe Benefits

Non-imposed employee fringe benefits related to General Fund salaries are assumed by the State and are not charged to the Department. These costs, totaling approximately \$47,300,000 for the fiscal year ended June 30, 2007, have been reported as revenues and expenditures of the Department's General Fund.

Payroll fringe benefit costs related to federally-funded salaries are not assumed by the State and are recorded as expenditures in the special revenue funds.

6. Employee Benefits

Employees' Retirement System

Substantially all eligible employees of the Department are members of the Employees' Retirement System of the State of Hawaii ("ERS"), a cost-sharing, multiple-employer public employee retirement plan. The ERS provides retirement benefits as well as death and disability benefits. All contributions, benefits and eligibility requirements are established by Chapter 88, HRS, and can be amended by legislative action.

The ERS is composed of a contributory retirement option and a noncontributory retirement option. Prior to July 1, 1984, the ERS consisted of only a contributory option. In 1984, legislation was enacted to add a new noncontributory option for members of the ERS who are also covered under social security. Persons employed in positions not covered by social security are precluded from

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the noncontributory option. The noncontributory option provides for reduced benefits and covers most eligible employees hired after June 30, 1984. Employees hired before that were allowed to continue under the contributory option or to elect the new noncontributory option and receive a refund of employee contributions. All benefits vest after five and ten years of credited service under the contributory and noncontributory options, respectively. Both options provide a monthly retirement allowance based on the employee's age, years of credited service and average final compensation ("AFC"). The AFC is the average salary earned during the five highest paid years of service including the vacation payment, if the employee became a member prior to January 1, 1971. The AFC for members hired on or after that date and prior to January 1, 2003, is based on the three highest paid years of service, excluding the vacation payment. Effective January 1, 2003, the AFC is the highest three calendar years or highest five calendar years plus lump sum vacation payment, or highest three school contract years, or last 36 credited months or last 60 credited months plus lump sum vacation payment. Contributions for employees of the Department are paid from the State General Fund and are included as part of the non-imposed fringe benefit costs discussed in Note 5.

On July 1, 2006, a new hybrid contributory plan became effective pursuant to Act 179, SLH of 2004. Members in the hybrid plan are eligible for retirement at age 62 with 5 years of credited service or age 55 and 30 years of credited service. Members will receive a benefit multiplier of 2% for each year of credited service in the hybrid plan. The benefit payment options are similar to the current contributory plan. Almost 58,000 current members, all members of the noncontributory plan and certain members of the contributory plan were eligible to join the new hybrid plan. Most of the new employees hired from July 1, 2006 will be required to join the hybrid plan.

Most covered employees of the contributory option are required to contribute 7.8% of their salary. The funding method used to calculate the total employer contribution requirement is the entry age normal actuarial cost method. Under this method, employer contributions to the ERS are comprised of normal cost plus level annual payments required to amortize the unfunded actuarial accrued liability over the remaining period of 29 years from July 1, 2000.

Actuarial valuations are prepared for the entire ERS and are not separately computed for each department or agency. Information on vested and nonvested benefits, and other aspects of the ERS, is also not available on a departmental or agency basis.

ERS issues a CAFR that includes financial statements and required supplementary information which may be obtained from the following address:

Employees' Retirement System of the State of Hawaii
201 Merchant Street, Suite 1400
Honolulu, Hawaii 96813

Post-retirement Health Care and Life Insurance Benefits

In addition to providing pension benefits, the State, pursuant to Chapter 87, HRS, provides certain health care and life insurance benefits to all qualified employees. For employees hired before July 1, 1996, the State pays the entire monthly health care premium for those retiring with ten or more years of credited service, and 50% of the monthly premium for those retiring with fewer than ten years of credited service. For employees hired after June 30, 1996, and retiring with fewer than ten years of service, the State makes no contributions. For those retiring with at least ten years but fewer than 15 years of service, the State pays 50% of the retired employees' monthly Medicare or non-Medicare premium. For employees hired after June 30, 1996, and retiring with at least 15 years but fewer than 25 years of service, the State pays 75% of the retired employees' monthly

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Medicare or non-Medicare premium; and for those retiring with over 25 years of service, the State pays the entire health care premium. Free life insurance coverage for retirees and free dental coverage for dependents under age 19 are also available. Retirees covered by the medical portion of Medicare are eligible to receive a reimbursement for the basic medical coverage premium. Contributions are financed on a pay-as-you-go basis.

Effective July 1, 2003, the Hawaii Employer-Union Health Benefits Trust Fund ("EUTF") replaced the Hawaii Public Employees Health Fund under Act 88, SLH 2001. The EUTF was established to provide a single delivery system of health benefits to state and county employees, retirees, and their dependants.

Accumulated Sick Leave

Sick leave accumulates at the rate of one and three-quarters working days for each month of service without limit, but may be taken only in the event of illness and is not convertible to pay upon termination of employment. However, a State employee who retires or leaves government service in good standing with 60 days or more of unused sick leave is entitled to additional service credit in ERS. At June 30, 2007, accumulated sick leave was approximately \$64,400,000.

Deferred Compensation Plan

The State established a deferred compensation plan ("Plan") in accordance with Section 457 of the Internal Revenue Code, which enables State employees to defer a portion of their compensation. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

All amounts of compensation deferred under the Plan, as well as property and rights purchased with these amounts and income attributable to these amounts are held in trust by third party agents for the exclusive benefit of participants and their beneficiaries. The assets and liabilities of the Plan are not reflected in the State of Hawaii or Department's financial statements.

7. Commitments and Contingencies

Operating Leases

The Department leases various office facilities and equipment on a long-term basis as provided for in the lease agreements. The following is a schedule of minimum future rent expense on noncancelable operating leases at June 30, 2007:

| | |
|-----------------------------|---------------------|
| Year ending June 30, | |
| 2008 | \$ 393,100 |
| 2009 | 323,700 |
| 2010 | 301,700 |
| 2011 | 255,100 |
| 2012 | 53,000 |
| | <u>\$ 1,326,600</u> |

Rent expenditures for the fiscal year ended June 30, 2007 approximated \$2,400,000.

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Insurance Coverage

The State maintains certain insurance coverage to satisfy bond indenture agreements as well as for other purposes, but is substantially self-insured for all other perils including workers' compensation. The State records a liability for risk financing and insurance related losses, including incurred but not reported, if it is determined that a loss has been incurred and the amount can be reasonably estimated. The State retains various risks and insures certain excess layers with commercial insurance companies. At June 30, 2007, the State recorded estimated losses for workers' compensation, automobile, and general liability claims as long-term liabilities as the losses will not be liquidated with currently expendable available financial resources. The estimated losses will be paid from legislative appropriations of the State's General Fund. The Department's portion of the State's workers' compensation expense for the year ended June 30, 2007 was approximately \$228,000.

Litigation

The Department is a party to various legal proceedings, the outcome of which, in the opinion of management, will not have a material adverse effect on the Department's financial position. Losses, if any, are either covered by insurance or will be paid from legislative appropriations of the State's General Fund.

Ceded Lands

The Office of Hawaiian Affairs ("OHA") and the State of Hawaii are presently in litigation involving the State's alleged failure to properly account for and pay to OHA monies due to OHA under the provisions of the Hawaii State Constitution and Chapter 10 of the Hawaii Revised Statutes for use by the State of certain ceded lands. As of June 30, 2007, the outcome of the lawsuit had not been decided.

In January 2008, the Office of Hawaiian Affairs ("OHA") and the State announced a settlement resolving the ceded land revenues dispute, which is subject to legislative approval. However, no further action will be taken on House Bill 266 (State OHA settlement) during the 2008 legislative session.

8. Restatements to the Department-wide Net Assets and Governmental Funds Fund Balance

The Department has restated its June 30, 2006 department-wide net assets and governmental funds fund balances to correct errors in accounting for appropriations, receivables and liabilities. The restatement adjustments removed appropriations that were included in the Department's financial statements that are assigned to another State agency, recorded liabilities that were not accrued, and recorded a receivable from another State agency.

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As a result of the correction, the Department made the following adjustments to its previously reported June 30, 2006 department-wide net assets and governmental funds fund balances.

| | Governmental Activities |
|--|------------------------------------|
| Net assets at June 30, 2006, as previously reported | \$ 175,207,506 |
| Adjustments attributable to | |
| Overstatement of allotments | (4,013,827) |
| Understatement of liabilities and expenses | (1,669,672) |
| Understatement of receivables | 31,549,351 |
| Net assets at June 30, 2006, as restated | <u>\$ 201,073,358</u> |

| | General Fund | Other Funds | Governmental Funds |
|---|-----------------------------|-----------------------------|-------------------------------|
| Fund balances at June 30, 2006, as previously reported | \$ 7,333,197 | \$ 76,923,208 | \$ 125,977,127 |
| Adjustments attributable to | | | |
| Overstatement of allotments | - | (4,013,827) | (4,013,827) |
| Understatement of liabilities and expenses | - | (1,669,672) | (1,669,672) |
| Understatement of receivables | 7,722,336 | - | 7,722,336 |
| Fund balances at June 30, 2006, as restated | <u>\$ 15,055,533</u> | <u>\$ 71,239,709</u> | <u>\$ 128,015,964</u> |

**Required Supplementary Information
Other than Management's
Discussion and Analysis**

State of Hawaii
Department of Health
Budgetary Comparison Schedule — General Fund
Year Ended June 30, 2007

| | Budgeted Amounts | | Actual Amounts (Budgetary Basis) |
|---|-------------------------|----------------|---|
| | Original | Final | |
| Revenues | | | |
| Current-year appropriations | \$ 431,382,556 | \$ 440,104,286 | \$ 438,051,384 |
| Total revenues | 431,382,556 | 440,104,286 | 438,051,384 |
| Expenditures | | | |
| General administration | 23,231,262 | 24,902,934 | 24,682,155 |
| Environmental health administration | 18,583,576 | 18,725,836 | 18,504,836 |
| Behavioral health services administration | 197,829,080 | 201,519,108 | 200,678,032 |
| Health resources administration | 191,738,638 | 194,956,408 | 194,186,361 |
| Total expenditures | 431,382,556 | 440,104,286 | 438,051,384 |
| Excess of revenues over expenditures | \$ - | \$ - | \$ - |

The accompanying notes are an integral part of this schedule.

State of Hawaii
Department of Health
Budgetary Comparison Schedule — Tobacco Settlement Fund
Year Ended June 30, 2007

| | Budgeted Amounts | | Actual Amounts (Budgetary Basis) |
|--------------------------------------|-------------------------|---------------|---|
| | Original | Final | |
| Revenues | | | |
| Current-year funds | \$ 43,143,467 | \$ 43,184,029 | \$ 37,733,011 |
| Total revenues | 43,143,467 | 43,184,029 | 37,733,011 |
| Expenditures | | | |
| Health resources administration | 43,143,467 | 43,184,029 | 39,023,102 |
| Total expenditures | 43,143,467 | 43,184,029 | 39,023,102 |
| Excess of expenditures over revenues | \$ - | \$ - | \$ (1,290,091) |

The accompanying notes are an integral part of this schedule.

State of Hawaii
Department of Health
Budgetary Comparison Schedule — Deposit Beverage Container Fund
Year Ended June 30, 2007

| | Budgeted Amounts | | Actual Amounts (Budgetary Basis) |
|---|-------------------------|----------------------|---|
| | Original | Final | |
| Revenues | | | |
| Current-year funds | <u>\$ 62,187,059</u> | <u>\$ 62,200,828</u> | <u>\$ 57,769,511</u> |
| Total revenues | 62,187,059 | 62,200,828 | 57,769,511 |
| Expenditures | | | |
| Environmental health administration | <u>62,187,059</u> | <u>62,200,828</u> | <u>59,571,698</u> |
| Total expenditures | <u>62,187,059</u> | <u>62,200,828</u> | <u>59,571,698</u> |
| Excess of revenues over expenditures | <u>\$ -</u> | <u>\$ -</u> | <u>\$ (1,802,187)</u> |

The accompanying notes are an integral part of this schedule.

State of Hawaii
Department of Health
Notes to Required Supplementary Information
June 30, 2007

1. Budgeting and Budgetary Control

The Department follows these procedures in establishing the budgetary data reflected in the basic financial statements:

- *The Budget* – Not less than 20 days before the State Legislature convenes in every odd-numbered year, the Governor submits to the State Legislature, and to each member thereof, a budget which contains the program and budget recommendation of the Governor for the succeeding biennium. The budget in general contains: the State program structure; statements of statewide objectives; financial requirements for the next biennium to carry out the recommended programs; a summary of State receipts and revenues in the last completed fiscal year; a revised estimate for the fiscal year in progress; and an estimate for the succeeding biennium.
- *Legislative Review* – The State Legislature considers the Governor’s proposed program and financial plan and budget, evaluates alternatives to the Governor’s recommendations, adopts programs, and determines the State budget. It may, from time to time, request the Department of Budget and Finance and any agency to conduct such analysis of programs and finances as will assist in determining the State’s program and financial plan and budget.
- *Program Execution* – Except as limited by policy decisions of the Governor, appropriations by the State Legislature, and other provisions of law, the agencies responsible for the programs administer the programs and are responsible for their proper management. The appropriations by the State Legislature for a biennium are allocated between the two fiscal years of the biennium in the manner provided in the budget or appropriations act and as further prescribed by the Director of Finance. No appropriation transfers or changes between programs or agencies can be made without legislative authorization. Authorized transfers or changes, when made, should be reported to the State Legislature.

Budgetary control is maintained at the appropriation line item level established in the appropriation acts.

Budgets are adopted for the General Fund of the Department and are prepared on the basis of cash receipts and amounts disbursed, which is a basis of accounting other than generally accepted accounting principles (“GAAP”).

The major difference between the budgetary and GAAP basis are that: (1) the budget is prepared on the basis of cash receipts and amounts disbursed; and (2) encumbrances are recorded as the equivalent of expenditures under the budgetary basis.

Since budgetary basis differs from GAAP, budget and actual amounts in the accompanying Required Supplementary Information – Budgetary Comparison Schedules are presented on the budgetary basis. A reconciliation of revenues in excess of (less than) expenditures on a budgetary basis at June 30, 2007, to revenues in excess of (less than) expenditures presented in conformity with GAAP is set forth in Note 2 to the Required Supplementary Information.

State of Hawaii
Department of Health
Notes to Required Supplementary Information
June 30, 2007

2. Explanation of Differences between Budgetary Actual and GAAP Revenues and Expenditures

| | General Fund | Tobacco Settlement Fund | Deposit Beverage Container Fund |
|---|-------------------------|--|--|
| Excess of revenues over expenditures (expenditures over revenues) – actual on a budgetary basis | \$ - | \$ (1,290,091) | \$ (1,802,187) |
| Reserve for encumbrances at year end | 35,839,310 | 9,534,543 | 9,560,102 |
| Expenditures for liquidation of prior year's encumbrances | (53,929,255) | (4,670,900) | (4,053,773) |
| Accrual and other adjustments | <u>24,776,166</u> | <u>19,076,515</u> | <u>83,397</u> |
| Excess of revenues over expenditures (expenditures over revenues) – GAAP basis | <u>\$ 6,686,221</u> | <u>\$ 22,650,067</u> | <u>\$ 3,787,539</u> |

**Schedule of
Expenditures of Federal Awards**

State of Hawaii
Department of Health
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2007

| Federal Grantor/Pass-Through Grantor/Program Title | Project Number | CFDA Contract, Award or Assistance ID Number | Federal Expenditures | Amount Provided to Subrecipient |
|--|----------------|--|----------------------|---------------------------------|
| U.S. Department of Health and Human Services (DHHS) | | | | |
| Direct Programs | | | | |
| Special Programs for Aging – Title VII Chapter 3 | 468 | 93.041 | \$ 11,542 | \$ - |
| Special Programs for Aging – Title VII Chapter 2 | 468 | 93.042 | 118,331 | - |
| Special Programs for Aging – Title III Part D | 401 | 93.043 | 100,162 | 100,162 |
| Special Programs for Aging – Title III Part B | 401 | 93.044 | 1,557,009 | 1,557,009 |
| Special Programs for Aging – Title III Part C1 & C2 | 401 | 93.045 | 2,326,579 | 2,326,579 |
| Nutrition Services Incentive Program | 406 | 93.053 | 434,931 | - |
| Subtotal Aging Cluster | | | 4,318,519 | 3,883,588 |
| Special Programs for Aging – Title IV | 405, 478 | 93.048 | 387,963 | 227,928 |
| Special Programs for Aging – Title III Part E | 401 | 93.052 | 738,637 | 738,637 |
| Project Ho'omohala - Transition to Adulthood | 229 | 93.104 | 846,352 | - |
| Maternal and Child Health Federal Consolidated Programs | various | 93.110 | 1,225,361 | 1,019,462 |
| Project Grants and Cooperative Agreements for Tuberculosis Control Programs | 247 | 93.116 | 827,969 | - |
| Emergency Medical Services for Children | 388 | 93.127 | 81,662 | 1,000 |
| Primary Care Services – Resource Coordination and Development | 298 | 93.130 | 177,151 | - |
| Injury Prevention and Control Research and State and Community Based Programs | various | 93.136 | 261,632 | 58,968 |
| Projects for Assistance in Transition from Homelessness ("PATH") | various | 93.150 | 321,703 | 300,000 |
| Hansen's Disease National Ambulatory Care Program | 264 | 93.215 | 725,483 | - |
| Family Planning – Services | 239 | 93.217 | 1,761,614 | 1,349,618 |
| Traumatic Brain Injury State Demonstration Grant Program | 434 | 93.234 | 83,305 | - |
| Abstinence Education Initiative | 273 | 93.235 | 128,475 | 4,000 |
| Cooperative agreements for State Treatment Outcomes and Performance Pilot Studies Enhancement | various | 93.238 | 80,841 | 80,000 |
| Rural Hospital Flexibility Program | 415 | 93.241 | 458,742 | 161,609 |
| Substance Abuse and Mental Health Services | various | 93.243 | 1,859,887 | 681,409 |
| Universal Newborn Hearing Screening | 416 | 93.251 | 97,234 | 19,073 |
| State Planning Grants Health Care Access for the Uninsured | various | 93.256 | 174,088 | 135,537 |
| Immunization Grants | various | 93.268 | 9,826,754 | 8,990,755 |
| Centers for Disease Control and Prevention | various | 93.283 | 8,949,681 | 1,505,650 * |
| Small Rural Hospital Improvement | 454 | 93.301 | 82,764 | 108,228 |
| Child Care and Development Block Grant | 244 | 93.575 | 64,367 | 60,455 |
| Community-Based Family Resource and Support Grants | 270 | 93.590 | 204,206 | 250,638 |
| Development Disabilities Basic Support and Advocacy Grants | 240 | 93.630 | 860,882 | 38,224 |
| State Survey and Certification of Health Care Providers and Suppliers | various | 93.777 | 1,491,864 | - * |
| Centers for Medicare and Medicaid Services Research, Demonstrations and Evaluations | various | 93.779 | 221,123 | 78,950 |
| National Bioterrorism Hospital Preparedness Program | 435 | 93.889 | 3,153,057 | 1,925,496 |
| Grants to States for Operation of Offices of Rural Health | 299 | 93.913 | 24,508 | 33,064 |
| HIV Care Formula Grants | 293 | 93.917 | 3,341,042 | 2,041,564 * |
| Healthy Start Initiative | various | 93.926 | 523,990 | 528,970 |
| HIV Prevention Project | 266 | 93.940 | 2,042,128 | 1,764,088 |
| HIV / AIDS Surveillance | various | 93.944 | 148,637 | - |
| Block Grants for Community Mental Health Services | various | 93.958 | 1,608,309 | 1,098,584 |
| Substance Abuse Prevention and Treatment Block Grants | various | 93.959 | 6,982,585 | 6,640,300 |
| Preventive Health Services – Sexually Transmitted Diseases Control Grants | 268 | 93.977 | 422,363 | - |
| Mental Health Disaster Assistance and Emergency Mental Health | 358 | 93.982 | 267,596 | - |
| Cooperative Agreements for State-Based Diabetes Control Programs and Evaluation of Surveillance System | 261 | 93.988 | 362,431 | 21,115 |
| Preventive Health and Health Services Block Grant | various | 93.991 | 823,505 | 94,183 |
| Maternal and Child Health Services Block Grant | various | 93.994 | 1,194,984 | 21,643 |
| Vital Statistics Cooperative Program | 285 | 93.200-89-7211 | 176,372 | - |
| Empowering Older People to Take More Control of Their Health | 357 | 93. | 113,440 | - |
| Drug and Alcohol Services Information System | 371 | 93. | 2,475 | - |
| Traumatic Brain Injury Planning Project | 295 | 93. | 99,299 | 94,557 |
| Other | 468 | 93. | 129,873 | - |
| Subtotal Direct Programs | | | 57,904,888 | 34,057,455 |
| Pass-through from the Department of Human Services | | | | |
| Temporary Assistance for Needy Families | various | 93.558 | 509,938 | - |
| Child Care and Development Block Grant | various | 93.575 | 300,586 | - |
| Association of Public Health Laboratories | 355 | 93. | 2,007 | - |
| Subtotal Pass-through Programs | | | 812,531 | - |
| Total Department of Health and Human Services | | | 58,717,419 | 34,057,455 |

* Denotes Major Federal Program

**State of Hawaii
Department of Health
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2007**

| Federal Grantor/Pass-Through Grantor/Program Title | Project Number | CFDA Contract, Award or Assistance ID Number | Federal Expenditures | Amount Provided to Subrecipient |
|---|----------------|--|-----------------------|---------------------------------|
| U.S. Department of Agriculture | | | | |
| Direct Program | | | | |
| Special Supplemental Nutrition Program for Women, Infants, and Children | 275 | 10.557 | 29,855,358 | 1,926,961 * |
| Total Department of Agriculture | | | 29,855,358 | 1,926,961 |
| Environmental Protection Agency ("EPA") | | | | |
| Direct Program | | | | |
| Air Pollution Control Program Support | 233 | 66.001 | 785,969 | - |
| Surveys, Studies, Investigations, Demonstrations and Special Purpose Activities Relating to the Clean Air Act | 294 | 66.034 | 76,338 | - |
| Water Pollution Control – State and Interstate Program Support | various | 66.419 | 1,037,304 | - |
| State Public Water System Supervision | 232 | 66.432 | 491,291 | - |
| Water Quality Management Program | 10284-11284 | 66.454 | 32,228 | - |
| Capitalization Grants for State Revolving Funds | 4206-15206 | 66.458 | 47,790,349 | 47,529,183 * |
| Nonpoint Source Implementation Grants | 3290-7289 | 66.460 | 1,125,455 | - |
| Capitalization Grants for Drinking Water State Revolving Funds | 2207-7207 | 66.468 | 21,323,556 | 20,639,089 * |
| Operator Certification Expense Grant | 310 | 66.471 | 40,000 | - |
| Beach Monitoring and Notification Program | various | 66.472 | 864,880 | - |
| Water Protection Coordination | 449 | 66.474 | 6,449 | - |
| Assessment and Watershed Protection Program Grants | 225 | 66.480 | 48,000 | - |
| Office of Research and Development, EPA | 408 | 66.511 | 57,620 | - |
| Water Infrastructure Oversight | 294 | 66.606 | 3,687 | - |
| Environmental Information Exchange Grant Program | 467 | 66.608 | 153,377 | - |
| Toxic Substances Compliance Monitoring Cooperative Agreements | 243 | 66.701 | 128,541 | - |
| TSCA Title IV State Lead Grants | 330 | 66.707 | 160,235 | - |
| Multi-Media Capacity Building Grants for States and Tribes | various | 66.709 | 21,469 | - |
| Hazardous Waste Management State Program Support | 230 | 66.801 | 559,249 | - |
| Superfund State Site Specific Cooperative Agreements | various | 66.802 | 273,482 | - |
| State Underground Storage Tanks Program ("UST" Program) | 220 | 66.804 | 168,974 | - |
| Leaking Underground Storage Tank ("LUST") Trust Fund Program | 258 | 66.805 | 347,602 | - |
| State Response Program Grants | 469 | 66.817 | 882,047 | - |
| Total Environmental Protection Agency | | | 76,378,102 | 68,168,272 |
| U.S. Department of Education | | | | |
| Pass through from the State Department of Education | | | | |
| Grants for Infants and Toddlers with Disabilities | 213 | 84.181 | 2,119,461 | 549,716 |
| State Improvement Grant II – Early Intervention | 481 | 84. | 19,967 | 17,431 |
| Total Department of Education | | | 2,139,428 | 567,147 |
| U.S. Department of Defense | | | | |
| Direct Program | | | | |
| Defense Environmental Restoration Program | 245 | 12.113 | 241,718 | - |
| State Homeland Security Grant | 470 | 12. | 26,890 | - |
| Total Department of Defense | | | 268,608 | - |
| U.S. Department of Justice | | | | |
| Direct Program | | | | |
| Enforcing Underage Drinking Laws Program | various | 16.727 | 137,141 | 135,032 |
| Other | 480 | 16. | 2,183 | - |
| Total Department of Justice | | | 139,324 | 135,032 |
| U.S. Department of Homeland Security | | | | |
| Direct Program | | | | |
| Crisis Counseling Immediate Services Program | 390 | 97.032 | 289,520 | - |
| Total Department of Homeland Security | | | 289,520 | - |
| Total Expenditures of Federal Awards | | | \$ 167,787,759 | \$ 104,854,867 |

* Denotes Major Federal Program

State of Hawaii
Department of Health
Notes to the Schedule of Expenditures of Federal Awards
Year Ended June 30, 2007

1. Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the State of Hawaii, Department of Health (the "Department"), and is presented on the cash basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, 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.

2. Loans Outstanding

The Department had the following loan balances outstanding at June 30, 2007. Loans made during the year are included in the federal expenditures presented in the schedule of expenditures of federal awards.

| Program Title | Federal CFDA Number | Amount Outstanding |
|---|--------------------------------|-------------------------------|
| Capitalization Grants for Clean Water State Revolving Funds | 66.458 | \$ 49,632,343 |
| Capitalization Grants for Drinking Water State Revolving Funds | 66.468 | 24,587,472 |

3. Noncash Awards

The Department also receives noncash awards in the form of vaccine that is provided to children for the Immunization Grants program. The Department expended \$7,380,228 in vaccines for the fiscal year ended June 30, 2007.

PART II
Government Auditing Standards

**Report of Independent Auditors on Internal Control Over
Financial Reporting and on Compliance and
Other Matters Based on an Audit of Financial Statements
Performed in Accordance with *Government Auditing Standards***

The Auditor
State of Hawaii

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Hawaii, Department of Health (the "Department") as of and for the year ended June 30, 2007, which collectively comprise the Department's basic financial statements and have issued our report thereon dated March 28, 2008. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying schedule of findings and questioned costs as Finding Nos. 07-01 and 07-02 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider Finding Nos. 07-01 and 07-02 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we have reported to the State Auditor and management of the Department in a separate letter dated March 28, 2008.

The Department's responses to the findings identified in our audit are described in the Department's Corrective Action Plan. We did not audit the Department's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the State Auditor, the Department's management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads "Accuity LLP". The signature is written in a cursive, flowing style.

Honolulu, Hawaii
March 28, 2008

PART III
OMB Circular A-133

**Report of Independent Auditors on Compliance with Requirements
Applicable to Each Major Program and on Internal Control Over Compliance
in Accordance with OMB Circular A-133**

The Auditor
State of Hawaii

Compliance

We have audited the compliance of the State of Hawaii, Department of Health (the "Department") 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 June 30, 2007. The Department's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Department's management. Our responsibility is to express an opinion on the Department'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 Department'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 the Department's compliance with those requirements.

As described in Finding No. 07-03 in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding Reporting that are applicable to its HIV Care Formula Grants Program, Centers for Disease Control and Prevention Investigations and Technical Assistance Program, State Survey and Certification of Health Care Providers and Suppliers, Capitalization Grants for Clean Water State Revolving Funds Program, and Capitalization Grants for Drinking Water State Revolving Funds Program. Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to those programs.

As described in Finding No. 07-04 in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding Eligibility that are applicable to its HIV Care Formula Grants Program. Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to that program.

As described in Finding No. 07-05 in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding Earmarking that are applicable to its HIV Care Formula Grants Program. Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to that program.

As described in Finding No. 07-06 in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding Procurement that are applicable to its HIV Care Formula Grants Program and Special Supplemental Nutrition Program for Women, Infants and Children. Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described above regarding the Department's compliance with the requirements for Reporting, Eligibility, Earmarking and Procurement, the Department complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2007. The results of our auditing procedures disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as Finding Nos. 07-07 through 07-10. We also noted certain other matters that we have reported to the State Auditor and management of the Department in a separate letter dated March 28, 2008.

Internal Control Over Compliance

The management of the Department 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 Department's internal control over compliance with the 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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the entity's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies and others that we consider to be material weaknesses.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as Finding Nos. 07-03 through 07-06 to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, we consider Finding Nos. 07-03 through 07-06 to be material weaknesses.

The Department's responses to the findings identified in our audit are described in the Department's Corrective Action Plan. We did not audit the Department's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the State Auditor, the Department's management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Accuity LLP

Honolulu, Hawaii
March 28, 2008

PART IV

Schedule Of Findings and Questioned Costs

**State of Hawaii
 Department of Health
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

Section I – Summary of Auditor’s Results

Financial Statements

| | |
|---|---------------|
| Type of auditor’s report issued: | Unqualified |
| Internal control over financial reporting: | |
| Material weakness(es) identified? | Yes |
| Significant deficiency(ies) identified that are not considered to be material weaknesses? | None reported |
| Noncompliance material to financial statements noted? | No |

Federal Awards

| | |
|--|---------------|
| Internal control over major programs: | |
| Material weakness(es) identified? | Yes |
| Significant deficiency(ies) identified that are not considered to be material weakness(es)? | None reported |
| Type of auditor’s report issued on compliance for major programs | Qualified |
| Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133? | Yes |

Identification of major programs:

| CFDA Number | Name of Federal Program or Cluster |
|------------------------|--|
| | U.S. Department of Health & Human Services |
| 93.283 | Centers for Disease Control and Prevention Investigations and Technical Assistance |
| 93.777 | State Survey and Certification of Health Care Providers and Suppliers |
| 93.917 | HIV Care Formula Grants |
| | U.S. Department of Agriculture |
| 10.557 | Special Supplemental Nutrition Program for Women, Infants & Children |
| | U.S. Environmental Protection Agency |
| 66.458 | Capitalization Grants for Clean Water State Revolving Funds |
| 66.468 | Capitalization Grants for Drinking Water State Revolving Funds |

| | |
|--|-------------|
| Dollar threshold used to distinguish between type A and type B programs: | \$3,000,000 |
| Auditee qualified as low-risk auditee? | No |

**State of Hawaii
 Department of Health
 Financial Statement Findings
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

II. Financial Statement Findings

| | | Questioned Cost |
|---|---|----------------------------|
| Finding No. 07-01: | Restatement of Beginning Fund Balance / Net Assets (Material Weakness) | \$ _____ - |
| Federal Agency: | Finding is not specific to a Federal Agency. | |
| CFDA Number and Title: | Finding is not specific to a Federal Agency. | |
| Award Number and Award Year: | Not applicable Not applicable | |

Finding and Cause and Effect

During our current year financial statement audit of the State of Hawaii, Department of Health (the "Department"), we identified an accounting error in the Department's basic financial statements as of and for the year ended June 30, 2006 due to the lack of oversight by fiscal management over the calculation of year end balances. Accordingly, the Department restated its opening net assets attributable to governmental activities and governmental funds fund balances as of July 1, 2006 to correct these errors which relate to the accounting for appropriations and amounts due from the Department of Human Services ("DHS").

The following table reconciles the net assets attributable to governmental activities at June 30, 2006, as previously reported, to the opening net assets attributable to governmental activities at July 1, 2006, as restated:

| | Governmental Activities |
|--|------------------------------------|
| Net assets at June 30, 2006, as previously reported | \$ 175,207,506 |
| Adjustments attributable to: | |
| Overstatement of allotments | (4,013,827) |
| Understatement of liabilities and expenses | (1,669,672) |
| Understatement of receivables | 31,549,351 |
| Net assets at July 1, 2006, as restated | <u>\$ 201,073,358</u> |

State of Hawaii
Department of Health
Financial Statement Findings
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007

The following table reconciles the governmental funds fund balances at June 30, 2006, as previously reported, to the opening governmental funds fund balances at July 1, 2006, as restated:

| | General Fund | Other Funds | Governmental Funds |
|---|-------------------------|------------------------|-------------------------------|
| Fund balances at June 30, 2006, as previously reported | \$ 7,333,197 | \$ 76,923,208 | \$ 125,977,127 |
| Adjustments attributable to: | | | |
| Overstatement of allotments | - | (4,013,827) | (4,013,827) |
| Understatement of liabilities and expenses | - | (1,669,672) | (1,669,672) |
| Understatement of receivables | 7,722,336 | - | 7,722,336 |
| Fund balances at July 1, 2006, as restated | \$ 15,055,533 | \$ 71,239,709 | \$ 128,015,964 |

Bond Fund Appropriations

During our review of the appropriations recorded by the Department, we noted that there were several appropriations that were included on the Department's Financial Accounting and Management Information System ("FAMIS") reports as of June 30, 2006 that were not appropriated by the Legislature to the Department. These appropriations should have been recorded by another State agency. Through inquiry and confirmation with the Department of Accounting and General Services ("DAGS"), these appropriations amounting to approximately \$4.0 million were mistakenly included on the Department's FAMIS report, and should have been on the other State agency's report. The Department should be reviewing the FAMIS reports to ensure that the accounts allocated to them are the property of the Department.

Due from DHS

During our testing we noted that there were various reimbursements related to the State's Medicaid program that were being recorded as revenue when received rather than earned. DHS is the State's Medicaid Agency, and is the State's authorized agency to request reimbursement for qualifying Medicaid reimbursements. These reimbursements should be accrued when they are due to the Department. The error resulted in a \$31.5 million understatement of receivables from DHS. This amount is comprised of a \$13.6 million receivable for the Developmental Disabilities/Mental Retardation ("DD/MR") Waiver program and \$17.9 for other Medicaid rehabilitation option claims.

Criteria

§__310 of OMB Circular A-133 requires the auditor to prepare financial statements that reflect its financial position, results of operations or changes in net assets and, where appropriate, cash flows for the fiscal year audited.

§__320 requires the auditor to submit a reporting package that includes:

- (1) Financial statements and schedule of expenditures of federal awards.
- (2) Summary schedule of prior audit findings.
- (3) Auditor's report.
- (4) Corrective action plan.

State of Hawaii
Department of Health
Financial Statement Findings
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007

Although audited financial statements were prepared and submitted as of and for the year ended June 30, 2006, the financial statements submitted were misstated, and restated beginning balances are reported in the financial statements as of and for the year ended June 30, 2007.

Recommendation

We recommend that, and the Department has already, restated the beginning balances in its basic financial statements for the year ended June 30, 2007 to correct the error identified. We also recommend that fiscal management of the Department provide greater oversight to ensure that the basic financial statements are prepared and presented in accordance with generally accepted accounting principles ("GAAP").

**State of Hawaii
 Department of Health
 Financial Statement Findings
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | Questioned Cost |
|-------------------------------------|--|--------------------|
| Finding No. 07-02: | Capital Assets (Material Weakness) | \$ _____ – |
| Federal Agency: | Finding is not specific to a Federal Agency. | |
| CFDA Number and Title: | Finding is not specific to a Federal Agency. | |
| Award Number and Award Year: | Not applicable | Not applicable |

Finding and Cause and Effect

In prior year audits (starting with the fiscal year 2004 audit), it was noted that the Department did not properly report capital purchases in accordance with the State's policies and procedures. It was recommended that the Department report capital asset additions to the State Procurement Office ("SPO") in a timely manner in accordance with the DAGS – SPO – Inventory Management Branch Training Manual ("State Inventory Manual"). It was also recommended that the Department implement a procedure for property custodians to reconcile quarterly equipment acquisitions in FAMIS to the DAGS computerized inventory reports ("MDB reports") from the State's Fixed Asset Inventory System ("FAIS") in a timely manner.

During our current year audit, we noted that the Department implemented procedures to assist the individual programs in recording capital purchases to FAIS in a timely manner by sending each program a detailed listing of all fixed assets purchases recorded to FAMIS on a quarterly basis. The programs are responsible for reconciling this listing to the FAIS inventory reports. However, we noted instances where the reconciliation was not performed and discrepancies were not resolved. Therefore, we continued to note instances where capital assets were purchased, but not reported in FAIS, resulting in an audit adjustment.

We also noted that the Department is not reporting assets in accordance with the State Inventory Manual, resulting in another audit adjustment. The following was noted during testing:

- Two (2) instances where the asset was recorded by two different programs due to one program purchasing the asset to be used by another program and both programs recording the asset.
- Expenditures were improperly charged to a non-fixed asset object code, resulting in the asset not being properly classified in FAMIS and hindering audit testing
- Improper recording of transfers between programs
 - Eight (8) instances where the transfers were not recorded
 - Four (4) instances where transfers were not recorded in the proper period
 - Four (4) instances where transfers were improperly coded in FAIS

**State of Hawaii
Department of Health
Financial Statement Findings
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007**

Criteria

The Department is required to follow guidance set forth in the State Inventory Manual issued by the Inventory Management Office. The State Inventory Manual is the guide for all State agencies to establish State-wide controls for fixed assets purchased with State and Federal funds. In order for the Department to ensure that their financial records related to fixed assets are properly recorded in FAIS, all of the Department's programs need to comply with the State Inventory Manual.

Recommendations

We continue to recommend that the Department report capital assets to the SPO in a timely manner in accordance with the State Inventory Manual. We also recommend the Department continue to provide listings of fixed assets expenditures recorded in FAMIS to the individual programs and implement a procedure for property custodians to reconcile these expenditures to the FAIS inventory reports and resolve any discrepancies. We recommend that the Department carefully review expenditures to ensure fixed assets are properly recorded to minimize the need for future audit adjustments for misreported assets.

State of Hawaii
Department of Health
HIV Care Formula Grant
Centers for Disease Control and Prevention –
National Cancer Prevention and Control Branch
State Survey and Certification of Health Care Providers and Suppliers
Capitalization Grants for Clean Water State Revolving Funds
Capitalization Grants for Drinking Water State Revolving Funds
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007

Section III. Federal Award Findings and Questioned Costs

| | | Questioned Cost |
|---|---|----------------------------|
| Finding No. 07-03: | Reporting (Material Weakness) | \$ _____ – |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | Environmental Protection Agency ("EPA") 93.917 – HIV Care Formula Grants ("HIV Care") | |
| | 93.283 – Centers for Disease Control and Prevention Investigations and Technical Assistance | |
| | 93.777 – State Survey and Certification of Health Care Providers and Suppliers | |
| | 66.458 – Capitalization Grants for Clean Water State Revolving Funds | |
| Award Number and Award Year: | 66.468 – Capitalization Grants for Drinking Water State Revolving Funds 2 X07HA00050-15-00 4/1/06 – 3/31/07 | |
| | CS-1500010X-X, 10/1/92 – 6/30/17 CS-1500019X-X | |
| | 1-996000449-A4 10/1/05 – 9/30/06 10/1/06 – 9/30/07 | |
| | FS-9998659X-1, 9/24/98 – 6/30/17 FS-99986500-1, FS-9998650X-0 | |

**State of Hawaii
Department of Health
HIV Care Formula Grant
Centers for Disease Control and Prevention –
National Cancer Prevention and Control Branch
State Survey and Certification of Health Care Providers and Suppliers
Capitalization Grants for Clean Water State Revolving Funds
Capitalization Grants for Drinking Water State Revolving Funds
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007**

Finding and Cause and Effect

During our current year audit, we noted the following instances of noncompliance with federal reporting requirements for the HIV Care program:

- Maintenance of Effort Report: The amount of State expenditures for FY 2005 was incorrectly reported as \$4,990,742 compared to \$4,378,512 in actual expenditures.
- Maintenance of Effort Report: The amount of State expenditures for FY 2006 was incorrectly reported as \$4,990,742 compared to \$4,494,978 in actual expenditures.

The reporting errors for the Maintenance of Effort Report were partially caused by the erroneous inclusion of encumbrances. State effort should be measured solely by expenditures made in the fiscal year. Also, it is improper to limit the amount of expenditures reported in the current year to the amount reported in the prior year. Total expenditures for all years must be accurately reported. Reporting errors are also caused by the program not having formalized processes in place to monitor invoices and actual expenditures. Reports were prepared based on budgeted amounts and outdated reports resulting in inaccurate reports submitted to the Federal government.

- Third Quarter AIDS Drug Assistance Program (“ADAP”) Quarterly Report: The amount of State contribution was incorrectly reported as \$126,845 compared to \$116,845 in actual expenditures.
- The Annual Financial Status Reports, Standard Form (“SF”)-269a was submitted approximately two months after the due date.
- The Final Annual Progress Report was submitted approximately one month after the due date.
- The Mid-Year Progress Report was submitted twenty days after the due date.
- The second quarter ADAP Quarterly Report was submitted twenty-three days after the due date.
- The PSC 272 Federal Cash Transaction Report was submitted approximately one month after the due date.
- The Report on Women, Infants, Children and Youth (“WICY”) was submitted three days after the due date.
- The Final Report on the Use of Minority AIDS Initiative (“MAI”) funds was submitted three days after the due date.

**State of Hawaii
Department of Health
HIV Care Formula Grant
Centers for Disease Control and Prevention –
National Cancer Prevention and Control Branch
State Survey and Certification of Health Care Providers and Suppliers
Capitalization Grants for Clean Water State Revolving Funds
Capitalization Grants for Drinking Water State Revolving Funds
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007**

- Per the subrecipient's, AIDS Community Care Team ("ACCT"), audit report for the year ended June 30, 2006, which was received by the HIV Care program in October 2007, we noted that the ACCT had not submitted any reports to the Department regarding the monitoring of ACCT's subrecipients or the results thereof.

We also noted the following instances of noncompliance during our testing of the Centers for Disease Control and Prevention Investigations and Technical Assistance program – National Cancer Prevention and Control Branch ("NCPB"):

- As of January 14, 2008, we noted that the Administrative Services Office ("ASO") had not submitted the SF-269 report for the period June 30, 2006 to June 29, 2007, due on September 29, 2007. Due to a staffing shortage and other personnel changes, the Department's ASO, which prepares the reports, failed to prepare the report.
- The Interim Annual Progress Report due on January 30, 2007 was submitted approximately 15 days after the due date.
- The two quarterly PSC 272 Federal Cash Transaction Reports tested were submitted approximately 10 days after the due date.
- In our testing of the timeliness of the SF-269 reports, we noted that the interim report, dated February 2007, was not submitted until the end of May 2007, which is two days over the allotted time for submission of the report. We also noted that prior year's final report was not submitted until the end of November 2006, which is one day after the allotted submission deadline.

We also noted the following matter during our testing of the State Survey and Certification of Health Care Providers and Suppliers program:

- For 2 out of 2 Quarterly CMS-64 reports submitted, we were unable to find adequate documentation for the amounts reported.

The lack of documentation was due to a change in personnel that resulted in a loss of the supporting documentation.

Finally, we also noted the following instances of noncompliance during our testing of the Clean Water State Revolving Fund and Drinking Water State Revolving Fund programs:

- As of September 30, 2007, we noted that the ASO had not submitted the SF-272 report for the period July 1, 2006 to December 31, 2006, due on January 15, 2007. Due to a staffing shortage and other personnel changes, the Department's ASO failed to prepare the report.

The untimely reporting was due to the lack of a formal procedure to monitor report submissions.

**State of Hawaii
Department of Health
HIV Care Formula Grant
Centers for Disease Control and Prevention –
National Cancer Prevention and Control Branch
State Survey and Certification of Health Care Providers and Suppliers
Capitalization Grants for Clean Water State Revolving Funds
Capitalization Grants for Drinking Water State Revolving Funds
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007**

As the programs are not in compliance with grant award and federal requirements, there is a risk the Federal government will withhold future funds from the respective programs.

Criteria

Each grant document details the reporting requirements for the respective grant year. There are various requirements and deadlines for each report and these are also detailed in the grant agreements. Failure to comply with the reporting requirements may result in deferral or additional restrictions of future funding decisions.

Recommendations

We recommend that program personnel develop and implement procedures to ensure that accurate and complete financial and performance reports are submitted to the awarding agencies. Supporting documentation should be retained and filed in order to ensure the accuracy of data reported as of the relevant date.

We recommend that ASO and the respective program personnel maintain a calendar or spreadsheet with all reporting requirements and submission deadlines, in order to ensure compliance with federal requirements. In the case of a staffing shortage, ASO and program management should ensure that the reports are submitted by another competent individual. Program personnel responsible for reporting should be provided with adequate training and supervision by management.

**State of Hawaii
 Department of Health
 HIV Care Formula Grants
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | |
|---|--|----------------------------|
| | | Questioned Cost |
| Finding No. 07-04: | Eligibility (Material Weakness) | \$ _____ - |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | 93.917 – HIV Care Formula Grants | |
| Award Number and Award Year: | 2 X07HA00050-16-00 4/1/06 – 3/31/07 2 X07HA00050-17-00 4/1/07 – 3/31/08 | |

Finding and Cause and Effect

During our current year audit, we tested 40 ADAP patient records and 9 H-COBRA patient records. Due to the Department maintaining insufficient supporting documents, we noted the following instances of noncompliance with eligibility requirements for the HIV Care program:

- For 11 out of 40 patient records tested, the program was unable to provide documentation to evidence the eligibility (estimated value of liquid assets) of the ADAP participants.
- For 9 out of 9 patient records tested, the program was unable to provide adequate documentation to evidence the eligibility (estimated value of liquid assets) of H-COBRA participants.
- For 20 out of 40 ADAP patient records tested, the program was unable to provide documentation to evidence that 6-month recertifications were performed.
- For 4 out of 40 patient records tested, the program was unable to provide documentation to evidence the eligibility (State of Hawaii residency requirement and gross income requirement) of the ADAP participants.

We noted that the program has taken steps to remediate this recurring finding from prior years (Finding No. 06-02 and No. 05-02). However, as the program is still in the process of implementing our recommendations, the program did not meet the Eligibility requirements in fiscal 2007.

Criteria

Title 42, Section 300ff-26(b) of the U.S. Code requires that the Department ensure that eligible individuals receive assistance. In order to qualify for assistance, an individual must have a medical diagnosis of HIV disease and be a low-income individual, as defined by the State.

The Notice of Grant Award to the ADAP, the Health Resources and Services Administration ("HRSA") of DHHS expects all Title II grantees to implement an ADAP recertification process to ensure that individuals remain eligible to receive assistance. At a minimum, an individual is required to be recertified every six months to ensure that the program only services eligible clients.

**State of Hawaii
Department of Health
HIV Care Formula Grants
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007**

Recommendation

We recommend that the Department take the following actions:

- Program personnel should conduct initial eligibility certifications and semi-annual eligibility recertifications of all participants as required by federal and State program guidelines. In addition, program personnel should review all case files without exception to ensure that all participant files contain the required documentation.
- Program personnel should develop and implement a formal participant acceptance process and thoroughly train program staff (and case managers) on how to review applications for eligibility for the H-COBRA program. This process and training should resemble procedures recently implemented in the ADAP program. All documentation supporting participant eligibility should be retained.

**State of Hawaii
 Department of Health
 HIV Care Formula Grants
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | |
|---|---|----------------------------|
| | | Questioned Cost |
| Finding No. 07-05: | Earmarking (Material Weakness) | \$ <u>140,659</u> |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | 93.917 – HIV Care Formula Grants | |
| Award Number and Award Year: | 2 X07HA00050-15-00 4/1/06 – 3/31/07 | |

Finding and Cause and Effect

During our current year audit of the HIV Care program, we noted the following instances of noncompliance with earmarking requirements for amounts expended on women, infants, children and youth during the grant period. The amount expended was \$261,645, which was \$140,659 less than required by terms of the applicable grant. The shortfall was due primarily to the fact that the need for services for women, infants and children is less than the amount of funds available.

Criteria

Part Four of the March 2007 Compliance Supplement states:

"For the purpose of providing health and support services to women, youth, infants, and children with HIV disease, including treatment measures to prevent the prenatal transmission of HIV, a State shall use for each of these populations not less than the percentage of Title II funds in a fiscal year constituted by the ratio of the population involved (women, youth, infants, or children) in the State with AIDS to the general population in the State of individuals with AIDS [42 USC 300ff-21(b)]. This information is provided to the State by HRSA in the annual application guidance (Appendix II, Estimated Number/Percent of Women, Infants, and Children Living with AIDS in States and Territories)."

Per the HRSA application guidance, the percentage of women, infants, children, and youth living with AIDS in Hawaii to the total population with AIDS in Hawaii should be multiplied against the total amount of Ryan White Care Act Title II funds expended for the grant year in determining the required earmark. Therefore, as 12.2% of the total population of people with AIDS in Hawaii are women, infants, children, and youth, the required earmark for the April 1, 2006 through March 31, 2007 grant year was \$402,304.

Recommendation

We recommend that program personnel develop and implement procedures to monitor expenditures for specific purposes and ensure compliance with earmarking provisions. Program personnel responsible for monitoring compliance with earmarking provisions should continue to ensure that the providers are aware that the funding is available, should the need arise.

**State of Hawaii
 Department of Health
 HIV Care Formula Grants
 Special Supplemental Nutrition Program for Women, Infants, and Children
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | Questioned Cost |
|---|--|----------------------------|
| Finding No. 07-06: | Procurement (Material Weakness) | \$ _____ |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | Department of Agriculture ("USDA") 93.917 – HIV Care Formula Grants 10.557 – Special Supplemental Nutrition Program for Women Infants and Children ("WIC") | |
| Award Number and Award Year: | 2 X07HA00050-16-00 4/1/06 – 3/31/07 2 X07HA00050-17-00 4/1/07 – 3/31/08 | |

Finding and Cause and Effect

During our testing of procurement and suspension and debarment requirements for the HIV Care program, we noted two instances of noncompliance with federal requirements:

- While procurement personnel ensure that the awardees are not suspended or debarred by the State, there were no procedures in place to ensure that the program does not execute contracts with federally suspended or debarred parties.
- Per the AIDS Community Care Team ("ACCT") Circular A-133 audit reports for the years ended June 30, 2006 and June 30, 2007, which were received by the HIV Care program in October and November 2007, respectively, we noted that the ACCT does not have a written policy or procedures for the procurement of supplies, and other expendable property, equipment, real property and other non-contractual services with Federal funds to ensure that such materials and services are obtained in an effective manner and in compliance with the provisions of applicable Federal statutes. It was also noted that the ACCT did not document any procedures for procurement transactions. Without supporting documentation of procurement procedures, the ACCT risks non-compliance with Federal Guidelines.

The Department's HIV/STD Prevention Branch has not yet issued a management decision as ACCT's audit reports were received in October and November 2007.

**State of Hawaii
Department of Health
HIV Care Formula Grants
Special Supplemental Nutrition Program for Women, Infants, and Children
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007**

During our testing of the WIC grants, we noted one instance of noncompliance with federal requirements:

- For contracts executed by the program, contract personnel have policies and procedures in place to ensure that the program does not execute contracts with parties that are debarred, suspended, proposed for debarment, declared ineligible, or voluntarily excluded from covered transaction by a Federal department or agency in accordance with 45 CFR Part 76. However, for contracts executed by the SPO on behalf of the program, procurement personnel have procedures to ensure that the awardees are not suspended or debarred by the State, but there are no procedures in place to ensure that the program does not execute contracts with federally suspended or debarred parties.

Although we noted that the awardees of the HIV Care program and WIC program contracts tested were not on the federal suspension or debarment listing, without proper controls in place, there is a risk that the program will enter into a procurement contract with a suspended or debarred party.

Criteria

In accordance with 2 CFR 180, non-federal entities are prohibited from contracting with or making subawards under covered transactions to parties that are suspended or debarred or whose principals are suspended or debarred. Covered transactions include those procurement contracts for goods and services awarded under a nonprocurement transaction (e.g., grant or cooperative agreement) that are expected to equal or exceed \$25,000. When a non-federal entity enters into a covered transaction with an entity, the non-federal entity must verify that the entity is not suspended or debarred or otherwise excluded. This verification may be accomplished by checking the *Excluded Parties List System ("EPLS")* maintained by the General Services Administration ("GSA"), collecting a certification from the entity, or adding a clause or condition to the contract.

OMB Circulars A-102 and A-110 requires all non-federal entities to follow federal laws and implement regulations applicable to procurements.

Recommendation

We recommend that the program designate an individual to check the awardees of federally funded contracts to the EPLS maintained by the GSA at www.epls.gov. The designated program personnel should also ensure proper documentation is maintained to evidence review of the EPLS.

We understand the contracts in question were procured by the SPO. Therefore, as the SPO sometimes procures goods or services on behalf of the program, we also recommend that the programs inform the SPO when an award is federally funded and work with the SPO to establish who is responsible for ensuring that all federal, as well as State, procurement requirements are met.

We also recommend that the programs issue a management decision on the subrecipient's audit findings within six months after receipt of the respective subrecipient audit report and work with ACCT to ensure that it takes timely and appropriate corrective action on the finding noted.

**State of Hawaii
 Department of Health
 HIV Care Formula Grant
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | |
|---|--|----------------------------|
| | | Questioned Cost |
| Finding No. 07-07: | Allowable Costs | \$ <u>8,000</u> |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | 93.917 – HIV Care Formula Grants | |
| Award Number and Award Year: | 2 X07HA00050-16-00 4/1/06 – 3/31/07 2 X07HA00050-17-00 4/1/07 – 3/31/08 | |

Finding and Cause and Effect

The ACCT A-133 audit reports for the years ended June 30, 2006 and June 30, 2007 were prepared by another auditor and received by the HIV Care program in October and November 2007, respectively. While reviewing the reports, we noted several instances of noncompliance with allowable cost requirements:

- The reports stated that ACCT management’s allocation of salary taxes and benefits did not match actual time spent by employees. However, no questioned costs were reported.
- ACCT charged to the program approximately \$4,000 in allowable costs related to penalties and interest to the program in fiscal years 2006 and 2007. Approximately \$2,000 was charged to Contracts # 03-218 and #06-162 in fiscal year 2006 and approximately \$2,000 in penalties and interest expense to Contract #06-162.
- ACCT program was reimbursed for approximately \$4,000 in unallowable costs for lease payments which were paid to a related entity. To record lease payments, the ACCT wrote a check for the lease payments out of one account and deposited the payment into another ACCT account which the ACCT utilizes for the related entity.

We note that the HIV/STD Prevention Branch has not yet issued a management decision as the A-133 audit reports were received in October and November 2007.

We noted that the subrecipient’s noncompliance affects this program’s ability to comply with Allowable Costs/Cost Principle requirements as stated in the OMB Circular A-133.

**State of Hawaii
Department of Health
HIV Care Formula Grant
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007**

Criteria

In accordance with Part 3 of the March 2007 OMB Circular A-133 Compliance Supplement (the "Compliance Supplement"), a non-profit recipient of federal awards must follow the principles stated in OMB Circular A-122 *Cost Principles for Non-Profit Organizations*:

- Circular A-122, Attachment B "Selected Items of Cost, Item 7 Compensation for personal services, paragraph m Support of salaries and wages (2)(a)" states,

 "The reports must reflect an after-the-fact determination of the actual activity of each employee. Budget estimates (i.e., estimates determined before the services are performed) do not qualify as support for charges to awards."
- The costs of fines and penalties resulting from violations of, or failure of an entity to comply with federal, state, and local laws and regulations are unallowable
- General Criteria, 1. "Basic Considerations to determine Cost, (b) Allowable Costs" states,

 "A cost is allowable under an award if the cost meets the following general criteria: (1) Be reasonable for the performance of the award and be allocable in accordance with A-122. (a) A cost is reasonable if, in its nature or amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. Consideration should be given to:...(ii) The restraints or requirements imposed by such factors as generally accepted sound business practices, arms length bargaining, Federal and State laws and regulations, and terms and conditions of the award."

Recommendation

We recommend that the program issue a management decision on these audit findings within six months after receipt of the respective subrecipient audit report. We also recommend that the program ensures that the subrecipient takes timely and appropriate corrective action on the audit findings noted.

**State of Hawaii
 Department of Health
 HIV Care Formula Grants
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | |
|---|---|----------------------------|
| | | Questioned Cost |
| Finding No. 07-08: | Equipment Management | \$ _____ - |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | 93.917 – HIV Care Formula Grants | |
| Award Number and Award Year: | 2 X07HA00050-16-00 4/1/06 – 3/31/07 | |

Finding and Cause and Effect

Per ACCT's Circular A-133 audit report for the year ended June 30, 2006, which was prepared by another auditor and received by the HIV Care program in October 2007, we noted that ACCT does not maintain a perpetual detailed record of equipment, nor inventory equipment at least once every two years.

ACCT risks the improper reporting, disposal, and ultimate remittance of equipment purchased with Federal Awards and affects the program's ability to comply with Equipment Management requirements as stated in OMB Circular A-133.

We note that the HIV/STD Prevention Branch has not issued a management decision as the ACCT audit report was received in October 2007.

We noted that the subrecipient's noncompliance affects this program's ability to comply with Equipment Management requirements as stated in OMB Circular A-133.

Criteria

In accordance with Part 3 of OMB Circular A-133, Compliance Requirement F Equipment and Real Property Management, "Equipment records shall be taken at least once every two years and reconciled to the equipment record."

Recommendation

We recommend that the program issue a management decision on these audit findings within six months after receipt of ACCT's audit report. We also recommend that the HIV Care program ensures that the subrecipient takes timely and appropriate corrective action on the audit findings noted.

**State of Hawaii
 Department of Health
 HIV Care Formula Grants
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | |
|---|---|----------------------------|
| | | Questioned Cost |
| Finding No. 07-09: | Subrecipient Monitoring | \$ _____ - |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | 93.917 – HIV Care Formula Grants | |
| Award Number and Award Year: | 2 X07HA00050-16-00 4/1/06 – 3/31/07 | |

Finding and Cause and Effect

During our testing of subrecipient monitoring, we noted the subrecipient did not submit its OMB Circular A-133 audit report for fiscal year 2006 in a timely basis. We note the HIV Care program failed to communicate a need for the timely submittal of the A-133 report. This failure to communicate Federal guidelines indicates a deficiency of the HIV Care program’s subrecipient monitoring process.

Criteria

In accordance with Part 3 of the March 2007 OMB Circular A-133 Compliance Supplement, the program should monitor the subrecipient’s use of Federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved. Ensuring that subrecipients receive an audit in accordance with OMB Circular A-133 is specifically stated as a requirement:

“(1) Ensuring that subrecipients expending \$500,000 or more in Federal awards during the subrecipient’s fiscal year for fiscal years ending after December 31, 2003 (or \$300,000 prior to that date) as provided in OMB Circular A-133 have met the audit requirements of OMB Circular A-133 . . . and that the required audits are completed within 9 months of the end of the subrecipient’s audit period; (2) issuing a management decision on audit findings within 6 months after receipt of the subrecipient’s audit report; and (3) ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings. In cases of continued inability or unwillingness of a subrecipient to have the required audits, the pass-through entity shall take appropriate action using sanctions.”

Recommendation

We recommend that the HIV program communicate Federal guidelines in writing to the subrecipient and work with the subrecipient to ensure all federal requirements are met.

We noted that the subrecipient subsequently obtained an audit in accordance with OMB Circular A-133 for its fiscal years ended June 30, 2006 and 2007. The Department received the audit reports in October and November 2007, respectively. Numerous findings were reported in both audit reports. However, management has not yet issued a management decision on the audit findings. Therefore, we recommend that HIV program issue its management decision within six months of receiving the reports.

**State of Hawaii
 Department of Health
 Centers for Disease Control and Prevention –
 National Cancer Prevention and Control Branch
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | |
|---|---|----------------------------|
| | | Questioned Cost |
| Finding No. 07-10: | Equipment Management | \$ _____ – |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | 93.283 – Centers for Disease Control and Prevention Investigations and Technical Assistance | |
| Award Number and Award Year: | U55/CCU922046-04 6/30/06 – 6/29/07 | |

Finding and Cause and Effect

During our testing of compliance over equipment management for the programs listed above, we noted that the NCPC program did not update the FAIS records to ensure additions, transfers, and disposals were properly reflected in a timely manner. This is a violation of the State's equipment management policies and procedures established in the State Inventory Manual.

The lack of enforcement by management to comply with the State's equipment management policies and procedures resulted in the noncompliance noted above.

Criteria

40 CFR 31.32 states that a state will use, manage, and dispose of equipment acquired in accordance with the state's laws and procedures.

Per the Inventory System User Manual issued by the SPO, Chapter 9, at the end of each quarter, but no later than the 15th of the following month, the designated property custodian submits AGS Form 17-A (Detail Inventory of Property) to the Inventory Management Office, reporting all property acquisition and changes to their master inventory balances.

Recommendation

We recommend that management of the Department ensure that all divisions and programs adhere to the State's established policies and procedures over equipment management in order to comply with Federal and State regulations.

**State of Hawaii
 Department of Health
 Centers for Disease Control and Prevention –
 National Cancer Prevention and Control Branch
 Schedule of Findings and Questioned Costs
 Year Ended June 30, 2007**

| | | |
|---|---|----------------------------|
| | | Questioned Cost |
| Finding No. 07-11: | Eligibility | \$ _____ – |
| Federal Agency: | Department of Health and Human Services ("DHHS") | |
| CFDA Number and Title: | 93.283 – Centers for Disease Control and Prevention Investigations and Technical Assistance | |
| Award Number and Award Year: | U55/CCU922046-04 6/30/06 – 6/29/07 | |

Finding and Cause and Effect

The program allows women to self-certify as to their eligibility for the program on the "Statement of Eligibility to Participate." The certification is often the program's only evidence of participants' eligibility to receive benefits from this grant and is acceptable evidence, per discussion with DHHS program personnel. Patient data is compiled and tracked in the CAST data collection system and submitted to the Centers for Disease Control ("CDC") for compliance monitoring purposes. During our testing for compliance with eligibility requirements, we noted the following matters:

- For 1 out of 40 patient files tested, the "Statement of Eligibility to Participate" did not include the patient's date of birth;
- For 1 out of 40 patient files tested, the "Statement of Eligibility to Participate" did not include the patient's average monthly income; and
- For 1 out of 40 patient files tested, the incorrect birth dates for the patients were documented in the "Statement of Eligibility to Participate".

The matters described above were the result of a lack of thorough review of completed statements by program personnel and service providers.

Failure to ensure that patients meet federal eligibility requirements could result in the rendering of services to an excessive number of patients and inaccurate statistical data being reported in the CAST system.

Criteria

Title 42, *The Public Health and Welfare Chapter 6a. The Public Health Service Preventive Health Measures with Respect to Breast and Cervical Cancers 42 U.S.C. § 300n*, states that to be eligible to receive assistance from the Program, priority should be given to underserved women, including those who are older, have low incomes, or are members of racial and ethnic minority groups. Program Announcement 02060 further establishes low income women as being at or below 250% of the Federal poverty level and uninsured and underinsured. To ensure that the patient meets the low income requirement, patients are required to fill out a "Statement of Eligibility to Participate" form.

**State of Hawaii
Department of Health
Centers for Disease Control and Prevention –
National Cancer Prevention and Control Branch
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007**

Recommendation

We recommend that the NCPC Branch ensure that service providers obtain complete and accurate Statements of Eligibility to Participate forms from patients. Program personnel should also independently review the certifications for timely completion and compliance with eligibility requirements.

PART V

Prior Year Findings And Questioned Costs

This section updates the status of findings and questioned costs that were reported in prior years. Finding numbers relate to the sequence reported in the respective year.

**State of Hawaii
 Department of Health
 Financial Statement Findings
 Status of Prior Year Findings and Questioned Costs
 Year Ended June 30, 2007**

Finding No. 06-01: Restatement of Beginning Fund Balance / Net Assets (Material Weakness)

During our prior year financial statement audit of the Department, we identified an accounting error in the Department's basic financial statements as of and for the year ended June 30, 2005 due to the lack of oversight by fiscal management over the calculation of the Deposit Beverage Container Fund's year end vouchers and contracts payable balance and related expenditures for fiscal year 2005. Accordingly, the Department restated its opening net assets attributable to governmental activities and governmental funds fund balances as of July 1, 2005 to correct the error.

The following table reconciles the net assets attributable to governmental activities at June 30, 2005, as previously reported, to the opening net assets attributable to governmental activities at July 1, 2005, as restated:

| | Governmental Activities |
|---|------------------------------------|
| Net assets at June 30, 2005, as previously reported | \$ 168,635,472 |
| Adjustment attributable to understatement of liabilities and expenses | <u>(1,404,727)</u> |
| Net assets at July 1, 2005, as restated | <u>\$ 167,230,745</u> |

The following table reconciles the governmental funds fund balances at June 30, 2005, as previously reported, to the opening governmental funds fund balances at July 1, 2005, as restated:

| | Deposit Beverage Container Fund | Governmental Funds |
|---|--|-------------------------------|
| Fund balances at June 30, 2005, as previously reported | \$ 15,187,384 | \$ 115,221,916 |
| Adjustment attributable to understatement of liabilities and expenses | <u>(1,404,727)</u> | <u>(1,404,727)</u> |
| Fund balances at July 1, 2005, as restated | <u>\$ 13,782,657</u> | <u>\$ 113,817,189</u> |

We recommended that the Department restate the beginning balances in its basic financial statements for the year ended June 30, 2006 to correct the error identified. We also recommend that fiscal management of the Department provide greater oversight to ensure that the basic financial statements are prepared and presented in accordance with GAAP.

Status

Unresolved. The restated June 30, 2005 balances were properly reported in the fiscal 2006 financial statements. Therefore, this finding will not carry forward. However, other financial statement errors were noted during our current year audit which resulted in restatement of \$31,546,558 related to appropriations and DHS receivables that were not properly recorded. See current year Finding No. 07-01.

**State of Hawaii
Department of Health
Financial Statement Findings
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007**

Finding No. 04-01: Fixed Assets

During the fiscal year 2004 audit, it was recommended that the Department report capital asset additions to the State in a timely manner in accordance with the State Inventory Manual. It was also recommended that the Department implement a procedure for property custodians to reconcile quarterly equipment acquisitions in the State's FAMIS to MDB reports in a timely manner.

Status

Unresolved. During our current year financial audit, we continued to note numerous instances where capital assets were purchased, but not reported in FAIS. Since the Department is in the process of implementing our recommendation above in conjunction with its implementation of our recommendation in the current year Finding No. 07-02, this finding will not carry forward.

**State of Hawaii
Department of Health
HIV Care Formula Grant
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007**

Finding No. 06-02: Eligibility Requirements (Material Weakness)

During our prior year audit, we tested 30 patient records. Due to the Department maintaining insufficient supporting documents, we noted the following instances of noncompliance with eligibility requirements for the HIV Care Formula Grants:

- For 26 out of 30 patient records tested, the program was unable to provide documentation to evidence the eligibility of the ADAP participants.
- For all 4 patient records tested, the program was unable to provide documentation to evidence the eligibility of H-COBRA participants.
- For 24 out of 30 ADAP patient records tested, the program was unable to provide documentation to evidence that 6-month verbal recertifications were performed.
- For 19 out of 30 ADAP patient records tested, the program was unable to provide documentation to evidence that 12-month semi-annual recertifications were performed.

The program has taken steps to remediate this recurring finding from the prior year (Finding No. 05-02). However, due to the timing of the completion of the fiscal 2005 audit, the program was unable to implement our recommendations and meet the Eligibility requirements in fiscal 2006.

We recommended that the Department take the following actions:

- Program personnel should develop and implement a formal participant acceptance process and thoroughly train program staff (and future case managers) on how to review applications for eligibility. All documentation supporting participant eligibility should be retained.
- Program personnel should develop and implement a single comprehensive participant application form for the ADAP and H-COBRA programs. Program personnel should all be knowledgeable of the necessary information to be included in the application and work with participants to ensure that applications are accurately completed.
- Program personnel should conduct semi-annual eligibility recertifications of all participants as required by federal and State program guidelines. In addition, program personnel should review case files periodically to ensure that all participant files contain the required documentation.

Status

Unresolved. Similar instances were noted during our current year audit. Since the Department is in the process of implementing our recommendation above in conjunction with its implementation of our recommendation in current year Finding No. 07-04, this finding will not carry forward.

**State of Hawaii
Department of Health
HIV Care Formula Grants
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007**

Finding No. 06-03: Reporting (Material Weakness)

During our prior year audit, we noted the following instances of noncompliance with reporting requirements for the program:

- *Final Progress Report.* The amount of outlays for AIDS/HIV drug assistance was incorrectly reported as \$2,170,460 compared to \$2,106,082 in actual expenditures.
- *Mid-Year Progress Report.* The amount of outlays for AIDS/HIV drug assistance was incorrectly reported as \$1,192,057 compared to \$757,910 in actual expenditures.

The reporting errors were caused by the program not having formalized processes in place to monitor invoices and actual expenditures. Reports appear to be prepared based on budgeted amounts and outdated reports resulting in inaccurate reports submitted to the federal government.

We recommended that program personnel develop and implement procedures to ensure that accurate and complete financial and performance reports are submitted to the awarding agency. Program personnel responsible for reporting should be provided with adequate training and supervision by management.

Status

Unresolved. Similar instances of this recurring finding were noted during our current year audit and are documented in Finding No. 07-03. Consequently, this finding will not carry forward.

**State of Hawaii
Department of Health
HIV Care Formula Grants
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007**

Finding No. 06-04: Earmarking (Reportable Condition)

During our prior year audit, we noted the following instances of noncompliance with earmarking requirements:

- The total amount expended for the Minority AIDS Initiative (“MAI”) during the grant period was \$12,734. The amount expended was \$276 less than required by terms of the applicable grant. The \$276 shortfall was caused by the STD/AIDS Prevention Branch not having appropriate procedures in place to monitor and comply with this earmarking requirement.
- The total amount expended for women, infants, children and youth during the grant period was \$236,946. The amount expended was \$94,409 less than required by terms of the applicable grant. The shortfall was due to the lack of formal procedures to monitor women, infant, children and youth expenditures.
- The total amount expended for ADAP during the grant period was \$2,106,082. The amount expended was \$54,960 less than required by terms of the applicable grant. We noted that the insufficient expenditure was due to the inability to substantiate the amount reported on the Final Progress Report.

We recommended that program personnel develop and implement procedures to monitor expenditures for specific purposes and ensure compliance with earmarking provisions. Program personnel responsible for monitoring compliance with earmarking provisions should receive adequate training and be supervised by management.

Status

Unresolved. Similar instances were noted during our current year audit and are documented in Finding No. 07-05. Consequently, this finding will not carry forward.

**State of Hawaii
Department of Health
Substance Abuse Prevention and Treatment Block Grant
Special Supplemental Nutrition Program for Women, Infants, and Children
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007**

Finding No. 06-05: Equipment Management

During our prior year testing of internal controls over equipment management for the programs listed above, we noted that the programs did not update the FAIS records to ensure additions, transfers, and disposals were properly reflected in a timely manner. This is a violation of the State's equipment management policies and procedures established in the State Inventory Manual.

The lack of enforcement by management to comply with the State's equipment management policies and procedures resulted in the noncompliance noted above.

We recommended that management of the Department ensure that all divisions and programs adhere to the State's established policies and procedures over equipment management in order to comply with federal and State regulations.

Status

Unresolved. Similar instances were noted during our current year audit, for other divisions and programs, which are reported in current year Finding Nos. 07-02 and 07-10. Consequently, this finding will not carry forward.

**State of Hawaii
Department of Health
HIV Care Formula Grant
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007**

Finding No. 06-06: Subrecipient Monitoring

During our prior year testing of the Subrecipient Monitoring compliance requirement for the HIV Care Formula Grants, we noted the following instances of noncompliance:

- AIDS Community Care Team (“ACCT”), a subrecipient, has not had an A-133 Single Audit performed since the fiscal year ended June 30, 2002.
- A subrecipient of ACCT was not informed of their noncompliance with program requirements during the subrecipient monitoring process. One of the ways that ACCT ensures compliance with federal regulations is by reviewing the certification forms. In this instance, ACCT documented in its review form that a certification form was missing. However, ACCT failed to notify the subrecipient of this issue and that the subrecipient should take appropriate and timely corrective action.

We recommended that the Department ensure that the audit requirements are met for the subrecipient, and that the Department, as the pass-through entity, communicates all errors encountered in a review to the subrecipient. Another member of the pass-through entity should review the results of the monitoring examination and ensure that all findings encountered in examinations are communicated to subrecipients.

Status

Unresolved. We noted a similar instance of noncompliance with the subrecipient monitoring requirements during our current year audit that is documented in Finding No. 07-09. Consequently, this finding will not carry forward.

**State of Hawaii
Department of Health
Centers for Disease Control and Prevention –
National Cancer Prevention and Control Branch
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007**

Finding No. 06-07: Eligibility

The NCPC program allows women to self-certify as to their eligibility for the program on the "Statement of Eligibility to Participate." The certification is often the program's only evidence of participants' eligibility to receive benefits from this grant and is acceptable evidence, per discussion with DHHS program personnel. Patient data is compiled and tracked in the CAST data collection system and submitted to the Centers for Disease Control ("CDC") for compliance monitoring purposes. During our prior year testing for compliance with eligibility requirements, we noted the following matters:

- For 1 of the 55 patients selected for testing, the program could not provide the "Statement of Eligibility to Participate" to evidence the eligibility of the individuals. As the program allows the women to self-certify to their eligibility to receive benefits on this form, it is the sole evidence used to verify the eligibility of the women. As we were unable to review the certification, we were unable to obtain evidence to support the eligibility of this individual;
- For 1 out of 55 patient files tested, the "Statement of Eligibility to Participate" did not include the patient's date of birth;
- For 2 out of 55 patient files tested, the "Statement of Eligibility to Participate" was not signed by the patient; and
- For 2 out of 55 patient files tested, the "Statement of Eligibility to Participate" was not signed by a witness.

The matters described above were the result of a lack of thorough review of completed statements by program personnel and service providers.

Failure to ensure that patients meet federal eligibility requirements could result in the rendering of services to an excessive number of patients and inaccurate statistical data being reported in the CAST system.

We recommended that the NCPC Branch ensure that service providers obtain complete and accurate Statements of Eligibility to Participate forms from patients. Program personnel should also independently review the certifications for timely completion and compliance with eligibility requirements.

Status

Unresolved. We noted similar instances of noncompliance with the eligibility requirements during our current year audit that are documented in Finding No. 07-11. Consequently, this finding will not carry forward.

**State of Hawaii
Department of Health
Financial Statement Finding
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007**

Finding No. 06-08: Cash Management

During our prior year review of the Department's cash management procedures, we noted that we could not verify whether DAGS disbursed funds from federal sources within three business days after the Department drew down the funds which is in accordance with the Cash Management Improvement Act Regulations & Guidance 31 CFR 205 (Final Rule). We also noted that the Department was not calculating or remitting any interest earnings attributable to these untimely disbursements. The delays were caused by the State's payment process that requires payments by all State departments to be processed through DAGS resulting in processing delays.

Noncompliance with federal regulations could result in a loss of funding that may jeopardize the operations of the Department's federally funded programs.

We recommended that the Department work with DAGS to ensure timely disbursement of federal funds. In addition, we recommend that the Department calculate and remit any interest liability to the federal government, if necessary, in accordance with federal regulations.

Status

Unresolved. In our current year testing, we noted that the State, through the Department of Budget and Finance, has entered into a Treasury-State Agreement ("TSA") with the federal government. The TSA lists the specific federal programs for which the State is required to calculate and remit excess interest earned on the draw down of federal funds. WIC and the CDC program are the Department's only federally funded programs that are included in the TSA. Consequently, those are the Department's only federally funded programs that are required to calculate and remit interest back to the federal government. However, neither the WIC nor CDC programs are calculating interest on the funds drawn down in advance.

In addition, all of the Department's federally funded programs are required to comply with the Cash Management Improvement Act's requirement to minimize the time between the transfer of funds from the U.S. Treasury and disbursement by the recipient.

State of Hawaii
Department of Health
Substance Abuse Prevention and Treatment Block Grant
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007

Finding No. 05-09: Allowable Costs – Purchase Requisition Approvals

During our prior year testing of purchasing controls for the SAPT program, we noted that approval of purchase requisitions by supervisors was inconsistently evidenced for the Alcohol and Drug Abuse Division (“ADAD”). The inconsistent approval was due to the lack of a formal requirement to evidence approval of purchase requisitions.

We recommended that the program (and Department) implement a formal requirement for supervisors to evidence their approval of all purchase requisitions to ensure compliance with OMB Circular A-87 and internally documented fiscal procedures.

Status

Unresolved. We understand that the program established a formal process for purchase orders in March 2007. However, as the updated procedures were only in place during the last three months of the fiscal year, a formal process was not in place throughout the majority of the year, allowing the inconsistent approvals previously noted.

**State of Hawaii
Department of Health
HIV Care Formula Grants
Status of Prior Year Findings and Questioned Costs
Year Ended June 30, 2006**

Finding No. 05-14: Earmarking – Quality Management Program

During our prior year testing of the HIV Care Formula Grants program, we noted that the program did not have a formalized quality management program in place to monitor whether program activities were consistent with the most recent Public Health Service (“PHS”) guidelines, as required under the grant agreement. However, we did note that program personnel were performing quality management activities on an informal basis. We were informed that the Department’s Quality Assurance and Evaluation Committee has developed a draft Quality Assurance Plan, which documents the standards for case management service delivery and monitoring of service delivery. The plan was expected to be finalized and implemented in late 2006.

We recommended that the Department finalize and implement its Quality Assurance Plan to ensure compliance with PHS guidelines and enable the Department to effectively monitor its HIV Care programs.

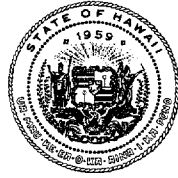
Status

Resolution ongoing. Due to staffing constraints, the program was unable to fully implement their Quality Assurance Plan. However, the program did establish the case manager position and certification of subrecipients. Case managers ensure that services are delivered in conformity with required eligibility guidelines. Case manager certifications are reviewed by the program. Program personnel will send back certifications prepared by the case managers.

We understand that program personnel are also attending training by the Institute of Quality Management of Training. HRSA provides this training specifically for quality management activities. Based on the training sessions attended, the program’s management will add two additional indicators: viral load and CD4. The measurement of these indicators will mean that the program will be better able to determine when individuals should receive drugs and how individuals are responding to drugs. The program aims to train Case Managers to make these measurements and input them into REGGIE, the program’s performance reporting system.

Corrective Action Plan

LINDA LINGLE
GOVERNOR OF HAWAII



CHIYOME LEINAALA FUKINO, M.D.
DIRECTOR OF HEALTH

STATE OF HAWAII
DEPARTMENT OF HEALTH

P.O. BOX 3378
HONOLULU, HAWAII 96801-3378

In reply, please refer to:
File:
ASO-F-4818

March 27, 2008

Office of the Auditor
465 South King Street, Suite 500
Honolulu, HI 96813

Dear State Auditor:

Attached are the Department of Health's Corrective Action Plan for the findings on the audit report for fiscal year 2007 and comments regarding prior year findings.

We appreciate the opportunity to comment on the audit report.

Sincerely,

Chiyome Leinaala Fukino, M.D.
Director of Health

Attachment

II. Financial Statement Findings

Finding No. 07-01 and 06-01 Restatement of Beginning Fund Balance/Net Assets (Material Weakness)

Finding and Cause and Effect

During our current year financial statement audit of the State of Hawaii, Department of Health (the "Department"), we identified an accounting error in the Department's basic financial statements as of and for the year ended June 30, 2006 due to the lack of oversight by fiscal management over the calculation of year end balances. Accordingly, the Department restated its opening net assets attributable to governmental activities and governmental funds fund balances as of July 1, 2006 to correct these errors which relate to the accounting for appropriations and amounts due from the Department of Human Services ("DHS").

Corrective Action Plan

The Department has already restated the beginning balances in the financial statements for the year ended June 30, 2007 to correct the error identified. The departmental fiscal officer will assist the programs in accruing the reimbursements due from DHS. The fiscal officer will also review the MBP 430B when received to ensure the proper appropriations are included on the Financial Management Information System ("FAMIS") reports.

Person Responsible

ASO Fiscal Officer

Anticipated Date of Completion

June 30, 2008

Finding No. 07-02 and 04-01 Capital Assets (Material Weakness)

Finding and Cause and Effect

In prior year audits (starting with the fiscal year 2004 audit), it was noted that the Department did not properly report capital purchases in accordance with the State's policies and procedures. It was recommended that the Department report capital asset additions to the State Procurement Office ("SPO") in a timely manner in accordance with the DAGS – SPO – Inventory Management Branch Training Manual ("State Inventory Manual"). It was also recommended that the Department implement a procedure for property custodians to reconcile quarterly equipment acquisitions in FAMIS to the DAGS computerized inventory reports ("MDB reports") from the State's Fixed Asset Inventory System ("FAIS") in a timely manner.

During our current year audit, we noted that the Department implemented procedures to assist the individual programs in recording capital purchases to FAIS in a timely manner by sending each program a

detailed listing of all fixed assets purchases recorded to FAMIS on a quarterly basis. The programs are responsible for reconciling this listing to the FAIS inventory reports. However, we noted instances where the reconciliation was not performed and discrepancies were not resolved. Therefore, we continued to note instances where capital assets were purchased, but not reported in FAIS, resulting in an audit adjustment.

Corrective Action Plan

The Department will continue to provide a quarterly list of fixed asset expenditures made as well as a list of the fixed assets recorded to FAIS. The programs will need to reconcile the two listing and respond to ASO-Fiscal as to the status of recording the fixed asset to the FAIS system. We will be in accordance with the DAGS-SPO-Inventory Management Branch Training Manual.

Person Responsible

Procurement and Supply Specialist and the Program Public Health Administration Officer

Anticipated Date of Completion

We have already started resolving the issue and expect that it will be fully implemented by June 30, 2008.

Section III. Federal Award Findings and Questioned Costs

Finding No. 07-03 and 06-03 Reporting (Material weakness)

Finding and Cause and Effect

During our current year audit, we noted the following instances of noncompliance with federal reporting requirements for the HIV Care program:

- Maintenance of Effort Report: The amount of State expenditures for FY 2005 was incorrectly reported as \$4,990,742 compared to \$4,378,512 in actual expenditures.
- Maintenance of Effort Report: The amount of State expenditures for FY 2006 was incorrectly reported as \$4,990,742 compared to \$4,494,978 in actual expenditures.

The reporting errors for the Maintenance of Effort Report were partially caused by the erroneous inclusion of encumbrances. State effort should be measured solely by expenditures made in the fiscal year. Also, it is improper to limit the amount of expenditures reported in the current year to the amount reported in the prior year. Total expenditures for all years must be accurately reported. Reporting errors are also caused by the program not having formalized processes in place to monitor invoices and actual expenditures. Reports were prepared based on budgeted amounts and outdated reports resulting in inaccurate reports submitted to the Federal government.

- Third Quarter AIDS Drug Assistance Program (“ADAP”) Quarterly Report: The amount of State contribution was incorrectly reported as \$126,845 compared to \$116,845 in actual expenditures.

- The Annual Financial Status Reports, Standard Form (“SF”)-269a was submitted approximately two months after the due date.
- The Final Annual Progress Report was submitted approximately one month after the due date.
- The Mid-year Progress Report was submitted twenty days after the due date.
- The second quarter ADAP Quarterly Report was submitted twenty-three days after the due date.
- The PSC 272 Federal Cash Transaction Report was submitted approximately one month after the due date.
- The Report on Women, Infants, Children and Youth (“WICY”) was submitted 3 days after the due date.
- The Final Report on the Use of Minority AIDS Initiative (“MAI”) funds was submitted three days after the due date.
- Per the subrecipient’s, AIDS Community Care Team (“ACCT”), audit report for the year ended June 30, 2006, which was received by the HIV Care program in October 2007, we noted that the ACCT had not submitted any reports to the Department regarding the monitoring of ACCT’s subrecipients or the results thereof.

We also noted the following instances of noncompliance during our testing of the Centers for Disease Control and Prevention Investigations and Technical Assistance program – National Cancer Prevention and Control Branch (“NCPC”):

- As of January 14, 2008, we noted that the Administrative Services Office (“ASO”) had not submitted the SF-269 report for the period June 30, 2006 to June 29, 2007, due on September 29, 2007. Due to a staffing shortage and other personnel changes, the Department’s ASO, which prepares the reports, failed to prepare the report.
- The Interim Annual Progress Report due on January 30, 2007 was submitted approximately 15 days after the due date.
- The two quarterly PSC 272 Federal Cash Transaction Reports tested were submitted approximately 10 days after the due date.
- In our testing of the timeliness of the SF-269 reports, we noted that the interim report, dated February 2007, was not submitted until the end of May 2007, which is two days over the allotted time for submission of the report. We also noted that prior year’s final report was not submitted until the end of November 2006, which is one day after the allotted submission deadline.

We also noted the following matter during our testing of the State Survey and Certification of Health Care Providers and Suppliers program:

- For 2 out of 2 Quarterly CMS-64 reports submitted, we were unable to find adequate documentation for the amounts reported.

The lack of documentation was due to a change in personnel that resulted in a loss of the supporting documentation.

We also noted the following instances of noncompliance during our testing of the Clean Water State Revolving Fund and Drinking Water State Revolving Fund programs:

- As of September 30, 2007, we noted that the ASO had not submitted the SF-272 report for the period July 1, 2006 to December 31, 2006, due on January 15, 2007. Due to a staffing shortage and other personnel changes, the Department's ASO failed to prepare the report.

The untimely reporting was due to the lack of a formal procedure to monitor report submissions.

As the programs are not in compliance with grant award and federal requirements, there is a risk the Federal government will withhold future funds from the respective programs.

Corrective Action Plan

- In the Maintenance of Effort Report, the STD/AIDS Prevention Branch (SAPB) includes both actual expenditures as well as obligated amounts as part of the expenditures in the preceding year.

Because invoices may be submitted up to twelve months after the grant expiration date, reporting only actual expenditures accrued up to the grant expiration date may result in a significant amount of expenditures not being included in the report to the awarding agency. This would result in an incomplete picture of HIV-related activities in Hawaii. Therefore, the SAPB reports both actual and obligated expenditures (in the form of encumbered amounts) to the awarding agency. Both are clearly labeled in the Maintenance of Effort Worksheet. Program personnel shall develop and implement procedures to ensure accurate and complete financial and performance reports are submitted to the awarding agency.

- Ryan White legislation specifically requires that:
The State will maintain HIV-related activities at a level that is equal to not less than the level of such expenditures by the State for the one-year period preceding the fiscal year for which the State is applying to receive a grant under Part B.

The figures included in the Maintenance of Effort Report show that Hawaii is expending funds at a level that is equal to the prior year.

Program personnel shall develop and implement procedures to ensure accurate and complete financial and performance reports are submitted on schedule to the awarding agency.

- All expenditure reports are now based on information taken from DATAMART reports for the required reporting period.

The Department is in the process of finalizing a spreadsheet with a listing of all Federal grants, grant award numbers and various reporting due dates to ensure compliance with federal requirements. This spreadsheet will be available to all the programs to allow the programs to keep track of what reports (SF

269 and PSC 272) have been and have not been submitted. The Department will have selected programs review the FSR's prior to final review by ASO-Fiscal to ensure accurate reporting.

Person Responsible for Corrective Action

ASO Accountant V and Program Planner (STD/AIDS)

Anticipated Date of Completion

We have already started resolving the issue and expect that it will be fully implemented by June 30, 2008.

Finding No. 07-04 and 06-02 Eligibility (Material Weakness)

Finding and Cause and Effect

During our current year audit, we tested 40 ADAP patient records and 9 H-COBRA patient records. Due to the Department maintaining insufficient supporting documents, we noted the following instances of noncompliance with eligibility requirements for the HIV Care program:

- For 11 out of 40 patient records tested, the program was unable to provide documentation to evidence the eligibility (estimated value of liquid assets) of the ADAP participants.
- For 9 out of 9 patient records tested, the program was unable to provide adequate documentation to evidence the eligibility (estimated value of liquid assets) of H-COBRA participants.
- For 20 out of 40 ADAP patient records tested, the program was unable to provide documentation to evidence that 6-month recertifications were performed.
- For 4 out of 40 patient records tested, the program was unable to provide documentation to evidence the eligibility (State of Hawaii residency requirement and gross income requirement) of the ADAP participants.

We noted that the program has taken steps to remediate this recurring finding from prior years (Finding No. 06-02 and No. 05-02). However, as the program is still in the process of implementing our recommendations, the program did not meet the Eligibility requirements in fiscal 2007.

Corrective Action Plan

Beginning May 2006, the SAPB changed the way in which eligibility and recertification are performed in order to improve compliance with Federal DHHS requirements. The new eligibility and recertification processes have improved compliance as compared to previous related audit findings (Finding No. 06-02 and Finding No. 05-02).

The program has taken the following steps to assure future compliance:

- 1) The staff position responsible for the supervision of ADAP and H-COBRA was filled in August 2007. Since the 2005 audit year, through the end of the 2007 audit year, the supervisor position was vacant.

- 2) SAPB has requested a structural reorganization to locate one additional staff position within the organizational unit responsible for ADAP and H-COBRA. This position will assist in documenting eligibility.
- 3) Criteria to determine liquid assets for program eligibility criteria were revised.
- 4) Timely 6-month recertification: The program database was revised to alert staff when a patient is overdue for recertification. Program brochures were updated in March 2006 to include the recertification requirement, and again in February 2008 to emphasize recertification as a requirement. All client files have been reviewed and the program documents which files are missing required documentation. Recertification status reports have been prepared every two months since July 2007. The contracted case management agencies are provided with lists of program clients and their recertification due date. Case managers are contacted when a patient is overdue for recertification to ensure that the case manager is making attempts to contact the patient. Case managers notify the program whenever they are unable to contact a patient. The program has solicited the assistance of the contract pharmacy and physicians offices to notify patients who are overdue for certification that they must contact the case manager.
- 5) In February, 2008, a personalized letter and written material regarding the recertification requirement was prepared for each patient enrolled prior to May 2006 who had still not completed six month recertification (and who was therefore not previously linked to the new eligibility and recertification processes). These letters were distributed to patients by the contract pharmacy along with the patient's medications.

Person Responsible for Corrective Action

Supervisor HIV Medical Management Services

Anticipated Date of Completion

August 2008

Finding No. 07-05 and 06-04 Earmarking (Material Weakness)

Finding and Cause and Effect

During our current year audit of the HIV Care program, we noted the following instances of noncompliance with earmarking requirements for amounts expended on women, infants, children and youth during the grant period. The amount expended was \$261,645, which was \$140,659 less than required by terms of the applicable grant. The shortfall was due primarily to the fact that the need for services for women, infants and children is less than the amount of funds available.

Corrective Action Plan

Levels of expenditures reported in the Women, Infants, Children, and Youth reports are based on actual expenditures. Actual expenditures reflect services provided in response to actual need. As the payor of last resort, Ryan White funds are accessed only after all other sources of funds have been exhausted, which results in requests for services at levels lower than the levels of resources that have been required to be set aside.

Program personnel will continue to ensure that providers are aware of the funding available for women, infants, children and youth. The Program will monitor expenditures for these specific purposes.

Person Responsible for Corrective Action

SAPB Planner

Anticipated Date of Completion

July 1, 2008

Finding No. 07-06 Procurement (Material Weakness)

Finding and Cause and Effect

During our testing of procurement and suspension and debarment requirements for the HIV Care program, we noted two instances of noncompliance with federal requirements:

- While procurement personnel ensure that the awardees are not suspended or debarred by the State, there were no procedures in place to ensure that the program does not execute contracts with federally suspended or debarred parties.
- Per the AIDS Community Care Team (“ACCT”) Circular A-133 audit reports for the years ended June 30, 2006 and June 30, 2007, which were received by the HIV Care program in October and November 2007, respectively, we noted that the ACCT does not have a written policy or procedures for the procurement of supplies, and other expendable property, equipment, real property and other non-contractual services with Federal funds to ensure that such materials and services are obtained in an effective manner and in compliance with the provisions of applicable Federal statutes. It was also noted that the ACCT did not document any procedures for procurement transactions. Without supporting documentation of procurement procedures, the ACCT risks non-compliance with Federal Guidelines.

The Department’s HIV/STD Prevention Branch has not yet issued a management decision as ACCT’s audit reports were received in October and November 2007.

During our testing of the WIC grants, we noted one instance of noncompliance with federal requirements:

- For contracts executed by the program, contract personnel have policies and procedures in place to ensure that the program does not execute contracts with parties that are debarred, suspended, proposed for debarment, declared ineligible, or voluntarily excluded from covered transaction by a Federal department or agency in accordance with 45 CFR Part 76. However, for contracts executed by the SPO on behalf of the program, procurement personnel have procedures to ensure that the awardees are not suspended or debarred by the State, but there are no procedures in place to ensure that the program does not execute contracts with federally suspended or debarred parties.

Although we noted that the awardees of the HIV Care program and WIC program contracts tested were not on the federal suspension or debarment listing, without proper controls in place, there is a risk that the program will enter into a procurement contract with a suspended or debarred party.

Corrective Action Plan

SAPB sent a letter to ACCT, dated March 11, 2008, requesting in writing by May 1, 2008, resolution to the issues raised in the ACCT audit and subsequently in the Departmental audit.

On March 17, 2008, a meeting was held with the SAPB Branch Chief, Planner, and Executive Director of ACCT to stress the importance of resolving ACCT's audit issues and to identify any barriers to resolution. ACCT's Executive Director stated that ACCT has made most of the needed changes and does not anticipate major difficulties completing those remaining. On March 18, 2008, SAPB received a fax from ACCT stating that ACCT is already working with its auditor to address the issues and that a written response on each finding would be provided to SAPB by May 1, 2008. A monthly monitoring visit to ACCT will be made by the Planner to ensure all findings are resolved.

The WIC program has established a procedure to ensure that, for contracts executed by SPO, the awardees are not suspended or debarred by the State. Prior to the Notice of Award, the WIC program used the Excluded Parties List System (EPLS) website maintained by the GSA to search if the name of the offeror is listed. Documentation to evidence this review will be in the form of a printout of the search results which will be incorporated in the procurement file. Federal Certifications will be provided to the State Procurement Office (SPO) for them to include in the contract.

Person Responsible for Corrective Action

Planner (HIV Care Formula Grants)

Contract Unit PHAO III (WIC)

Anticipated Date of Completion

August 2008

Finding No. 07-07 Allowable Costs

Finding and Cause and Effect

The ACCT A-133 audit reports for the years ended June 30, 2006 and June 30, 2007 were prepared by another auditor and received by the HIV Care program in October and November 2007, respectively. While reviewing the reports, we noted several instances of noncompliance with allowable cost requirements:

- The reports stated that ACCT management's allocation of salary taxes and benefits did not match actual time spent by employees. However, no questioned costs were reported.
- ACCT charged to the program approximately \$4,000 in allowable costs related to penalties and interest to the program in fiscal years 2006 and 2007. Approximately \$2,000 was charged to Contracts # 03-218 and #06-162 in fiscal year 2006 and approximately \$2,000 in penalties and interest expense to Contract #06-162.
- ACCT program was reimbursed for approximately \$4,000 in unallowable costs for lease payments which were paid to a related entity. To record lease payments, the ACCT wrote a check for the lease

payments out of one account and deposited the payment into another ACCT account which the ACCT utilizes for the related entity.

We note that the HIV/STD Prevention Branch has not yet issued a management decision as the A-133 audit reports were received in October and November 2007.

We noted that the subrecipient's noncompliance affects this program's ability to comply with Allowable Costs/Cost Principle requirements as stated in the OMB Circular A-133.

Corrective Action Plan

SAPB sent a letter to ACCT, dated March 11, 2008, requesting in writing by May 1, 2008, resolution to the issues raised in the ACCT audit and subsequently in the Departmental audit.

On March 17, 2008, a meeting was held with the SAPB Branch Chief, Planner, and Executive Director of ACCT to stress the importance of resolving ACCT's audit issues and to identify any barriers to resolution. ACCT's Executive Director stated that ACCT has made most of the needed changes and does not anticipate major difficulties completing those remaining. On March 18, 2008, SAPB received a fax from ACCT stating that ACCT is already working with its auditor to address the issues and that a written response on each finding would be provided to SAPB by May 1, 2008. A monthly monitoring visit to ACCT will be made by the Planner to ensure all findings are resolved.

Person Responsible for Corrective Action

SAPB Planner

Anticipated Date of Completion

August 2008

Finding No. 07-08 Equipment Management

Finding and Cause and Effect

Per ACCT's Circular A-133 audit report for the year ended June 30, 2006, which was prepared by another auditor and received by the HIV Care program in October 2007, we noted that ACCT does not maintain a perpetual detailed record of equipment, nor inventory equipment at least once every two years.

ACCT risks the improper reporting, disposal, and ultimate remittance of equipment purchased with Federal Awards and affects the program's ability to comply with Equipment Management requirements as stated in OMB Circular A-133.

We note that the HIV/STD Prevention Branch has not issued a management decision as the ACCT audit report was received in October 2007.

We noted that the subrecipient's noncompliance affects this program's ability to comply with Equipment Management requirements as stated in OMB Circular A-133.

Corrective Action Plan

SAPB sent a letter to ACCT, dated March 11, 2008, requesting in writing by May 1, 2008, resolution to the issues raised in the ACCT audit and subsequently in the Departmental audit.

On March 17, 2008, a meeting was held with the SAPB Branch Chief, Planner, and Executive Director of ACCT to stress the importance of resolving ACCT's audit issues and to identify any barriers to resolution. ACCT's Executive Director stated that ACCT has made most of the needed changes and does not anticipate major difficulties completing those remaining. On March 18, 2008, SAPB received a fax from ACCT stating that ACCT is already working with its auditor to address the issues and that a written response on each finding would be provided to SAPB by May 1, 2008. A monthly monitoring visit to ACCT will be made by the Planner to ensure all findings are resolved.

Person Responsible for Corrective Action

Planner

Anticipated Date of Completion

August 2008

Finding No. 07-09 and 06-06

Subrecipient Monitoring

Finding and Cause and Effect

During our testing of subrecipient monitoring, we noted the subrecipient did not submit its OMB Circular A-133 audit report for fiscal year 2006 in a timely basis. We note the HIV Care program failed to communicate a need for the timely submittal of the A-133 report. This failure to communicate Federal guidelines indicates a deficiency of the HIV Care program's subrecipient monitoring process.

Corrective Action Plan

SAPB sent a letter to ACCT, dated March 11, 2008, requesting in writing by May 1, 2008, resolution to the issues raised in the ACCT audit and subsequently in the Departmental audit.

On March 17, 2008, a meeting was held with the SAPB Branch Chief, Planner, and Executive Director of ACCT to stress the importance of resolving ACCT's audit issues and to identify any barriers to resolution. ACCT's Executive Director stated that ACCT has made most of the needed changes and does not anticipate major difficulties completing those remaining. On March 18, 2008, SAPB received a fax from ACCT stating that ACCT is already working with its auditor to address the issues and that a written response on each finding would be provided to SAPB by May 1, 2008. A monthly monitoring visit to ACCT will be made by the Planner to ensure all findings are resolved

Person Responsible for Corrective Action

SAPB Planner

Anticipated Date of Completion

August 2008

Finding No. 07-10 and 06-05**Equipment Management****Finding and Cause and Effect**

During our testing of compliance over equipment management for the programs listed above, we noted that the NCPC program did not update the FAIS records to ensure additions, transfers, and disposals were properly reflected in a timely manner. This is a violation of the State's equipment management policies and procedures established in the State Inventory Manual.

The lack of enforcement by management to comply with the State's equipment management policies and procedures resulted in the noncompliance noted above.

Corrective Action Plan

The Breast & Cervical Cancer Control Program, Public Health Administrative Officer (PHAO) will send documentation (copies of purchase orders and invoices, etc.) of changes to the equipment inventory (additions, transfers and disposals) to the Chronic Disease Management and Control Branch (CDMCB) Secretary, who is the inventory custodian for the branch. Additionally, by the last day of each quarter, the PHAO will summarize the quarter's equipment inventory transactions and will send this to the CDMCB Secretary. The requirement to update the FAIS system by the 15th of the following month will be noted on the quarterly update. The Branch Secretary will work with the property custodian to record the changes by the 15th of the month following the end of the quarter.

Person Responsible for Corrective Action

Public Health Administrative Officer III

Anticipated Date of Completion

Completed, March 2008

Finding 07-11 and 06-07**Eligibility****Finding and Cause and Effect**

The program allows women to self-certify as to their eligibility for the program on the "Statement of Eligibility to Participate." The certification is often the program's only evidence of participants' eligibility to receive benefits from this grant and is acceptable evidence, per discussion with DHHS program personnel. Patient data is compiled and tracked in the CAST data collection system and submitted to the Centers for Disease Control ("CDC") for compliance monitoring purposes. During our testing for compliance with eligibility requirements, we noted the following matters:

- For 1 out of 40 patient files tested, the "Statement of Eligibility to Participate" did not include the patient's date of birth;
- For 1 out of 40 patient files tested, the "Statement of Eligibility to Participate" did not include the patient's average monthly income; and

- For 1 out of 40 patient files tested, the incorrect birth dates for the patients were documented in the “Statement of Eligibility to Participate”.

The matters described above were the result of a lack of thorough review of completed statements by program personnel and service providers.

Failure to ensure that patients meet federal eligibility requirements could result in the rendering of services to an excessive number of patients and inaccurate statistical data being reported in the CAST system.

Corrective Action Plan

The “Statement of Eligibility to Participate” forms are sent to the Data Processor either by fax or through the mail by the hospitals or clinics. The Data Processor reviews them for accuracy and completeness. “Statements” will be double checked by the program’s Registered Nurse and/or Public Health Administrative Officer to verify accuracy and completeness. It is then sent back to the Data Processor with any changes.

Person Responsible for Corrective Action

PHAO III

Anticipated Date of Completion

Completed, March 2008

Finding No. 06-08: Cash Management

During our prior year review of the Department’s cash management procedures, we noted that we could not verify whether DAGS disbursed funds from federal sources within three business days after the Department drew down the funds which is in accordance with the Cash Management Improvement Act Regulations & Guidance 31 CFR 205 (Final Rule). We also noted that the Department was not calculating or remitting any interest earnings attributable to these untimely disbursements. The delays were caused by the State’s payment process that requires payments by all State departments to be processed through DAGS resulting in processing delays.

Noncompliance with federal regulations could result in a loss of funding that may jeopardize the operations of the Department’s federally funded programs.

We recommended that the Department work with DAGS to ensure timely disbursement of federal funds. In addition, we recommend that the Department calculate and remit any interest liability to the federal government, if necessary, in accordance with federal regulations.

Corrective Action Plan

The Department is continuously working with the Department of Accounting and General Services (DAGS) and the state Department of Budget and Finance (B&F) to establish a faster process of depositing and disbursing federal money to ensure compliance with Federal Regulations as well as meet the state

department's treasury deposit and fiscal accounting responsibilities. The Department has internally made changes to the procedures to ensure the paperwork required to record the deposit and make the payments are processed as soon as possible. Without changes to the B&F and DAGS processes, the Department cannot ensure compliance to the Federal Regulations.

Person Responsible for Corrective Action

Administrative Services Officer and Fiscal Officer

Anticipated Date of Completion

September 2008

Finding No. 05-09: Allowable Costs – Purchase Requisition Approvals

During our prior year testing of purchasing controls for the SAPT program, we noted that approval of purchase requisitions by supervisors was inconsistently evidenced for the Alcohol and Drug Abuse Division ("ADAD"). The inconsistent approval was due to the lack of a formal requirement to evidence approval of purchase requisitions.

We recommended that the program (and Department) implement a formal requirement for supervisors to evidence their approval of all purchase requisitions to ensure compliance with OMB Circular A-87 and internally documented fiscal procedures.

Corrective Action Plan

The Alcohol and Drug Abuse Division (ADAD) has updated their procedures to ensure proper authorization of purchase requisitions.

Person Responsible for Corrective Action

ADAD Public Health Administrative Officer V

Anticipated Date of Completion

Completed, March 2007

Finding No. 05-14: Earmarking – Quality Management Program

During our prior year testing of the HIV Care Formula Grants program, we noted that the program did not have a formalized quality management program in place to monitor whether program activities were consistent with the most recent Public Health Service ("PHS") guidelines, as required under the grant agreement. However, we did note that program personnel were performing quality management activities on an informal basis. We were informed that the Department's Quality Assurance and Evaluation Committee has developed a draft Quality Assurance Plan, which documents the standards for case management service delivery and monitoring of service delivery. The plan was expected to be finalized and implemented in late 2006.

We recommended that the Department finalize and implement its Quality Assurance Plan to ensure compliance with PHS guidelines and enable the Department to effectively monitor its HIV Care programs.

Corrective Action Plan

The program has taken the following steps to assure future compliance:

- 1) Two SAPB staff members coordinate development of a quality management program. They participate in the Low-Incidence States Quality Management Initiative. In April 2007, two staff members participated in the HIV/AIDS Bureau/National Quality Center Low Incidence Initiative Quality Management Meeting in Washington, D.C. In 2007, a staff member attended a training of trainers meeting in Chicago. Grantee staff continues to participate in the National Quality Center national Low Incidence Initiative technical assistance conference calls. Staff continues to participate in and submit National Quality Center bi-monthly quality reports.
- 2) For the HIV/AIDS Bureau/National Quality Center bi-monthly reporting activity, grantee staff have selected, monitored and reported on five quality management performance indicators.
- 3) The Branch is in the final phases of completing a quality management plan. A quality management advisory committee has been identified to assist staff in developing clinical quality management performance standards and indicators, establishing realistic goals and objectives for the quality management program, and providing input from the service delivery perspective.
- 4) Regarding data collection, SAPB is currently restructuring the case management services to focus more on medical case management. Training in support of this new model has begun and specific plans for changing the data collection system have been made.

For the longer term, SAPB has requested to do a structural reorganization that would create an HIV Care Quality Management Program to fully conform to the HIV Care Formula Grant requirement related to quality management.

Person Responsible for Corrective Action

SAPB Branch Chief

Anticipated Date of Completion

The Quality Management Plan will be completed by April 2008.