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The program's continued reliance on self-reported amounts increases the risk of under-reporting by distributors and over-reporting by redemption centers.

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Financial and Program Audit of the Deposit Beverage Container Program, June 30, 2014

Report No. 15-02, April 2015

Deposit Beverage Container Program still relies on self-reported data, still at risk

Unaddressed program flaws result in millions of dollars in overpayments and undermine financial sustainability

This is our fifth audit of the Deposit Beverage Container (DBC) Program. As in our previous audits, we found that the program relies on self-reported data from distributors that may be fraudulently or erroneously under-reporting beverage containers sold or distributed, and certified redemption centers that may be fraudulently or erroneously over-reporting beverage containers redeemed. This systemic flaw, coupled with the absence of a detailed audit function, has exposed the program to abuse and risk of fraud since program inception.

From FY2013 through FY2014, the DBC Program paid \$2.6 million in deposit refunds for approximately 3.5 million pounds of recycled materials that cannot be accounted for. The Department of Health, which administers the program, has been aware of this flawed payment system since 2006 but has done little to address it, either with changes to the program or through enforcement of inspections. As a result, the program continues to be exposed to fraud, which may result in higher program costs and an unreliable reported redemption rate.

Program was unaware that distributor substantially underpaid the DBC Fund for more than six years

Distributors are required by law to report the number of deposit beverage containers sold/distributed and pay beverage container deposit and container fees to the program on a monthly basis. The program, however, continues to rely on unsupported amounts reported by distributors because it lacks a systematic verification or inspection process. We reviewed distributor receipts and found that one distributor—Whole Foods Market, Inc.—underpaid beverage container deposits and fees for more than six years, which went undetected by the program. For the six years it has been operating in Hawai'i, Whole Foods was paying the DBC fund 6¢ per case instead of 6¢ per container. Whole Foods reported that the underpayment is approximately \$34,000 for FY2012 through FY2014. The DBC Program has consulted with the Department of the Attorney General on whether the program will be able to collect the full amount of the six-year underpayment. The attorney general has advised that the program could collect the last two years, but likely not the prior four. These errors highlight the need for the program to closely monitor amounts reported and paid by distributors. Not doing so exposes the DBC Program to fraud.

Agency Response

The department concurred with many of our findings. However, it felt that two statements represented "incomplete findings," namely, that the program does not pay a shrinkage rate above 2.5 percent and the program reimburses no more than 5¢ per container, but redemption centers may choose to reimburse consumers more than that. The department also expressed concern with the layout of our report, claiming that certain formatting effects could be misleading and create confusion. Based on the department's comments, we made edits for clarity and style but we stand by our findings and conclusions. We did not change our report layout, which reflects our standard style.

Regarding our recommendation to adopt a back-end payment system to address risks associated with continued reliance on redemption centers' self-reported numbers, the department disagreed such a system will shift risk away from the State and asserted that it should no longer be considered a viable solution. The department did not, however, offer another solution to address the risk. We implore the department to develop an alternative plan to address systemic flaws in the deposit and redemption process as soon as possible. Until such a solution is implemented, the DBC Program will continue to be under significant risk of fraud and abuse.