AN OVERVIEW BY THE LEGISLATIVE AUDITOR OF THE FINANCIAL AUDIT OF THE HAWAII HOUSING AUTHORITY

INTRODUCTION

The financial audit of the Hawaii Housing Authority identifies serious shortcomings in the financial management, accounting and internal control systems of the authority. The consequence of these shortcomings is that in this audit, conducted jointly by the Legislative Auditor and the CPA firm of Coopers and Lybrand, we were not able to attest that the financial statements of the authority do, in fact, represent its actual financial position.

With respect to certain funds, the auditors rendered an adverse opinion that the financial statements of the authority did *not* fairly present the authority's financial position. With respect to other funds, because of various deficiencies and omissions in the accounts, the auditors filed a disclaimer of opinion that the statements could not be examined in accordance with accepted auditing standards. An adverse opinion with respect to some accounts and a disclaimer of opinion with respect to all other accounts are tantamount to a verdict of "no confidence" in the authority's financial practices and records.

In auditing, a disclaimer of opinion is rendered only under exceptional circumstances. The American Institute of Certified Public Accountants reports that in 1973, of audits conducted on 600 companies, there was not a single disclaimer of opinion. We emphasize that auditors treat as a most serious matter the rendering of a disclaimer of opinion. In the case of the Hawaii Housing Authority, the disclaimer underscores the overall finding that there are serious deficiencies in its financial management and practices.

SYNOPSIS OF MAJOR FINDINGS

Throughout the report, we identify numerous deficiencies, which, each in isolation, may not appear to be consequential but which, *in toto,* are indicative of a financial system in virtual disarray. We believe that the Hawaii Housing Authority, as the agency with the major responsibility for one of the most urgent programs in the State, has a special responsibility to set its financial house in order so that it can make the right kinds of decisions on behalf of the client group it serves. There is a close and inextricable relationship between financial practices and their effects on people served by the program, a fact which appears not to have been fully understood or appreciated by the authority. We point out two instances where the interests of the authority's clients were not served by its practices.

Interest earnings lost to housing programs. The Hawaii Housing Authority has full powers to invest funds which are temporarily in excess of its immediate needs. To the extent that the authority fails to capitalize on the opportunity to earn interest on its funds, that much less is available for housing programs. We found that as of June 30, 1973, the authority had only 3.5 percent of its funds in investments. A large amount, nearly $6 million, had been deposited with the State treasury without instructing the department of budget and finance to invest the funds to the credit of the housing authority. As a result, our estimate is that $355,000 in interest earnings was lost to housing programs. In its response to this finding, the authority states that it was unaware that it could exercise control over its special fund balances and that it understood that interest did accrue to the general fund. The latter, of course, is not the point. The authority has a responsibility to its clients to assure that there is maximum investment of all of its cash balances and a responsibility to assure that all interest earnings are properly credited to the funds established for housing programs.

Reporting expenditures when there were none. We found that for years, the authority had shown as an expenditure an amount which totaled over $150,000. There was no actual and valid expense to support that amount. In fact, the amount was simply an accumulated reserve amount which, carried as an expenditure, was a phantom expenditure. Presumably, however, in assessing the overall financial position of the authority and the amounts to be recovered through housing rentals, it would have had to be a consideration in the setting of rental rates. While the authority, from its response, does not apparently consider this to be a serious matter, we point out that this error, if it continues to be made, may have adverse economic effects on the authority's tenants, since this amount may be included as one of the expenses to be recovered through rental charges.

There are other practices which reflect on the authority's capacity to serve its clients and to manage its programs. Its methods for determining eligibility for public housing result in inconsistencies in the treatment of applicants, it takes an excessive amount of time to prepare vacated units for occupancy, its purchasing policies and procedures are weak, and it does not exercise sufficient property and inventory controls.

CONCLUSION

For the most part, the authority is in agreement with the audit findings and recommendations. The authority states that "most of the recommendations are good and we have or will correct the deficiencies . . ." We have no reason to doubt the sincerity of the authority, but we do believe that for the authority to establish a sound financial management system where none exists, it needs professional help. We recommend that the executive agencies charged with financial management responsibilities, such as the department of accounting and general services and the department of budget and finance, render assistance to the Hawaii Housing Authority, or alternatively, for the authority to secure the services of a firm with experience in establishing financial and internal control systems.

Clinton T. Tanimura
Legislative Auditor
State of Hawaii

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