
Financial Audit of the Department of Health

A Report to the
Governor
and the
Legislature of
the State of
Hawaii

Report No. 92-30
December 1992

THE AUDITOR
STATE OF HAWAII

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Conducted by

The Auditor
State of Hawaii
and
Nishihama & Kishida,
CPA's, Inc.

Submitted by

THE AUDITOR
STATE OF HAWAII

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Foreword

This is a report of the financial audit of the Department of Health for the fiscal year July 1, 1991 to June 30, 1992. The audit was conducted pursuant to Section 23-4, Hawaii Revised Statutes, which requires the State Auditor to conduct post audits of all departments, offices, and agencies of the State. The audit was conducted by the Office of the Auditor and the certified public accounting firm of Nishihama & Kishida, CPA's, Inc.

We wish to express our appreciation for the cooperation and assistance extended by officials and staff of the Department of Health.

Marion M. Higa
State Auditor

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Chapter 1

Introduction

This is a report of our financial audit of the State of Hawaii Department of Health. The audit was conducted by the Office of the Auditor and the certified public accounting firm of Nishihama & Kishida, CPA's, Inc.

The audit was conducted pursuant to Section 23-4, Hawaii Revised Statutes, which requires the State Auditor to conduct post audits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State and its political subdivisions.

Objectives of the Audit

1. Report on the fair presentation of the financial statements of the department.
2. Assess the adequacy, effectiveness, and efficiency of the systems and procedures for financial accounting, internal control, and financial reporting; and recommend improvements.
3. Ascertain whether expenditures and other disbursements have been made and whether all revenues and other receipts have been collected and accounted for in accordance with federal and state laws, rules and regulations, and policies and procedures.

Scope and Methodology

We audited the financial records and transactions and the related systems of accounting and internal controls of the department for the fiscal year July 1, 1991 to June 30, 1992. Included were all fund types and account groups, except the proprietary fund which was audited by other auditors whose reports were not available to us, and the general fixed assets account group. We also reviewed those transactions, systems, and procedures for compliance with applicable laws and regulations.

The audit examined the accounting, reporting, and internal control structure to identify deficiencies and weaknesses and to make appropriate recommendations for improvements. Included were the forms, records, and the accounting and operating procedures.

The accountants' opinion as to the fairness of the financial statements presented is that of Nishihama & Kishida, CPA's, Inc. The audit was

conducted from May 1992 through October 1992 in accordance with generally accepted government auditing standards.

Background

In the Hawaii State Government Reorganization Act of 1959 (Act 1, Second Special Session Laws of Hawaii 1959) the Legislature created the Department of Health. Section 26-13, Hawaii Revised Statutes, describes the department's responsibilities:

The department shall administer programs designed to protect, preserve, care for, and improve the physical and mental health of the people of the State. The programs shall include the administration and enforcement of matters and laws of public health of the State, including the program for the Waimano home and for the state hospital, but excluding assistance and care for the indigent and the medically indigent.

Organization of the Department

The department is headed by the director of health. The director has overall responsibility for planning, directing, and coordinating the various programs of the department. The department is organized into staff offices and administrative units.

Staff offices

Seven staff offices provide support services to the department.

- The Administrative Services Office provides general internal management and fiscal and budgetary assistance to the director.
- The Health Information System Office provides technical assistance and consultation on matters relating to public health applications of electronic data processing.
- The Personnel Office provides for general personnel management and administration including services to all levels of management in attaining program objectives.
- The Office of Affirmative Action administers and develops the nondiscrimination and affirmative action programs of the department.
- Three District Health Offices administer and coordinate public health services in each of the counties of Kauai, Maui and Hawaii.

Administrative units

Six administrative units carry out the programs of the department.

- The Environmental Health Administration administers statewide programs concerned with the abatement of various categories of pollution.
- The Behavioral Health Services Administration administers programs to promote, care for, and improve the mental health of the people of the State.
- The Community Hospitals Administration administers the community hospitals system and provides a broad range of general and specialized medical treatment, care, and services statewide on an inpatient and outpatient basis.
- The Personal Health Services Administration provides and coordinates community based services to improve the health of families, including mothers and children. It also provides prevention, treatment, and rehabilitation services to persons with disabilities and to those with developmental disabilities.
- The Health Promotion and Disease Prevention Administration develops and implements health education programs designed to promote, inform, and advise the community on health matters and problems. It also provides services for the prevention and control of chronic illnesses, communicable diseases, and dental diseases.
- The Health Resources Administration develops and implements a State Health Plan which focuses on public health programs and identifies specific objectives, policies, and actions for health and environmental health services.

Units assigned for administrative purposes

Five additional units are assigned to the department for administrative purposes.

- The Environmental Council administers the law on environmental impact statements.
- The Office of Environmental Quality Control coordinates efforts for monitoring the quality of the environment.
- The Commission on Persons with Disabilities serves as a clearinghouse and repository of public and private activities and information relating to persons with handicaps. It also

serves as a public advocate of such persons and advises the State and counties on matters affecting those with handicaps.

- The State Planning Council on Developmental Disabilities prepares the state plan for persons with developmental disabilities and coordinates the services and programs of the departments and private agencies. It also serves as the advocate for the needs of those with developmental disabilities.
- The State Health Planning and Development Agency conducts the health planning activities of the State, determines statewide health needs, and implements the State Health Plan.

Chapter 2

Internal Control Practices

Internal controls are steps instituted by management to assure that objectives are met and resources are safeguarded. This chapter presents general findings and recommendations on the financial accounting and internal control practices and procedures of the Department of Health.

Summary of Findings

We find that the department's contracting practices fail to assure that legislatively mandated services are provided to the public in a manner that safeguards the interests of the department, the service providers, and the recipients of services. We also find weaknesses in the department's financial management. More specifically, we find:

1. Contracts for purchase of services are not always executed before providers begin providing services.
2. Payment terms in certain contracts written by the Alcohol and Drug Abuse Division are unclear and contradictory.
3. The department does not have written contract monitoring procedures and the extent of contract monitoring is not always documented.
4. Controls over cash receipts are inadequate.
5. Moneys are improperly deposited into special revenue fund accounts instead of the general fund.
6. The Developmental Disabilities Division is not performing bank reconciliations for one of its checking accounts.
7. Fixed asset acquisitions are not always reported to DAGS as required.

Contracts Are Not Executed in a Timely Manner

The department is responsible for the timely completion and execution of contracts to provide legislatively mandated health services to the public.

We found that the department is chronically late in executing contracts with service providers. In the sample of contracts that we reviewed, 90 percent were executed *after* the services were expected to be provided to the public. Of those that were late, fully 20 percent were executed more than 90 days after services were to be provided.

The Legislature appropriates moneys to the department for health services to the public over a specified period of time, normally for the fiscal year beginning July 1. The various divisions of the department contract with private providers to deliver services to the public. These divisions have developed somewhat similar contracting procedures. We have created a flowchart with an accompanying narrative that generally represents the contracting steps followed by the individual divisions and have included it as an attachment to this report.

From our review of the contracts, we found that most private providers began to provide services before contracts were finalized because they expected the contracts would be forthcoming. This is not in the best interests of the State, the private providers, or even the public. Properly executed contracts are essential to ensure that (1) the type and scope of services to be provided have been agreed upon, (2) the services are those for which the Legislature appropriated moneys, and (3) the roles and responsibilities of the department and service providers are clearly delineated to avoid confusion or misunderstandings.

It is essential that contracts be properly executed before any services are provided. Without the benefit of a contract, there is no assurance that services being provided are those that are necessary or those intended by the Legislature. Additionally, providing services without contractually defined roles and responsibilities puts both the State and the providers in jeopardy should any legal problems arise.

Recommendation

We recommend that the department take steps necessary to ensure that contracts for services are properly executed before delivery of those services by contractors is scheduled.

Contract Payment Terms are Unclear

Contract terms were not always clear and the department did not always follow the contract requirements. Certain contracts written by the Alcohol and Drug Abuse Division stated that contractors would be paid based on services provided, with final payment contingent upon verification that services had been provided during the contract period. Other sections of these contracts required unexpended funds to be

returned to the department without specifying what constitutes unexpended funds.

We found that the division reviews the contractors' records and makes payment based on its determination of the *lesser of* either (a) the actual costs incurred by the contractor when providing services or (b) the contractually agreed upon amount for the services provided.

Payment terms in the above contracts did not clearly support the division's lesser-of-cost or agreed-upon-amount approach. Contracts for services included terms which referred to payment for services as well as cost reimbursement. There was absolutely no reference that payments would be based on the lesser of the two.

Contract payment terms should be clear and the department should follow the specified conditions.

Recommendation

We recommend that contracts executed by the Drug and Alcohol Abuse Division contain clear payment terms and that the department comply with the terms.

Contract Monitoring Procedures Need to be Standardized

The department has no contract monitoring guidelines for its divisions. Contract monitoring is the process by which the department assures itself that contract terms are being followed and services are being provided. Contract monitoring should be formally documented and kept with other contract documents.

Without departmental direction on contract monitoring, divisions and branches have developed their own contract monitoring practices, which predictably differ. It is not unusual for providers to have contracts with more than one division. The nature and extent of monitoring of these providers' contracts will differ, depending on how each division monitors its contracts. Contractors should expect and receive a standard monitoring effort by the department.

The divisions and branches report that they maintain close and frequent contact with their contractors, but they have not always documented their efforts. As a result, in several cases we were unable to verify whether contracts were, in fact, being monitored.

Recommendation

We recommend that the department develop for its divisions written contract monitoring standards as guidelines on how contracts should be monitored and how monitoring activities should be documented.

Controls Over Cash Receipts are Inadequate

During our audit, we noted that the divisions and branches did not always remit cash receipts in a timely manner to the Administrative Services Office (ASO) for deposit. At times, cash receipts were remitted 6 to 27 working days after they had been received. Delays in depositing cash to the state treasury result in lost interest earnings to the State. Also, delays in making deposits increase the possibility that cash receipts may be lost or misplaced.

Some branches deposit cash receipts directly to the state treasury instead of remitting the receipts to ASO. But the deposits were not always reported to ASO in a timely manner for recording in the state's accounting records. Deposits were reported as late as 26 working days after the deposit was made.

Recommendation

Receipts should be deposited in the state treasury and recorded in the state's accounting records daily.

Moneys are Improperly Held in Special Revenue Fund Accounts

The department receives reimbursements from users for certain costs incurred in its water pollution and family planning programs. The department has been depositing these moneys into special revenue fund accounts instead of the general fund. At June 30, 1992, the cash balances of these accounts totalled \$225,000.

Both programs are supported by general fund appropriations and the Legislature has not authorized the department to establish and maintain special revenue fund accounts for these funds. Lacking legislative authorization for holding these receipts aside, the department should return the moneys to the general fund. Future receipts should also be deposited directly to the general fund.

Recommendations

The department should immediately transfer the cash balances of these accounts to the general fund. In addition, future reimbursements under these programs should be deposited directly into the general fund.

Bank Reconciliations Are Not Performed

The Developmental Disabilities Division maintains a \$50,000 checking account outside of the state treasury. The division had not performed a reconciliation of this account during the year. Performing bank reconciliations is a critical control over the checking account. Without a reconciliation of its account, the division cannot determine (1) whether all deposits have been properly recorded, (2) whether checks issued have been properly cashed, and (3) whether there are any unusual or erroneous charges to the bank account.

Recommendation

We recommend the division perform monthly bank reconciliations of its checking account.

Assets Are Not Recorded in Inventory

We found that not all equipment purchased during the year had been reported to the Department of Accounting and General Services (DAGS). DAGS maintains the official fixed asset inventory records of the State. These records are essential to maintain accountability for assets purchased with public funds. The DAGS Inventory Systems Manual requires each department to report all inventory transactions to DAGS within 15 days after the end of each quarter. The department failed to report to DAGS certain equipment it acquired during the year. As a result, these assets are not recorded on the official inventory records of the State.

Recommendation

We recommend that the department comply with DAGS' requirements and ensure that all equipment acquisitions are reported to DAGS on a timely basis.

Chapter 3

Financial Audit

This chapter presents the results of the financial audit of the Department of Health for the fiscal year ended June 30, 1992. It displays financial statements of all fund types and account groups administered by the department, together with explanatory notes. It also includes reports on the internal control structure and tests of compliance with laws and regulations.

Summary of Findings

In the opinion of Nishihama & Kishida, CPA's, Inc., based on their audit, except for the state hospitals fund and the general fixed assets account group, the financial statements present fairly, in all material respects, the combined financial position of the department as of June 30, 1992, and the combined results of its operations for the fiscal year then ended in conformity with generally accepted accounting principles.

Nishihama & Kishida, CPA's, Inc. noted no matters involving the internal control structure and its operation that they considered to be material weaknesses as defined in the report on the internal control structure. They also noted, with respect to items tested, that the department has complied, in all material respects, with laws and regulations applicable to the department.

Independent Auditors' Report

Nishihama & Kishida, CPA's, Inc.'s report filed with the Auditor is as follows:

Independent Auditors' Report

To the Auditor
State of Hawaii

We have audited the following financial statements of the State of Hawaii Department of Health:

Combined balance sheet—all fund types and account groups—June 30, 1992 (Exhibit A);

Combined statement of revenues, expenditures, and changes in fund balances—all governmental fund types and

expendable trust funds—fiscal year ended June 30, 1992
(Exhibit B); and

**Combined statement of revenues and expenditures—
budget and actual (budgetary basis)—general and special
revenue fund types—fiscal year ended June 30, 1992
(Exhibit C).**

These combined financial statements are the responsibility of the management of the State of Hawaii Department of Health. Our responsibility is to express an opinion on these combined financial statements based on our audit.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards and 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 combined financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall combined financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In accordance with the terms of our engagement, the scope of our audit did not include the audit of the state hospitals fund and the general fixed assets account group. The state hospitals fund and the general fixed assets account group are included in the accompanying financial statements of the State of Hawaii Department of Health for informational purposes only, and have been prepared from the books without audit and we express no opinion on them.

As discussed in the notes, the combined financial statements of the Department of Health are intended to present the financial position and results of operations of only that portion of the funds and account groups of the State of Hawaii that is attributable to the transactions of the Department of Health.

In our opinion, except for the matters described in the third paragraph, the combined financial statements referred to above present fairly, in all material respects, the financial position of the

State of Hawaii Department of Health as of June 30, 1992, and the results of its operations for the fiscal year then ended in conformity with generally accepted accounting principles.

/s/ Nishihama & Kishida, CPA's, Inc.

Honolulu, Hawaii
October 16, 1992

Description and Definitions

This section provides descriptions of the financial statements audited and definitions of technical terms used in this chapter.

Descriptions of financial statements and schedules

The following is a brief description of the financial statements audited by Nishihama & Kishida, CPA's, Inc. The financial statements are attached at the end of this chapter.

Combined balance sheet—all fund types and account groups (Exhibit A). This statement presents assets, liabilities, and fund balances of all fund types and account groups used by the department on an aggregate basis.

Combined statement of revenues, expenditures, and changes in fund balances—all governmental fund types and expendable trust funds (Exhibit B). This statement presents revenues, expenditures, other financing sources (uses) and changes in fund balances for all governmental fund types, and expendable trust funds of the department on an aggregate basis. Revenues include state appropriations mandated by the General Appropriations Act of 1991 (Act 296, Session Laws of Hawaii 1991) and other specific appropriations acts.

Combined statement of revenues and expenditures—budget and actual—general and special revenue fund types (Exhibit C). This statement presents a comparison of budgeted and actual revenues, expenditures, and other financing sources for the general fund accounts and special revenue funds used by the department.

The following is a brief description of the financial statements which have been prepared from the books of the department without audit by Nishihama & Kishida, CPA's, Inc. The financial statements are attached at the end of this chapter and are labeled "unaudited."

Statement of revenues, expenses, and changes in fund balance—state hospitals fund (Exhibit D). This unaudited statement presents the revenues, expenses, and changes in fund balance of the state hospitals fund used by the department.

Statement of cash flows—unrestricted state hospitals fund (Exhibit E). This unaudited statement presents the statement of cash flows of the unrestricted state hospitals fund used by the department.

Definition of terms

Technical terms are used in the financial statements and in the notes to the financial statements. The more common terms and their definitions are as follows:

Appropriation. An authorization granted by the State Legislature permitting a state agency, within established fiscal and budgetary controls, to incur obligations and to make expenditures.

Allotment. An authorization by the director of finance to a state agency to incur obligations and to make expenditures pursuant to the appropriation made by the State Legislature.

Encumbrance. An obligation in the form of a purchase order or contract which is chargeable to an appropriation, the incurring of which sets aside the appropriation for the amount of the obligation.

Expenditure. The actual disbursement of funds for the payment of goods delivered or services rendered, the obligation to pay for such goods or services having been incurred against authorized funds.

Reserve. An account used to earmark a portion of the fund balance to indicate that it is not available for expenditure.

Transfers. The transaction between funds, departments, and/or programs which is approved by the appropriate authority.

Notes to the Combined Financial Statements

Explanatory notes which are pertinent to an understanding of the combined financial statements and financial condition of the funds administered by the department are discussed in this section.

Financial statement presentation

General. The accompanying combined financial statements of the Department of Health present the financial position of various fund types and account groups, and the results of operations of the various fund types for the fiscal year ended June 30, 1992.

Reporting entity. The Department of Health is a department of the State of Hawaii.

Fund accounting. The financial activities are recorded in individual funds classified by type and described in the following sections, each of which is deemed to be a separate accounting entity. The financial position and operations of each fund are accounted for in separate self-balancing accounts which represent the fund's assets, liabilities, equity, revenues and expenditures or expenses.

Account groups are used to establish accounting control and accountability for the department's general fixed assets and general long-term obligations. Account groups are not funds as they do not reflect available financial resources and related liabilities.

Governmental fund types. Financial resources which are not accounted for in other funds are accounted for in the general fund. The measurement focus of governmental funds is on determination of financial position and changes in financial position rather than upon net income determination. The budget adopted by the Legislature provides the basic framework within which the resources and obligations of the general fund are accounted. The general fund of the department is a part of the State's general fund and the accompanying general fund financial statements are limited to and reflect only the appropriations, expenditures, and obligations of the general fund accounts used by the department, and the general fund allotments received by the department.

Financial resources obtained from specific revenue sources and used for restricted purposes are accounted for in the special revenue funds.

Substantially all financial resources obtained and used for the acquisition or construction of the department's general fixed assets and facilities are reflected in the capital projects fund. Such resources are derived principally from proceeds of general obligation bond issues and operating transfers from the special revenue funds.

Proprietary fund type. The state hospitals fund accounts for transactions related to the financial activities of the following community hospitals:

Hilo Hospital	Lanai Community Hospital
Honokaa Hospital	Leahi Hospital
Kau Hospital	Samuel Mahelona Memorial
Kauai Veterans Memorial	Hospital
Hospital	Maluhia Hospital
Kohala Hospital	Maui Memorial Hospital
Kona Hospital	and Hana Medical Center
Kula Hospital	

Fiduciary fund types. Expendable trust funds account for transactions related to assets held by the department in a trustee capacity to be expended for designated purposes. Agency funds are accounts for funds held by the department as agent.

Account groups. The general fixed assets account group is used to account for all fixed assets of the department other than those accounted for in the proprietary fund type. The general long-term debt account group is used primarily to account for the accrued vacation payable for governmental fund types.

Total columns on combined financial statements. Total columns on the accompanying combined financial statements are captioned “memorandum only” to indicate that they are presented only to facilitate financial analysis. Data in these columns do not purport to present financial position, results of operations, or changes in financial position or fund equity of the department in conformity with generally accepted accounting principles. Such data is not comparable to a consolidation.

Summary of significant accounting policies

Basis of accounting. The accounts of the governmental fund and fiduciary fund types are reported using the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when they become measurable and available to finance operations of the current fiscal year. Measurable means that the amount of the transaction can be determined. Available means that the amount is collected in the current fiscal year or soon enough after year-end to liquidate liabilities existing at the end of the fiscal year. Expenditures are generally recognized when the related liability is incurred, except for accumulated unpaid vacation and accrued workers’ compensation claims which are recognized as expenditures when payable from expendable available financial resources. Encumbrances are recorded obligations in the form of purchase orders or contracts. The department records encumbrances at the time purchase orders or contracts are awarded and executed. Encumbrances outstanding at fiscal year-end are reported as reservations of fund equity since they do not constitute expenditures or liabilities.

The proprietary fund is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of this fund are included on the balance sheet. Fund equity (i.e., net total assets) is segregated into contributed capital and retained earnings (deficit) components. Proprietary fund type operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets.

The accounts of the proprietary fund type are reported under the accrual basis of accounting. Under this method of accounting, revenues are recognized when they are earned and expenses are recorded when they are incurred.

Accumulated vacation and sick leave. Employees' vested annual vacation and sick leave are recorded as expenditures when actually taken. The employees of the department are entitled to receive cash payment for accumulated vacation leave upon termination. The liability for such accumulated vacation leave pay is not reflected in the governmental funds but is reflected in the general long-term debt account group for all funds, except for the proprietary fund type, which records accumulated vacation leave earned by hospital employees in the State hospitals fund.

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 have been recorded as operating transfers in the combined financial statements.

Inventory. Inventories of materials and supplies in the proprietary fund type are stated at the lower of cost (determined by the first-in, first-out method) or market. Inventories in all other funds are recorded as expenditures when purchased.

Investments. Investments are generally stated at cost, which approximates market. Fiduciary fund type investments are stated at fair market value at the date of donation.

Grants. Federal grants and assistance awards made on the basis of entitlement periods are recorded as intergovernmental receivables and revenues when entitlement occurs. All other Federal reimbursement type grants are recorded as intergovernmental receivables and revenues when the related expenditures or expenses are incurred.

Infrastructure fixed assets. Funds disbursed for the cost of infrastructure fixed assets are expended in the capital projects funds

and are not capitalized or reported in the department's combined balance sheet.

Depreciation. Depreciation is provided for property, plant and equipment in the proprietary fund type on the straight-line basis over the estimated useful lives of 5 to 50 years for buildings and improvements and 5 to 40 years for equipment.

Budgeting and budgetary control

The budget of the department is a detailed operating plan identifying estimated costs and results in relation to estimated revenues. The budget includes (1) the program, services and activities to be provided during the fiscal year, (2) the estimated revenues available to finance the operating plan and (3) the estimated spending requirements of the operating plan. The budget represents a process through which policy decisions are made, implemented, and controlled. Revenue estimates are provided to the Legislature at the time of budget consideration and are revised and updated throughout the fiscal year. Amounts reflected as budgeted revenues in Exhibit C are those estimates as compiled by the department. Budgeted expenditures are derived primarily from the General Appropriations Act of 1991 (Act 296, SLH 1991) and other specific appropriations acts.

All expenditures of these appropriated funds are made pursuant to the appropriation in the 1991-1993 biennial budget. The final legally adopted budget in Exhibit C represents the original appropriations, transfers, and other legally authorized legislative and executive changes.

Budgetary control is maintained at the appropriation line item as established in the appropriations acts. The governor is authorized to transfer appropriations within a state agency; however, transfers of appropriations between state agencies generally require legislative authorization. Records and reports reflecting the detail level of control are maintained by and are available at the department. During the fiscal year ended June 30, 1992, there were no expenditures in excess of appropriations at the legal level of budgetary control.

To the extent not expended or encumbered, general fund appropriations generally lapse at the end of the fiscal year in which the appropriations were made. The Legislature specifies the lapse date and any other particular conditions relating to terminating the authorization for other appropriations.

Budgets adopted by the Legislature for the general and special revenue funds are presented in Exhibit C. The department's annual budget is prepared on the modified accrual basis of accounting with several

differences, principally related to the encumbrances of purchase order and contract obligations. These differences represent departures from generally accepted accounting principles (GAAP). A reconciliation between non-GAAP budgetary actual and GAAP actual is as follows:

	General Fund	Special Revenue Funds
Excess of revenues and other sources over expenditures and other uses—actual on budgetary basis	\$ 1,101,926	\$ 26,729,569
Reserved for encumbrances at fiscal year-end	34,214,256	23,613,887
Expenditures for liquidation of prior fiscal year encumbrances	<u>(8,808,003)</u>	<u>(29,291,145)</u>
Excess of revenues and other sources over expenditures and other uses—GAAP basis	<u>\$26,508,179</u>	<u>\$21,052,311</u>

Loans, note and advances receivable

1. Loans receivable—At June 30, 1992, the Special Revenue Fund loans receivable consisted of \$22,139,836 in loans from the water pollution control program.
2. Note receivable—The department has an unsecured note receivable in the amount of \$47,079 from the Molokai General Hospital. The note provides for no payment of principal or interest during the first year. For the second through tenth years, payments shall be \$3,588 per month including interest at 10 1/2% per annum with any unpaid principal and interest due on August 1, 1993.
3. Advances receivable—The department advanced \$367,500 to the County of Hawaii for certain environmental projects. The advances are non-interest bearing and are due one year after the completion of the projects. As of June 30, 1992, no payments have been received.

General fixed assets

The changes in the general fixed assets (unaudited) were as follows:

	Land and Land Improvements	Buildings and Improvements	Equipment	Total
Balance at July 1, 1991	\$ 340,000	\$25,602,896	\$21,291,762	\$47,234,658
Additions	--	5,674	3,219,830	3,225,504
Deductions	--	--	648,330	648,330
Balance at June 30, 1992	<u>\$ 340,000</u>	<u>\$25,608,570</u>	<u>\$23,863,262</u>	<u>\$49,811,832</u>

General Long-Term Debt

The changes in the general long-term debt were as follows:

	Accrued Employee Benefits Payable	Installment Contracts Payable	Total
Balance at July 1, 1991	\$14,233,975	\$ 42,939	\$ 14,276,914
Net additions and payments	--	(12,803)	(12,803)
Net vacation earned but not taken	<u>277,556</u>	--	<u>277,556</u>
Balance at June 30, 1992	<u>\$14,511,531</u>	<u>\$ 30,136</u>	<u>\$ 14,541,667</u>

The department purchased office equipment under installment purchase contracts. Maturities of the installment purchase contracts are as follows:

Fiscal Year Ending June 30	Amount
1993	\$ 12,159
1994	9,425
1995	5,202
1996	<u>3,350</u>
	<u>\$ 30,136</u>

Changes in Assets and Liabilities of the Agency Fund

The agency fund is purely custodial (assets equal liabilities) and thus does not involve measurement of results of operations. The changes in assets and liabilities of the agency fund for the fiscal year ended June 30, 1992, were as follows:

	Balance July 1, 1991	Additions	Deductions	Balance June 30, 1992
ASSETS				
Cash and other assets held in trust	<u>\$ 1,341,499</u>	<u>7,350,656</u>	<u>6,996,486</u>	<u>\$ 1,695,669</u>
LIABILITIES				
Due to individuals and others	<u>\$ 1,341,499</u>	<u>7,350,656</u>	<u>6,996,486</u>	<u>\$ 1,695,669</u>

Retirement plan

All eligible employees of the department are required by Chapter 88 of the Hawaii Revised Statutes to become 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. Prior to June 30, 1984, the plan 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 excluded from the noncontributory option. The noncontributory option provides for reduced benefits and covers most eligible employees hired after June 30, 1984. Employees hired before that date 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 for the contributory and noncontributory options, respectively.

The ERS's funding policy provides for employer contributions at actuarially determined rates that should provide sufficient resources to pay member pension benefits when due. The funding method used to calculate the total employer contribution required is the frozen initial liability method.

Under this method, the total employer contribution is comprised of the "normal cost" plus the level annual payment required to amortize the frozen unfunded accrued liability. The employer normal cost is the level percentage of payroll contribution to pay all future benefits, after subtracting expected future member contributions, the unfunded accrued liability, and the assets accumulated as of the valuation date. Actuarial gains and losses resulting from differences between actual and assumed experience are reflected in the employer normal cost rates.

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.

The amount shown as “pension benefit obligation” is a standardized disclosure measure of the present value of credited projected pension benefits, adjusted for effects of projected salary increases, estimated to be payable in the future as a result of member service to date. The measure is the actuarial present value of credited projected benefits and is intended to help users assess the funding status of the ERS on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement systems. The measure is independent of the actuarial funding method used to determine contributions to the ERS described previously.

The pension benefit obligation was determined as of June 30, 1991. Significant assumptions underlying the actuarial computations include:

- In accordance with the provisions of Act 184 of the 1989 Regular Session of the State legislature, the long-term rate of investment yield on the assets of the ERS is assumed to be 8% per year.
- An assumed annual salary increase of 6-1/2% per year for all members.
- The assumed rates of retirement, turnover and disability were based upon the ERS’s experience.
- The assumed mortality rates were based on published statistical data as determined by the ERS’s experience.
- The unused sick leave credit accumulated by members is assumed at 12 days per year.

At June 30, 1991, the total and unfunded pension benefit obligation for all members of the ERS was as follows:

Pension benefit obligation:	
Pensioners and beneficiaries currently receiving benefits and terminated members not yet receiving benefits	\$ 2,126,690,400
Current members:	
Accumulated member contributions	832,605,300
Employer-financed vested	1,377,273,900
Employer-financed nonvested	<u>1,210,584,900</u>
Total pension benefit obligation	5,547,154,500
Net assets available for pension benefits, at cost	<u>4,080,839,938</u>
Unfunded pension benefit obligation	<u>\$ 1,466,314,562</u>

Ten-year historical trend information designed to provide information about the ERS's progress in accumulating sufficient assets to pay benefits when due is included in the separately issued audited financial statements of the ERS.

In addition to providing pension benefits, the State provides certain health care and life insurance benefits to retired State employees. Contributions are based upon negotiated collective bargaining agreements, and are funded by the State as accrued. The department's general fund and state hospitals fund share of the expense for post-retirement benefits for the fiscal year ended June 30, 1992, has not been separately computed and is not reflected in the department's combined financial statements. The department's special revenue fund share of the post-retirement health care and life insurance benefits expense for the fiscal year ended June 30, 1992, was approximately \$698,200 and is included in the special revenue funds' financial statements.

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 rentals on noncancelable operating leases at June 30, 1992:

Fiscal Year Ending June 30	Amount
1993	\$ 169,691
1994	62,563
1995	63,824
1996	61,495
1997	<u>42,798</u>
	<u>\$ 400,371</u>

Commitments and contingencies

Insurance coverage. Insurance coverage is maintained at the State level. The State is substantially self-insured for all perils including workers' compensation. Expenditures for workers' compensation and other insurance claims are appropriated annually from the state general fund.

Litigation. The department is a party to various legal proceedings, most of which normally occur in governmental operations. Although the department and its counsel are unable to express opinions as to the outcome of the litigations, it is their opinion that any potential liability arising therefrom, will not have a material adverse effect on the financial position of the department because any judgments against the department are judgments against the State and would have to be paid by legislative appropriation of the state general fund and not by the department.

Accumulated sick pay. Employees earn sick leave credits at the rate of one and three-quarters working days for each month of service without limit. Sick leave can 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 sixty days or more of unused sick leave is entitled to additional service credit in the Employees' Retirement System. Accumulated sick leave as of June 30, 1992 approximated \$42,500,000, including \$25,100,000 relating to the community hospitals in the state hospitals fund.

Deferred compensation plan. In 1983, the State established a deferred compensation plan which enables state employees to defer a portion of their compensation. The state Department of Personnel Services has the fiduciary responsibility of administering the plan. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency. All amounts of compensation deferred under the plan, all property and

rights purchased with those amounts, and all income attributable to those amounts, property, or gifts are (until paid or made available to the employee or other beneficiary) solely the property and rights of the State (without being restricted to the provisions of benefits under the plan), subject to the claims of the state's general creditors. Participants' rights under the plan are equal to those of the general creditors of the State in an amount equal to the fair market value of the deferred account for each participant.

Independent Auditors' Report on the Internal Control Structure

To the Auditor
State of Hawaii

We have audited the combined financial statements, except for the state hospitals fund and the general fixed assets account group, of the State of Hawaii Department of Health as of and for the fiscal year ended June 30, 1992, and have issued our report thereon dated October 16, 1992.

We conducted our audit in accordance with generally accepted auditing standards and 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 combined financial statements are free of material misstatement.

In planning and performing our audit of the combined financial statements of the State of Hawaii Department of Health for the fiscal year ended June 30, 1992, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the combined financial statements and not to provide assurance on the internal control structure.

The management of the State of Hawaii Department of Health is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of combined financial statements in accordance with

generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

- Revenues and receipts
- Purchases and disbursements
- Payroll

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the combined financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operation that we consider to be material weaknesses as defined above.

However, we noted certain matters involving the internal control structure and its operation that we have reported to the Auditor, State of Hawaii, in Chapter 2.

This report is intended for the information of the Auditor, State of Hawaii and management of the State of Hawaii Department of Health. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

/s/ Nishihama & Kishida, CPA's, Inc.

Honolulu, Hawaii
October 16, 1992

**Independent
Auditors' Report
on Compliance
Based on an Audit
of the Combined
Financial
Statements**

To the Auditor
State of Hawaii

We have audited the combined financial statements, except for the state hospitals fund and the general fixed assets account group, of the State of Hawaii Department of Health as of and for the fiscal year ended June 30, 1992, and have issued our report thereon dated October 16, 1992.

We conducted our audit in accordance with generally accepted auditing standards and 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 combined financial statements are free of material misstatement.

Compliance with laws and regulations applicable to the State of Hawaii Department of Health is the responsibility of the State of Hawaii Department of Health's management. As part of obtaining reasonable assurance about whether the combined financial statements are free of material misstatement, we performed tests of the State of Hawaii Department of Health's compliance with certain provisions of laws and regulations. However, our objective was not to provide an opinion on overall compliance with such provisions.

The results of our tests indicate that, with respect to the items tested, the State of Hawaii Department of Health complied, in all material respects, with the provisions referred to in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that the Department of Health had not complied, in all material respects, with those provisions.

This report is intended for the information of the Auditor, State of Hawaii and management of the State of Hawaii Department of Health. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

/s/ Nishihama & Kishida, CPA's, Inc.

Honolulu, Hawaii
October 16, 1992

State of Hawaii
 Department of Health
 COMBINED BALANCE SHEET - ALL FUND TYPES AND ACCOUNT GROUPS
 June 30, 1992

	Governmental Fund Types			Proprietary Fund Type	Fiduciary Fund Type	Account Groups		Total (Memorandum Only)
	General	Special Revenue	Capital Projects	State Hospitals (Unaudited)	Trust and Agency	General Fixed Assets (Unaudited)	General Long-Term Debt	
ASSETS								
Cash	\$42,839,781	\$57,824,547	\$5,600,126	\$ 15,171,395	\$2,813,911	\$ -	\$ -	\$124,249,760
Investments	-	7,000,000	-	-	808	-	-	7,000,808
Receivables								
Trade, net of allowance for doubtful accounts of \$35,266,885	-	-	-	47,951,850	-	-	-	47,951,850
Note receivable	47,079	-	-	-	-	-	-	47,079
Loans receivable	-	22,139,836	-	-	-	-	-	22,139,836
Advances	367,500	-	-	-	-	-	-	367,500
Premium settlement	-	5,519,497	-	-	-	-	-	5,519,497
Accrued interest receivable	-	759,787	-	-	-	-	-	759,787
Other	-	4,267	-	2,084,702	-	-	-	2,088,969
Due from Federal government	-	2,375,686	-	197,979	-	-	-	2,573,665
Due from other funds	-	172,540	-	10,267	-	-	-	182,807
Inventories	-	-	-	3,129,426	-	-	-	3,129,426
Prepaid expenses and deposits	-	-	-	21,197	-	-	-	21,197
Land and land improvements	-	-	-	1,454,660	-	340,000	-	1,794,660
Buildings and improvements	-	-	-	104,048,670	-	25,608,570	-	129,657,240
Equipment	-	-	-	58,440,256	-	23,863,262	-	82,303,518
Less accumulated depreciation	-	-	-	(69,159,017)	-	-	-	(69,159,017)
Construction in progress	-	-	-	8,077,158	-	-	-	8,077,158
Restricted assets, including cash of \$1,090,761	-	-	-	9,239,652	-	-	-	9,239,652
Amount to be provided for the retirement of general long-term debt	-	-	-	-	-	-	14,541,667	14,541,667
TOTAL ASSETS	\$43,254,360	\$95,796,160	\$5,600,126	\$180,668,195	\$2,814,719	\$49,811,832	\$14,541,667	\$392,487,059

(Continued)

State of Hawaii
Department of Health
COMBINED BALANCE SHEET - ALL FUND TYPES AND ACCOUNT GROUPS (Continued)
June 30, 1992

	Governmental Fund Types			Proprietary Fund Type	Fiduciary Fund Type	Account Groups		Total (Memorandum Only)
	General	Special Revenue	Capital Projects	State Hospitals (Unaudited)	Trust and Agency	General Fixed Assets (Unaudited)	General Long-Term Debt	
LIABILITIES AND FUND EQUITY								
LIABILITIES								
Vouchers payable	\$ 7,369,351	\$ 2,638,598	\$ 262,654	\$ 6,059,406	\$ 127,796	\$ -	\$ -	\$ 16,457,805
Accrued wages and employee benefits payable	1,155,504	97,225	-	11,274,643	-	-	14,511,531	27,038,903
Custodial funds and deposits	-	-	-	277,556	-	-	-	277,556
Due to State General Fund	515,249	5,744,821	-	92,526,794	-	-	-	98,786,864
Other accrued liabilities	-	-	-	2,433,286	-	-	-	2,433,286
Due to other funds	-	64,858	-	10,267	107,682	-	-	182,807
Due to individuals	-	-	-	184,238	1,695,669	-	-	1,879,907
Installment contracts payable	-	-	-	-	-	-	30,136	30,136
Total liabilities	<u>9,040,104</u>	<u>8,545,502</u>	<u>262,654</u>	<u>112,766,190</u>	<u>1,931,147</u>	<u>-</u>	<u>14,541,667</u>	<u>147,087,264</u>
FUND EQUITY								
Investment in general fixed assets	-	-	-	-	-	49,811,832	-	49,811,832
Fund balances								
Restricted	-	-	-	9,216,308	-	-	-	9,216,308
Unrestricted	-	-	-	58,685,697	-	-	-	58,685,697
Reserved for encumbrances	34,214,256	23,613,887	5,337,472	-	665,161	-	-	63,830,776
Reserved for loans and grants	-	61,798,898	-	-	-	-	-	61,798,898
Reserved for others	-	-	-	-	218,411	-	-	218,411
Unreserved	-	1,837,873	-	-	-	-	-	1,837,873
Total fund equity	<u>34,214,256</u>	<u>87,250,658</u>	<u>5,337,472</u>	<u>67,902,005</u>	<u>883,572</u>	<u>49,811,832</u>	<u>-</u>	<u>245,399,795</u>
TOTAL LIABILITIES AND FUND EQUITY	<u>\$43,254,360</u>	<u>\$95,796,160</u>	<u>\$5,600,126</u>	<u>\$180,668,195</u>	<u>\$2,814,719</u>	<u>\$49,811,832</u>	<u>\$14,541,667</u>	<u>\$392,487,059</u>

See accompanying notes to the combined financial statements.

State of Hawaii
Department of Health
COMBINED STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - ALL GOVERNMENTAL
FUND TYPES AND EXPENDABLE TRUST FUNDS
Fiscal year ended June 30, 1992

	Governmental Fund Types			Fiduciary Fund Type Expensible Trust	Total (Memorandum Only)
	General	Special Revenue	Capital Projects		
REVENUES					
State allotted appropriations	\$245,606,741	\$ -	\$ 13,000,000	\$ -	\$258,606,741
Intergovernmental revenues	-	50,809,140	-	-	50,809,140
Interest income	-	2,896,710	-	11,710	2,908,420
Other revenues	-	832,363	-	1,489,765	2,322,128
	<u>245,606,741</u>	<u>54,538,213</u>	<u>13,000,000</u>	<u>1,501,475</u>	<u>314,646,429</u>
EXPENDITURES					
Natural physical environment	1,466,459	1,083,662	-	-	2,550,121
Pollution control	3,660,005	20,124,345	-	-	23,784,350
Health promotion and disease prevention	43,118,784	19,510,088	-	-	62,628,872
Hospital care	4,725,697	-	-	-	4,725,697
Behavioral health	61,163,032	7,666,198	-	-	68,829,230
Personal health	33,898,240	3,459,750	-	-	37,357,990
Environmental health services	6,545,000	240,245	-	-	6,785,245
Health resources and program support	32,116,436	1,432,316	-	-	33,548,752
Overall program support for social services	-	67,650	-	-	67,650
Overall program support	11,198,830	3,325,041	-	-	14,523,871
Capital outlays	-	-	694,669	-	694,669
Others	-	-	-	1,329,764	1,329,764
	<u>197,892,483</u>	<u>56,909,295</u>	<u>694,669</u>	<u>1,329,764</u>	<u>256,826,211</u>
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	<u>47,714,258</u>	<u>(2,371,082)</u>	<u>12,305,331</u>	<u>171,711</u>	<u>57,820,218</u>
OTHER FINANCING SOURCES (USES)					
Operating transfers in	-	31,574,855	2,080,000	52,256	33,707,111
Operating transfers out	(21,206,079)	(8,151,462)	(13,000,000)	-	(42,357,541)
	<u>(21,206,079)</u>	<u>23,423,393</u>	<u>(10,920,000)</u>	<u>52,256</u>	<u>(8,650,430)</u>
EXCESS OF REVENUES AND OTHER SOURCES OVER EXPENDITURES AND OTHER USES	26,508,179	21,052,311	1,385,331	223,967	49,169,788
OTHER CHANGES IN FUND BALANCES					
Lapsed appropriations	(5,219,700)	-	(1,227)	-	(5,220,927)
Increase in reserve for loans receivable	-	22,139,836	-	-	22,139,836
	<u>(5,219,700)</u>	<u>22,139,836</u>	<u>(1,227)</u>	<u>-</u>	<u>16,918,909</u>
EXCESS OF REVENUES AND OTHER SOURCES OVER EXPENDITURES, OTHER USES AND OTHER CHANGES IN FUND BALANCES	21,288,479	43,192,147	1,384,104	223,967	66,088,697
FUND BALANCES AT JULY 1, 1991	<u>12,925,777</u>	<u>44,058,511</u>	<u>3,953,368</u>	<u>659,605</u>	<u>61,597,261</u>
FUND BALANCES AT JUNE 30, 1992	<u>\$ 34,214,256</u>	<u>\$ 87,250,658</u>	<u>\$ 5,337,472</u>	<u>\$ 883,572</u>	<u>\$127,685,958</u>

See accompanying notes to the combined financial statements.

State of Hawaii
Department of Health
COMBINED STATEMENT OF REVENUES AND EXPENDITURES - BUDGET AND ACTUAL (BUDGETARY BASIS) - GENERAL AND SPECIAL REVENUE FUND TYPES
Fiscal year ended June 30, 1992

	General Fund			Special Revenue Funds		
	Actual on Budgetary Basis	Budget	Variance Favorable (Unfavorable)	Actual on Budgetary Basis	Budget	Variance Favorable (Unfavorable)
REVENUES						
State allotted appropriations	\$245,606,741	\$245,606,741	\$ -	\$ -	\$ -	\$ -
Intergovernmental revenues	-	-	-	33,853,021	28,776,253	5,076,768
Other revenues	-	-	-	284,363	587,408	(303,045)
Unbudgeted revenues	-	-	-	19,881,248	-	19,881,248
	<u>245,606,741</u>	<u>245,606,741</u>	<u>-</u>	<u>54,018,632</u>	<u>29,363,661</u>	<u>24,654,971</u>
EXPENDITURES						
Natural physical environment	1,607,293	1,709,667	102,374	1,386,129	2,504,303	1,118,174
Pollution control	4,696,173	4,837,550	141,377	2,694,612	3,348,311	653,699
Health promotion and disease prevention	48,204,912	48,766,385	561,473	18,335,431	19,694,749	1,359,318
Hospital care	5,093,923	5,093,923	-	-	-	-
Behavioral health	65,855,044	66,143,852	288,808	7,686,708	9,617,517	1,930,809
Personal health	6,676,351	6,685,569	9,218	-	-	-
Environmental health services	37,938,011	38,543,041	605,030	3,933,843	5,400,623	1,466,780
Health resources and program support	46,487,173	46,632,542	145,369	1,279,564	2,235,589	956,025
Overall program support for social services	-	-	-	67,444	67,522	78
Overall program support	7,705,313	7,816,357	111,044	3,227,482	5,703,532	2,476,050
Unbudgeted	-	-	-	11,135,787	-	(11,135,787)
	<u>224,264,193</u>	<u>226,228,886</u>	<u>1,964,693</u>	<u>49,747,000</u>	<u>48,572,146</u>	<u>(1,174,854)</u>
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	<u>21,342,548</u>	<u>19,377,855</u>	<u>1,964,693</u>	<u>4,271,632</u>	<u>(19,208,485)</u>	<u>23,480,117</u>
OTHER FINANCING SOURCES (USES)						
Operating transfers in	-	-	-	30,609,399	30,297,855	311,544
Operating transfers out	(20,240,622)	(19,377,855)	(862,767)	(8,151,462)	-	(8,151,462)
	<u>(20,240,622)</u>	<u>(19,377,855)</u>	<u>(862,767)</u>	<u>22,457,937</u>	<u>30,297,855</u>	<u>(7,839,918)</u>
EXCESS OF REVENUES AND OTHER SOURCES OVER EXPENDITURES AND OTHER USES	<u>\$ 1,101,926</u>	<u>\$ -</u>	<u>\$ 1,101,926</u>	<u>\$26,729,569</u>	<u>\$ 11,089,370</u>	<u>\$ 15,640,199</u>

See accompanying notes to the combined financial statements.

State of Hawaii
 Department of Health
 STATEMENT OF REVENUES, EXPENSES, AND
 CHANGES IN FUND BALANCE - STATE HOSPITALS FUND
 Fiscal year ended June 30, 1992
 (Unaudited)

OPERATING REVENUES		
Patients service revenue		\$188,706,153
Contractual and other allowances and adjustments		<u>(44,513,398)</u>
Net revenue from services to patients		144,192,755
Other operating revenues		<u>3,174,251</u>
Total operating revenues		147,367,006
OPERATING EXPENSES		
Personal services	\$ 34,092,573	
Nursing services	57,110,394	
General administration	61,503,168	
Depreciation	6,943,208	
Other	<u>5,327,400</u>	<u>164,976,743</u>
Loss from operations		(17,609,737)
NON-OPERATING REVENUES		
Others		<u>31,609,094</u>
Excess of revenues over expenses before other financing sources		13,999,357
OTHER FINANCING SOURCES		
Net transfers in from State of Hawaii Capital Projects Funds	7,265,638	
Donated equipment	64,469	
Prior year transfers	142,022	
Other	<u>(107,318)</u>	<u>7,364,811</u>
NET EARNINGS		21,364,168
FUND BALANCE AT JULY 1, 1991		<u>46,537,837</u>
FUND BALANCE AT JUNE 30, 1992		\$ <u>67,902,005</u>

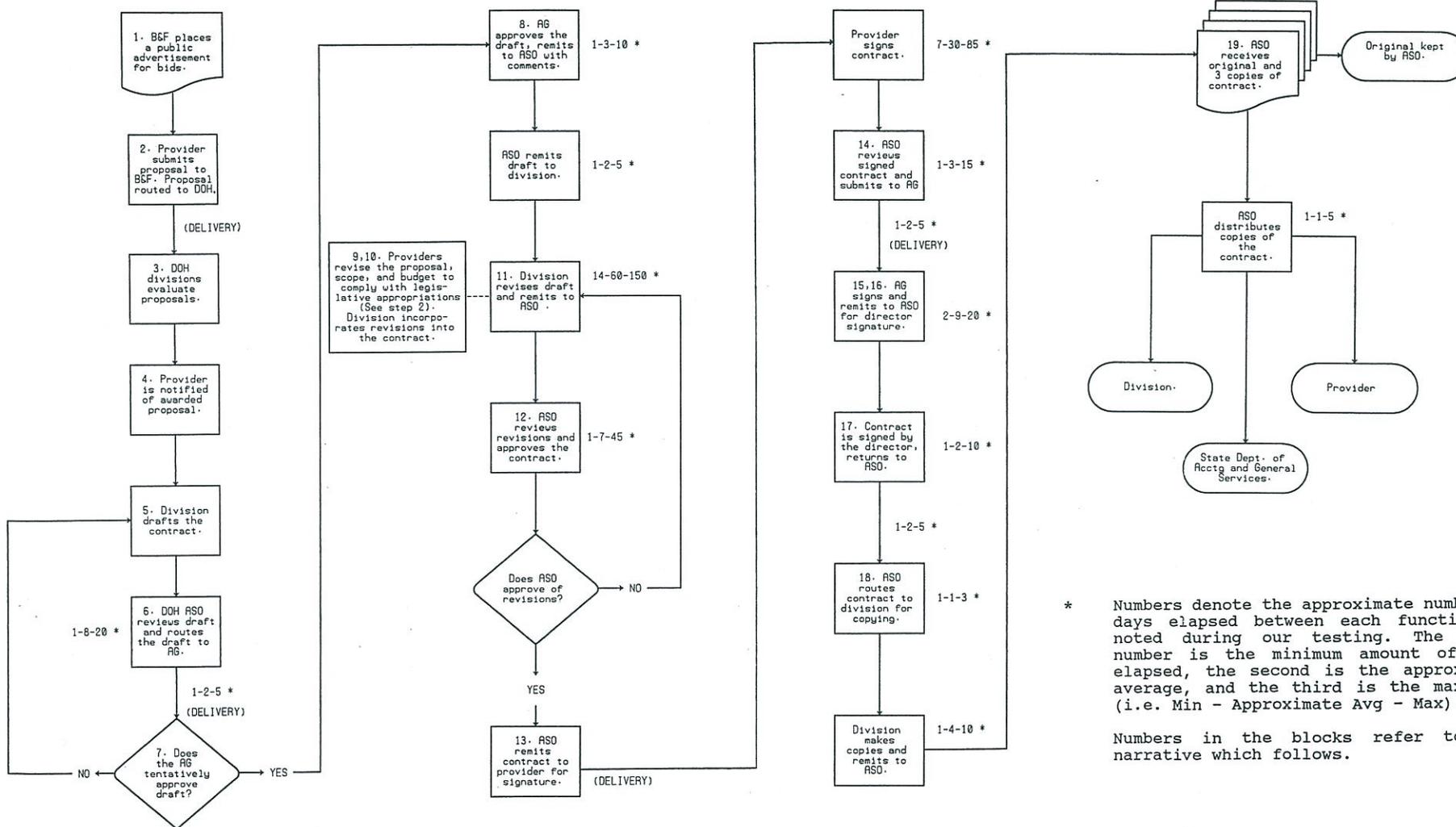
See accompanying notes to the combined financial statements.

State of Hawaii
 Department of Health
 STATEMENT OF CASH FLOWS -
 UNRESTRICTED STATE HOSPITALS FUND
 Fiscal year ended June 30, 1992
 (Unaudited)

Cash flows from operating activities		
Loss from operations		\$(17,609,737)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	\$ 6,943,208	
Other	1,189,908	
Increase in accounts receivable	(8,451,341)	
Decrease in other receivables	2,277,326	
Increase in inventories	(376,566)	
Decrease in prepaid expenses and deposits	25,824	
Decrease in vouchers payable	(2,919,305)	
Increase in other accrued liabilities	<u>7,565,018</u>	<u>6,254,072</u>
Net cash used in operating activities		(11,355,665)
Cash flows from noncapital financing activities		
Interest paid on bonds	(847,761)	
Transfers for payment of interest	876,498	
Operating transfers in from State General Fund	21,703,077	
Operating transfers in from State Special Revenue Funds	5,887,651	
Other noncapital cash flows	<u>52,857</u>	
Net cash provided by noncapital financing activities		27,672,322
Cash flows from capital and related financing activities		
Acquisition and construction of property and equipment	(6,493,341)	
Transfer from restricted funds	2,926,246	
Payments on capital lease obligations	(119,765)	
Other	<u>(25,287)</u>	
Net cash used in capital and related financing activities		<u>(3,712,147)</u>
NET INCREASE IN CASH		12,604,510
Cash at July 1, 1991		<u>2,566,885</u>
Cash at June 30, 1992		<u><u>\$15,171,395</u></u>

See accompanying notes to the combined financial statements.

State of Hawaii
 Department of Health
PURCHASE OF SERVICES CONTRACT PROCESSING SYSTEM
 Fiscal year ended June 30, 1992



NARRATIVE OF PURCHASE OF SERVICES CONTRACT PROCESSING SYSTEM

1. The State Department of Budget and Finance advertises for bid proposals for all state departments in a generally circulated newspaper within the first quarter of the state fiscal year to attract prospective bidders.
2. The Department of Budget and Finance normally allows six weeks for providers to submit their proposals. Proposals are then forwarded to the Department of Health through the department's Administrative Services Office (ASO).
3. The Department of Health divisions evaluate proposals and recommend a provider to ASO. Initial recommendations from the department are usually due to the Department of Budget and Finance six weeks from the provider submission deadline.
4. The department, through the divisions, notifies the selected provider of the award in writing after the Department of Budget and Finance and the governor approve the department's recommended budget and list of providers.
5. The divisions may develop the contract draft prior to the appropriations given by the Legislature, based on the proposal accepted from the potential providers.
6. The ASO reviews the first draft of the contract for completeness of format (i.e. inclusion of authoritative sources to contract and expend for services, funding source, scope of service, time of performance, etc.). This generally occurs in March.
7. The Office of the Attorney General (AG) reviews the first draft of the contract for appropriateness of contract language and legislative intent.
8. When the AG does not approve the draft, it is returned to the divisions for revisions, in which steps 6 through 7 are repeated until the AG tentatively approves the draft. The AG sends the approved draft to ASO for initialization of the finalized form.
9. The Legislature generally appropriates the moneys to the department in late April. ASO then notifies the divisions of appropriated amounts generally in early May (although the Governor generally does not sign the appropriations act until June).
10. The division notifies the provider of the appropriated amounts. The provider revises the scope of services and expenditure budgets to comply with the appropriations and submits the revision to the division for approval.
11. The division reviews the revisions and incorporates them into a final draft for approval from ASO. There may be several approval levels within a division depending on the size of the division. At this point, an average of one to two months elapses from the time ASO notifies the divisions of the appropriations.
12. ASO reviews the final draft to determine if all earlier comments for revisions by ASO and the AG were made.

13. Once the ASO approves the final contract draft, ASO sends the contract to the provider for signature(s). Occasionally, when technicalities are not readily resolved, the contract is returned to the division for correction and the division sends the corrected contract to the provider for signature. Another month may pass before the provider returns the contract signed. The provider must also submit an acknowledgment form, corporate resolution form, and certificate of insurance at the same time with the signed contract.
14. ASO performs a final review of the signed contract before submitting it to the AG for final approval. ASO checks that all required attachments are present and that the Certificate of Insurance is consistent with the contract period and amount of liability coverage.
15. The AG performs a final review, signs, and returns the contract to ASO.
16. ASO forwards the contract to the director's office for signature.
17. ASO forwards the signed contract to the divisions for photocopying.
18. Divisions forward the original and 2 copies to ASO for distribution to the provider and the State Department of Accounting and General Services. A third copy is retained by the division. The original remains with ASO.

Response of the Affected Agency

Comments on Agency Response

We transmitted a draft of this report to the Department of Health on December 7, 1992. A copy of the transmittal letter to the department is included as Attachment 1. The department's response is included as Attachment 2.

The department generally agrees with our findings and recommendations. It is attempting to improve contract processing time and develop clear contract payment terms. The department states it will develop guidelines for contract monitoring. Further, the department recognizes the problems of untimely deposits and failure to reconcile checking accounts and is working on procedures to ensure timely deposits and bank reconciliations. It also concurs with our recommendation to comply with DAGS' requirements to report equipment acquisitions on a timely basis.

The department does not agree, however, with our recommendation to return moneys to the general fund. The department intends to seek legislative approval to expend the funds currently held in special revenue accounts instead of returning the money to the general fund. It contends that depositing receipts generated by the family planning program into the general fund would prevent the department from complying with federal requirements. It cites a statement in the federal guidelines that program income shall be retained by the recipient and used for allowable costs of the project. Since this program is substantially supported by general fund appropriations, we believe the State is the proper recipient of program receipts and that the funds should be deposited to the general fund.

ATTACHMENT 1

STATE OF HAWAII
OFFICE OF THE AUDITOR
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917



MARION M. HIGA
State Auditor

(808) 587-0800
FAX: (808) 587-0830

C O P Y

December 7, 1992

The Honorable John C. Lewin, M.D.
Director of Health
State of Hawaii
1250 Punchbowl Street
Honolulu, HI 96813

Dear Dr. Lewin:

Enclosed are three copies, numbered 6 through 8, of our draft report, *Financial Audit of the Department of Health*. We ask that you telephone us by Wednesday, December 9, 1992, on whether you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Thursday, December 17, 1992.

The Governor and presiding officers of the two houses of the Legislature have also been provided copies of this draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

Marion M. Higa
State Auditor

Enclosures



JOHN WAIHEE
GOVERNOR OF HAWAII

JOHN C. LEWIN, M.D.
DIRECTOR OF HEALTH

STATE OF HAWAII
DEPARTMENT OF HEALTH

P. O. BOX 3378
HONOLULU, HAWAII 96801
FAX - 548-3263

In reply, please refer to:
File:

December 16, 1992

ASO-F-6469

Ms. Marion M. Higa
State Auditor
Office of the Auditor
State of Hawaii
465 South King Street, Room 500
Honolulu, Hawaii 96813

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OFC. OF THE AUDITOR
STATE OF HAWAII

Dear Ms. Higa:

We have reviewed the preliminary draft of the Financial Audit of the Department of Health and would like to address the findings made in this report.

1. Contracts Are Not Executed in a Timely Manner.

The Department has continually made efforts to streamline and expedite the contract process by establishing an earlier timetable to submit contract drafts to the Administrative Services Office (ASO), developing standard boilerplates and scopes of services, and informing the contractors to return the signed contracts directly to ASO rather than to the programs.

While we recognize the numerous steps in our decentralized system, we feel these steps in the process are necessary for program accountability and would welcome any suggestions for improvements.

The Divisions will be reminded to expedite the final contracts to ASO as soon as the Legislature determines the final lump sum POS amounts. Section 42D-12, HRS, which allows for a ninety day extension into the subsequent fiscal year, will also help to alleviate some of the timeliness problem.

To: Marion Higa
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December 16, 1992

For the upcoming fiscal biennium, the Department is developing a POS contract format which would be similar to the Attorney General's consultant format and should reduce the review time in ASO and the Attorney General's Office.

2. Contract Payment Terms are Unclear.

The Department agrees that the payment terms are not always clear and will change the payment terms of the Alcohol and Drug Abuse Division's contracts in the upcoming biennium to be based on reimbursements of actual expenditures with performance levels specified in the contract to ensure that a minimum number of service units will be provided.

3. Contract Monitoring Procedures Need to be Standardized.

The Department will develop guidelines for contract monitoring to comply with the audit recommendations and Section 42D-25, HRS.

4. Controls Over Cash Receipts are Inadequate.

The Department recognizes the problem of untimely deposits. We have had some difficulties ensuring total compliance. Fortunately, the incidents have been limited and we will continue to send reminders and ask our programs to more closely monitor their cash receipt deposits.

5. Moneys are Improperly Held in Special Revenue Fund Accounts.

The Department intends to seek Legislative approval to expend funds for both the water pollution and family planning programs. We believe these funds are program earned and should remain within the programs' accounts. It should be noted, for example, that if the receipts were deposited into the General Fund, we would not be able to comply with 45 CFR, part 74.42 (d), Grant

To: Marion Higa
Page 3
December 16, 1992

Related Income, as mandated in the Notice of Grant Award for the Title X Family Planning Project. This section of the CFR states that program income shall be retained by the recipient and used for allowable costs of the project, and may count toward satisfying a matching requirement.

6. Bank Reconciliations Were Not Performed.

The Developmental Disabilities Division administers the respite program and its petty cash checking account for the Personal Health Services Administration. The petty cash account was established to accommodate and facilitate timely disbursements to the program's beneficiaries.

The Division initially established a manual system of reconciliation. The respite program staff was to reconcile requests, disbursements, and deposits against monthly bank statements. System transitioning and increase volume of workload caused delays in manual reconciliations. Therefore, the Division implemented a computerized system of reconciliation and is in the final stages of refining that system.

7. Assets Were Not Recorded in Inventory.

The Department concurs with this finding and intends to comply with DAGS' requirements that equipment acquisitions are reported on a timely basis.

Thank you for providing us with the opportunity to respond to your audit findings and recommendations.

Sincerely,


Dr. JOHN C. LEWIN, M.D.
Director of Health