Financial Audit of the Department of Human Services

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

Report No. 94-5
January 1994

THE AUDITOR
STATE OF HAWAII

Financial Audit of the Department of Human Services

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

THE AUDITOR
STATE OF HAWAII

Financial Audit of the Department of Human Services

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

Conducted by

The Auditor
State of Hawaii
and
KPMG Peat Marwick, Certified Public Accountants

Submitted by

THE AUDITOR
STATE OF HAWAII

Report No. 94-5
January 1994

Foreword

This is a report of our financial audit of the Department of Human Services for the fiscal year July 1, 1992 to June 30, 1993. 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 KPMG Peat Marwick.

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

Marion M. Higa
State Auditor

Table of Contents

Chapter 3 Financial Audit

List of Tables

List of Exhibits

List of Schedules

Chapter 1
Introduction

This is a report of our financial audit of the State of Hawaii, Department of Human Services. The audit was conducted by the Office of the Auditor and the certified public accounting firm of KPMG Peat Marwick. 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 combined financial statements of the department.

2. Assess the adequacy, effectiveness, and efficiency of the systems and procedures relating to the financial accounting, reporting, and internal controls of the department and to recommend improvements to such systems, procedures, and reports.

3. Determine whether expenditures and other disbursements have been made and 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.

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 Social Services and Housing. In 1987, the name was changed to the Department of Human Services. Section 26-14, HRS, describes the department's responsibilities:

> The department shall administer programs designed to improve the social well-being and productivity of the people of the State. Without limit to the generality of the foregoing, the department shall concern itself with problems of human behavior, adjustment, and daily living through the administration of programs of family, child and adult welfare, economic assistance, health care assistance, rehabilitation toward self-care and support, public housing, and other related programs provided by law.

Organization

The department is headed by the director of human services. The director has overall responsibility for planning, directing, and coordinating the various programs. The department is organized into staff offices and operating divisions.

Staff offices

Six staff offices provide support services to the department.

The Administrative Services Office provides fiscal management, budgeting, and management improvement services.

The Information Systems Office is responsible for the planning, management, development, and maintenance of all matters relating to the department's electronic data processing applications.

The Personnel Office manages the personnel programs.

The Planning Office assists and coordinates the budget preparation, implementation, and monitoring activities of all programs in the department.

The Administrative Appeals Office reviews administrative proceedings and advises the director on matters pertaining to the department's administrative rules.

The Evaluation Office assists in evaluating and assessing the department's capabilities in implementing public programs and utilizing resources more effectively.

Operating divisions

Four operating divisions carry out the programs of the department.

The Family and Adult Services Division provides social services, economic assistance, and medical care assistance payments to eligible families and individuals.

The Health Care Administration Division has overall management of the plans, policies, regulations, and procedures of the department's medical assistance program.

The Vocational Rehabilitation and Services for the Blind Division administers programs of vocational rehabilitation, independent living rehabilitation, services for the blind, and disability determination, as provided in federal and state statutes, regulations, policies, and agreements between the State and federal government agencies.

The Self-Sufficiency and Support Services Division provides case management, educational, job training, job placement services and opportunities, child care services, children's health services, and extensive supportive services to preserve and strengthen eligible families, including adults and children, to help them achieve personal and economic self-sufficiency.

Other units

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

The State Commission on the Status of Women acts as the coordinating body for governmental and non-governmental activities and information relating to the status of women.

The Office of Youth Services offers a continuum of prevention, rehabilitation, and treatment services and programs for youth at risk to prevent delinquency among juveniles.

The Hawaii Housing Authority administers and manages federal and state housing projects and rent subsidy programs.

Scope and Methodology

We audited the financial records and transactions and reviewed the related systems of accounting and internal controls of the Department of Human Services for the fiscal year July 1, 1992 to June 30, 1993. Included in our audit were all fund types and account groups except: (1) the operations of the Hawaii Housing Authority, which were audited by other auditors whose reports were furnished to us, and (2) the general fixed assets account group. We also reviewed those transactions, systems, and procedures for compliance with applicable laws and regulations.

The audit included a review of the accounting, reporting, and internal control structures to identify deficiencies and weaknesses and to make appropriate recommendations for improvement. It also reviewed forms, records, accounting, and operational procedures.

The independent auditors' opinion as to the fairness of the combined financial statements presented in Chapter 3 is that of KPMG Peat Marwick. The audit was conducted from May 1993 through December 1993 in accordance with generally accepted government auditing standards.

Chapter 2
Internal Control Practices

This chapter presents our findings and recommendations on the financial accounting and internal control practices and procedures of the Department of Human Services (DHS).

Summary of Findings

1. We found significant deficiencies in DHS's financial accounting and internal control practices and procedures that resulted in seven reportable conditions. These findings are summarized below:

    a. DHS has repeatedly and deliberately circumvented state laws and fiscal controls by improperly charging expenditures of certain programs to appropriations for other programs in order to cover cash shortages. The department does not know the exact amount improperly charged because it kept no records. In addition, DHS has violated federal laws by transferring federal funds from one program to another. These matters are of such magnitude as to be classified as material weaknesses. They also constitute material noncompliance with laws and regulations.

    b. DHS did not lapse federal reimbursements into the State's general fund as required by law. Instead, it used a portion of these funds to finance program expenditures that had not been authorized by the Legislature. We consider this a material noncompliance with laws and regulations.

    c. The department's inability to track and recover welfare overpayments is appalling.

    d. DHS has been remiss in claiming federal reimbursements.

    e. For the past eleven months of FY1992-93, DHS did not perform bank reconciliations for 56 bank accounts held outside the state treasury. In addition, these accounts were not replenished on a timely basis as required by law.

    f. DHS has inappropriately encumbered funds without valid supporting purchase orders or contracts. In addition, "old" encumbrances and encumbrances that are no longer necessary continue to remain on the State's financial records.

    g. DHS is not performing federally required contractor performance reviews on a timely basis.

2. In addition to the reportable conditions described above, we found problems in the Medicaid budget, in the controls over income maintenance programs and computer data, and in several other aspects of the internal control structure and its operation.

Reportable Conditions Reflect Serious Deficiencies

The magnitude of the deficiencies we found reflects an overall failure of stewardship by DHS management. The financial operations of the department have not been administered in a responsible manner. DHS received over $778 million in FY1992-93 for a wide variety of assistance and social services programs. The director of human services must assume an active role in developing policies and directing the department's financial management to ensure that it faithfully carries out its many obligations. To correct the many problems we found will demand a concerted effort at the very top levels of the department and state government.

We noted seven reportable conditions, including one reportable condition which we believe to be a material weakness in the internal control structure. We also noted three instances of material non-compliance with laws and regulations. Reportable conditions must be taken seriously. Our experience is that this number of reportable conditions is found infrequently in Hawaii's government agencies today. Material weaknesses are rare.

Reportable conditions are significant deficiencies in the design or operation of an organization's internal control structure that could adversely affect its ability to record, process, summarize, and report financial data consistent with the assertions of management in the combined financial statements.

A material weakness in the internal control structure is the worst possible reportable condition. A material weakness exists when internal controls are such that significant errors or irregularities may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. In other words, illegal acts such as thefts could go undetected.

Non-compliance with federal laws and regulations may jeopardize future federal funding for essential programs and services. Non-compliance with state laws and regulations suggests that legislative controls are being circumvented or legislative intent is not being carried out.

In the following sections, we discuss the seven reportable conditions at DHS.

DHS Has Mischarged Program Expenditures

DHS has repeatedly circumvented state laws and fiscal controls by improperly and deliberately charging expenditures of certain programs to appropriations meant for other programs. We consider this to be a material noncompliance with laws and regulations.

Chapter 37, Part II, HRS, on the State's budget establishes an allotment system. The allotment system governs all agency expenditures and is intended to ensure that departments plan for program expenditures in correct amounts from appropriations designated for those programs. The law provides that no department may expend any sum for any purpose not specifically authorized by the Legislature and not made available pursuant to the allotment system. All allotments must be approved by the director of finance and no department may expend or incur any sum in excess of an allotment. Allotments are made according to classifications of expenditures in the appropriation measures and must be expended according to these classifications.

DHS has not complied with state budget laws. Throughout FY1992-93, it faced the dilemma of not being able to pay benefits to welfare and social service recipients because of cash shortages in several program appropriations. The department's solution was to cover the cash shortages by routinely charging expenditures for welfare/social service programs with insufficient funds to welfare/social service programs with available funds.

No records of mischarges kept

To compound the problem, DHS did not always reimburse the program appropriation that it had improperly charged when it later received additional funds. It did not know how much to reimburse.

DHS kept no records or schedules to indicate the date, amount, and the appropriation improperly charged or the date and amount of reimbursements it had made. We noted instances where appropriations were reimbursed twice or not fully reimbursed. Further, because it lacked records, DHS does not know how many wrong charges were made to appropriations or how much they amounted to. Since the extent and exact amount of improper charges during FY1992-93 cannot be determined, our certified public accountants have stated an exception to the fairness of the combined financial statements because they were unable to determine if expenditures are properly reported.

DHS personnel estimate that at least $23.3 million in expenditures were charged to wrong appropriations in FY1992-93. They estimate that approximately $10.9 million was expended for the Individual and Family Grant (resulting from Hurricane Iniki), $3.5 million for the Child Foster Care Services program, and $3.7 million for the Aid to Families with Dependent Children (AFDC) program. DHS acknowledges that expenditures were charged to wrong appropriations in many other instances; however, it could not determine the exact amounts.

In addition, we noted two instances where DHS violated federal financial assistance requirements by transferring approximately $3.3 million of federal funds from the Medicaid program to cover cash shortages in the AFDC program.

Mischarges have many causes

The department's cash shortages can be attributed to shortfalls in the budgeting and accounting process and to procedures not being performed on a timely basis. Specifically, we found that:

1. The DHS biennium budget request was not sufficient to cover program expenditures. Even though the Legislature appropriated supplemental and emergency funds aggregating approximately $101 million in FY1992-93, DHS still experienced periodic cash shortages.

2. DHS personnel did not take steps to avoid shortages. Accounting office staff did not attend all meetings scheduled to discuss the financial status of programs. They were not at these meetings to present data necessary to identify potential cash shortages and determine what could be done to prevent them.

3. DHS could make weekly "drawdowns" on federal letters of credit for reimbursements from the federal government. Because DHS staff did not perform drawdowns on a timely basis, they had to find other sources of funds to make payments. Program expenditures are initially paid from the general fund and then are reimbursed by the federal government for its share of the program expenditures. DHS requests reimbursements for eligible program expenditures by preparing drawdowns on a letter of credit established by the federal government. The federal government bases the amount of the letter of credit primarily on actual expenditures incurred during the previous quarter. Once the drawdowns are made, DHS records federal reimbursements in its special revenue funds and transfers these moneys from the special funds to reimburse the general fund.

4. DHS does not adequately monitor the status of federal grant awards. We noted it does not maintain an updated schedule of its federal grants and grant activities and often does not know what federal funds are available. It also does not maintain a schedule of all claims for federal grant reimbursements and actual cash receipts. In addition, DHS does not always deposit federal reimbursements on a timely basis because DHS staff either did not anticipate federal receipts or could not match receipts to the proper federal program.

As a control, the department should have a schedule to reconcile any federal grant funds received to this schedule to ensure that all funds have been received and deposited in a timely manner.

5. DHS delayed processing claims for federal reimbursements for Hurricane Iniki expenditures even though its accounting office had the necessary documentation. Consequently, the department had to charge the expenditures improperly to another program because reimbursements were not received until several months after state funds had been expended.

These irregularities occurred because DHS management overrode the internal controls that were in place. Pre-audit staff of the Department of Accounting and General Services (DAGS) review all expenditures for availability of funds. DAGS will not process expenditures when appropriations lack sufficient funds to pay for them. DHS also has staff with a similar pre-audit function. However, whenever DHS found that expenditures would exceed available funds, authorized individuals of the department would approve changing the appropriation codes for these expenditures to charge them to appropriations with available funds. The "revised" authorized expenditures were then forwarded to DAGS pre-audit for processing.

Governor's warning goes unheeded

This practice did not go unnoticed. In a letter dated June 30, 1993, Governor John Waihee wrote to the director of human services about improperly charging appropriations, stating:

> It also has come to my attention that the shortfall in the HMS 303 program has been in existence for some time and that your department has been charging different program accounts to fund the foster care expenditures. In the future, please ensure that proper budgeting and accounting procedures are followed so that the random charging of accounts to cover shortfalls in programs does not occur. This practice is not only inappropriate but it also circumvents established fiscal controls and makes subsequent review of your request to release restrictions confusing and futile.

Despite the governor's warning and our discussions with DHS, it continues the practice of improperly charging appropriations meant for other programs. The governor, the Department of Budget and Finance (B&F), and DAGS all share responsibility for correcting this problem. They should ensure adherence to state budgeting and accounting requirements. They should require DHS to halt its practice of mischarging appropriations immediately. DHS should pay more attention to forecasting its cash flow requirements by making sure all appropriate staff are involved and made aware of all pertinent data. In addition, DHS should revise its quarterly allotment and budget requests to realistically reflect its needs.

DHS should maximize the availability of federal reimbursement by requesting drawdowns on the federal letter of credit on a timely basis. Further, it should maintain a listing of all federal grants together with copies of the grant award letters so that it can monitor federal grant activities.

DHS Expended Federal Reimbursements Without Authorization

DHS has failed to lapse federal reimbursements to the State's general fund as it should. Instead, it has used at least $20 million in federal reimbursements to finance program expenditures in excess of legislative appropriations. This has masked the full cost of programs from legislative review and authorization.

Social services and welfare programs receive both state and federal funds. At the end of the fiscal year, the federal share of expenditures made through the general fund is compared against the actual funds received from the federal government—any difference is either requested from or returned to the federal government. When federal funds are received in the following fiscal year, the funds should lapse to the State's general fund. For the past three fiscal years, DHS has failed to lapse these funds to the State's general fund on a timely basis. Instead, it has improperly used federal reimbursements to finance current program expenditures not authorized by the Legislature.

At June 30, 1993, DHS should have lapsed approximately $34.5 million of federal reimbursements to the general fund. The $34.5 million consisted of $22.5 million from FY1991-92 and $12 million from FY1990-91 and earlier. DHS should be lapsing these reimbursements to the State's general fund as they are received.

Instead, the department improperly accounted for the federal reimbursements as reductions of expenditures instead of reimbursements due to the State's general fund. This violates state laws on the budget and the lapsing of appropriations. These laws require DHS to lapse the funds and then seek additional appropriations from the Legislature. DHS should immediately halt its practice of using federal reimbursements to finance program expenditures that have not been authorized by the Legislature.

DHS Has No Effective System for Controlling Welfare Overpayments

Welfare overpayments are a cause of public concern. Recovery efforts should be appropriate, swift, and effective. DHS lacks, however, a cohesive, systematic, and effective overpayment recovery system. It has no idea of the total amount of welfare overpayments owed the State. Collection efforts are fragmented and not prioritized. DHS's lack of a system to manage welfare overpayments is appalling.

In the past fiscal year alone, DHS identified more than 7,300 overpayments. Overpayments are generally discovered when eligibility workers do case reviews and check benefits against such information as income levels, changes in dependents, or changes in addresses. The DHS Investigations Office also receives calls or anonymous calls are received on the "fraud hotline."

Once discovered, DHS determines the amount of overpayment and informs recipients that the State will seek recovery. DHS has two systems for recording overpayments—the Hawaii Automated Welfare Information (HAWI) system and the Accounts Recovery System (ARS). The HAWI system is used if the recovery is from someone currently receiving benefits. DHS works out a payment schedule and deducts the payments from future benefit payments processed through its on-line HAWI system. Sometimes DHS works out a payment schedule and bills the recipient using its ARS. DHS sometimes also seeks recovery by attaching income tax refunds or by filing lawsuits. In all cases, the amounts to be recovered are recorded in ARS. Subsequent receipts are recorded in HAWI or ARS as appropriate.

The problem is that ARS only prints individual bills. It has no capability to compile, total, or even print out a list of all known overpayments. During the past fiscal year, DHS attempted to recover almost 12,000 overpayments through the tax refund attachment process. The 12,000 overpayments totalled about $18.2 million. This is only a portion of the identified overpayments entered into the ARS. DHS has absolutely no idea of the magnitude, composition, or age of outstanding overpayments that have been identified and entered into the system.

Warnings to recover payments are ignored

Since 1990, those auditing DHS have not been able to determine the amounts due the State. Outside auditors have pointed out this problem to DHS in audit reports for the years ending June 30, 1990, 1991, and 1992. It is appalling that DHS has ignored this problem and has made no improvements, particularly in light of the number of times auditors have seen fit to note this in their audit reports.

DHS should be able to quantify, manage, and track the status of overpayments once they are identified and entered into the system. Without knowing the magnitude, composition, or age of outstanding overpayments, management is severely hampered in its ability to prioritize collection efforts or even determine the effectiveness of its collection efforts. DHS should identify the type of information it needs to develop a system to properly record and process overpayments and then take steps to implement such a system.

DHS Is Remiss In Claiming Federal Reimbursements

Since DHS experiences continual cash shortages, it should be alert to maximizing federal reimbursements. Limited resources have caused a reduction in its services. This became especially evident recently when DHS could not provide child care assistance for over 600 children of low-income families due to a lack of federal funding. We found that DHS had not maximized federal funding available for child care programs due to errors and delays.

Errors in coding have led to the loss of federal funds. DHS receives federal grant awards under Title IV-A of the Social Security Act for child care social service programs. We found that child care costs eligible for 50 percent federal reimbursement were being coded as expenditures under the Job Opportunities and Basic Skills (JOBS) program. The JOBS program receives no federal reimbursement and approximately $109,000 of federal reimbursements were lost in the last nine months of the year because of the way the costs were coded. No figures were available for the first three months of the year. In addition, DHS did not claim any federal reimbursement for eligible child care program expenditures in FY1990-91 and FY1991-92. DHS should emphasize to its personnel the importance of coding expenditures properly and, if necessary, establish additional cost center codes to facilitate proper classification of expenditures.

A delay in processing a grant request with the Office of the Governor also resulted in a delay of federal reimbursement of $1,151,636 under a child care development grant. DHS had to wait until FY1993-94 for the reimbursement. The federal funds could have been received earlier if the grant request had been expeditiously processed.

DHS should establish procedures to identify all program expenditures eligible for federal reimbursement and submit claims that would maximize federal grant awards. In addition, DHS should monitor federal grants to ensure that funds are maximized and received on a timely basis.

DHS Does not Reconcile or Replenish Bank Accounts As Needed

DHS maintains 56 welfare imprest bank accounts totalling $311,050 outside the state treasury. These accounts are maintained at various locations throughout the State and used primarily for emergency financial assistance to welfare recipients.

As of July 15, 1993, the department had not reconciled these bank accounts for about a year—since August 1992. DHS said that this was due to staff vacancies within the accounting office. Without a reconciliation of its bank accounts, DHS cannot determine whether (1) all deposits have been properly recorded, (2) checks issued have been properly cashed, or (3) there are any unusual or erroneous charges to the bank accounts.

Section 40-85, HRS states that: "The welfare imprest fund shall be replenished at the end of each quarter and may be replenished at other times as required by the usage of the fund." Our audit revealed that these bank accounts were either not replenished during the past 12 months or not replenished on a timely basis. DHS should perform bank reconciliations for all bank accounts on a monthly basis. We also recommend that these bank accounts be replenished as required by statute.

DHS Uses Questionable Encumbrances to Avoid Lapsing

Through questionable encumbrances, DHS has avoided complying with state lapsing requirements. Appropriations lapse to the State's general fund unless they are expended or encumbered. Section 40-66, HRS, states that: "Unless otherwise provided by law all sums of money which are appropriated to the public service for any fiscal period and which are not expended during the period, shall lapse ... unless a contract of engagement has been made and entered into ... and a certified copy of which contract or engagement has been deposited with the comptroller."

At June 30, 1993, DHS had encumbered appropriations with purchase orders that were not supported by executed contracts or binding purchase commitments. DHS used these purchase orders to encumber appropriations for services to be provided in the following fiscal year. We also noted that DHS did not monitor encumbrances for continued validity or lapse them when appropriate. Specifically, we found:

1. The department twice encumbered $1 million for services to be rendered under a Memorandum of Understanding with the U.S. General Services Administration for technical assistance to enhance the Child Protective Services System. It encumbered the first $1 million on June 12, 1992. On June 30, 1993, it encumbered another $1 million for the same services because it did not realize the first encumbrance had not expired. We were informed that DHS will be canceling the second $1 million encumbrance in FY1993-94. Although DHS encumbered the funds more than a year ago, it has yet to expend any money against the encumbrance.

2. DHS encumbered $200,000 from FY1992-93 appropriations under an Agreement For Consultant Services contract for transportation services for participants in the JOBS program. The contract was dated July 1, 1993, with services to be provided for the period July 1, 1993 to June 30, 1994. The department also encumbered

another $119,040 from FY1992-93 appropriations under an Agreement For Consultant Services contract for transportation for Maui Participants in the JOBS program. The contract was dated July 1, 1993, with services to be provided from July 1, 1993 to June 30, 1995. These services for day-to-day program operations should be charged to FY1993-94 and FY1994-95 appropriations.

3. Four purchase orders totalling $1,714,508 were used to encumber funds without a binding purchase commitment. Of these, two totalling $297,658 were processed solely to prevent appropriations from lapsing to the State's general fund.

4. An undated purchase order for $55,146 was used to encumber funds at June 30, 1993. The supporting documentation was merely two "Non-Budgeted Computer Hardware or Software Requests" that were either missing the necessary approvals or had approvals that were dated in August or September of 1993.

5. At June 30, 1993, we found to be still outstanding 48 encumbrances of general fund appropriations totalling $215,788 that had originated prior to July 1, 1991 and dated back to 1983. We also noted as still outstanding 3 encumbrances of special revenue fund appropriations totalling $130,896 that had originated prior to July 1, 1991 and dated back to 1988. We question the need for these encumbrances.

DHS should review its encumbrance policies to ensure that all encumbrances are supported by executed contracts or binding purchase commitments. It should also monitor outstanding encumbrances. In particular, DHS should evaluate longstanding encumbrances to determine if they should be lapsed.

DHS Reviews of Subrecipients Have Not Been Timely

DHS has not yet completed the reviews of subrecipients required by the federal government. DHS contracts with various agencies to provide services under federal Title XX Block Grant and Vocational Rehabilitation funds. The contracting agencies are commonly referred to as subrecipients of federal funds. Federal regulations require program reviews of these subrecipients on a timely basis and corrective action plans to be developed for any findings contained in any audit reports on the subrecipients.

DHS has yet to complete the program reviews for fiscal years ended 1990, 1991, and 1992—primarily because it has not received the federally required audit reports from the subrecipients. Further, DHS does not investigate the status or development of required corrective action plans. DHS's failure to comply with federal guidelines may jeopardize the receipt of future federal funds for these programs. DHS should require subrecipients to submit the required audit reports and corrective action plans and complete its subrecipient reviews on a timely basis.

Weaknesses in Internal Controls Are Found In Many Other Areas

In addition to the reportable conditions described above, we noted several other weaknesses involving DHS's internal controls and its operations which are summarized as follows:

1. Medicaid budget requests do not reflect all projected program costs.

2. Controls over income maintenance programs could be improved, specifically:

    a. Data entered into the HAWI system are not checked for errors;

    b. The level of documentation maintained in case folders is not standardized and does not always provide for a proper review for compliance with program eligibility requirements;

    c. The income verification process is inefficient and not consistently followed; and

    d. Verification of the residential address of welfare recipients and their dependents is not performed.

3. Computer controls relating to security and program changes to data files have not been implemented and certain computer equipment is significantly under-utilized.

4. The cost allocation process is inefficient and susceptible to error.

5. Payments for real property leases may not be proper.

6. DHS needs to identify and correct problems relating to vacant positions.

7. DHS could put its Evaluation Office to better use to improve program operations, financial management, and internal controls.

Medicaid Budget Requests Do Not Reflect Program Costs

The State shares the costs of its Medicaid program with the federal government on an approximately 50/50 basis. The DHS Health Care Administration Division (HCAD) is responsible for budgeting for the

Medicaid program and for providing necessary information to the Legislature as part of the biennium budget process.

Prior to the fiscal biennium 1993-95, the budget request was based primarily on actual program expenditures of the preceding year. HCAD did not consider the increasing costs of health care and changing health care utilization patterns in the budgeting process. Although HCAD was aware of the shortcomings of this budgeting process, B&F instructed DHS to prepare its budget proposal based on "zero growth."

Table 2.1 compares state appropriations for the Medicaid program (based on HCAD's budget requests) with the actual program expenditures for fiscal years 1990-91, 1991-92, and 1992-93. Medicaid program expenditures have exceeded state appropriations based on HCAD's base budget requests by increasingly larger amounts—from $3.2 million in FY1990-91 to $79 million for FY1992-93. The dramatic increases were largely due to the increased cost of basic health care and the increase in the number of claims paid. In each case, the Legislature had to make emergency or supplemental appropriations.

Table 2.1
Medicaid Budget Requests and Expenditures

FY1990-91	
Base budget request (Act 299, SLH 1990)	$ 128,469,755
Inter-program transfer	3,243,229
Total appropriations	$ 131,712,984
Total expenditures	$ 131,712,967
FY1991-92	
Base budget request (Act 296,SLH 1991)	$ 130,295,542
Emergency funding request (Act 2,SLH 1992)	64,000,000
Total appropriations	$ 194,295,542
Total expenditures	$ 187,968,734
FY1992-93	
Base budget request (Act 296, SLH 1991)	$ 130,608,048
Supplemental request (Act 300, SLH 1992)	44,000,000
Emergency funding request (Act 4, SLH 1993)	35,250,924
Total appropriations	$ 209,858,972
Total expenditures	$ 208,357,309

In 1992, DHS projected that an additional $137 million would be needed for the Medicaid budget for the 1993-95 biennium. However, its budget request still followed B&F guidelines for zero growth. So DHS requested only $174.6 million of the Legislature. This was equivalent to the FY1992-93 general and supplemental appropriations of $130.6 million and $44.0 million, respectively and exclusive of the emergency funding of $35 million sought in 1993. The zero growth budgets were in response to B&F's general guidelines which said:

> Total general fund departmental budget requests for each fiscal year of FB1993-1995 shall be the total allocation ceiling amounts approved for departments in FY 1993.
>
> Any departmental operating submission for either FY 1994 or 1995 which is in excess of the allocated funding level shall be returned without action.

These statements run counter to Section 37-64(4), HRS, which states one of the governing principles of the State's budgeting system is that: "The full cost...shall be identified for all programs," and that these costs: "shall be displayed in the year of their anticipated expenditure regardless of whether such costs...require new appropriations."

For the FB1993-95, HCAD had developed projections that showed that program needs would exceed the zero growth budgets by approximately $55 million in FY1993-94 and $81 million in FY1994-95. Table 2.2 compares the DHS Medicaid budget request to its own projected expenditures for the same periods.

Table 2.2
Comparison of Medicaid Budget Request to Projected Expenditures

	Base Budget	Projected Expenditures	Expected Deficit
FY1993-94	$ 174,608,048	$ 229,875,562	$ 55,267,514
FY1994-95	$ 174,608,048	$ 256,415,358	$ 81,807,310

These estimates could have been included in its budget request to B&F and in the executive budget presented to the Legislature prior to the start of the 1993 legislative session. Instead, the request to fund the projected deficit was included in the *Governor's Message* delivered to the Legislature after the legislative session had begun.

This reduced the time available to the Legislature to review and analyze the needed budget for this program. The DHS budget request submitted to B&F should have included all projected program costs so that the Legislature had an accurate executive budget request to consider.

Certain Internal Controls For Income Maintenance Programs Are Poor

DHS needs better controls over its four largest income maintenance programs—Medicaid, AFDC, General Assistance (GA), and Food Stamps. Table 2.3 illustrates the substantial caseload and expenditures for each program for the month of June, 1993.

Table 2.3
Program Caseload and Expenditures
June 1993

Program	Number of Cases	Expenditures
Medicaid	27,118	$ 33,347,359
AFDC	18,431	11,895,929
GA	5,737	2,393,890
Food Stamps	37,342	9,377,088

The DHS Family and Adult Services Division (FASD) is responsible for administering these programs. The application and reapplication reviews, face-to-face interviews and verification process are conducted by approximately 375 eligibility workers located at 39 units throughout the State.

We found weaknesses in the following areas:

- data entry that is not checked for accuracy;
- failure to standardize documentation requirements;
- inefficient income verification;
- failure to follow federal reporting requirements; and
- failure to verify residency.

By way of introduction, we describe the case handling process. Once the application is verified, eligibility workers input the information on-line into the HAWI system. The workers determine applicants' eligibility for various types of financial assistance and the amount of assistance to be provided. Once entered into the system, HAWI automatically generates warrants for disbursements to participants in the AFDC and GA programs and Authorization to Participate (ATP) cards for the Food Stamps program each month. HMSA, the State's fiscal agent for Medicaid claims processing, generates Medicaid identification cards each month through its Medical Management Information System (MMIS). The HAWI system updates eligibility information on the MMIS using magnetic tapes.

As a condition of continued assistance, recipients are generally required to submit Monthly Eligibility Report Forms (MERFs), showing income and household information. In addition, they must reapply annually for assistance.

The State maintains a data base, the Income and Eligibility Verification System (IEVS). The system generates 4 IEVS reports to assist eligibility workers in verifying income:

- State Wage Information and Collections Agency (SWICA) - Quarterly
- Unemployment Compensation (UC) - Monthly
- Beneficiary Earning Exchange Records (BEER) - Monthly
- Internal Revenue Service (IRS) - Quarterly

Upon receipt of the IEVS reports, the workers must manually verify the income reported by welfare recipients against the reports. The workers maintain case folders for all welfare recipients. In some cases it is required, in others it is recommended, that all pertinent documents, including applications, copies of verification documents, correspondence, HAWI printouts, and MERFs be maintained in case folders. The IEVS reports, however, are not maintained in the case folders for reasons of confidentiality.

Data entry not checked for errors

Eligibility workers enter information on welfare recipients on-line into the HAWI system after obtaining and verifying the information. Inaccurate information entered into the HAWI system has resulted in overpayments. Someone other than the eligibility worker should review the data entered to ensure completeness and accuracy.

When the eligibility worker has completed entering data, HAWI prints a "budget" screen. This printout summarizes significant information entered into the system. Key data entered into the HAWI system—for both new applications and for updated information for ongoing cases—is not checked for accuracy. Given the on-line nature of the HAWI system, an accuracy check should be made within a day of entering information into the HAWI system, and the check should be documented by the reviewer's signature on the "budget" screen printout in the case folder.

DHS informed us that effective June 1993, a supervisory review is being performed for all cases handled by new employees. A limited review of one case per month will be made for other eligibility workers. The review process will ensure that eligibility information in the HAWI system has been correctly obtained, verified, and properly entered.

Documentation is not standardized

Eligibility workers are required to obtain certain kinds of documentation to verify that recipients meet eligibility requirements. We found that the case folders did not contain copies of all documents needed to show compliance with eligibility requirements. Federal and state program guidelines require welfare recipients to meet general eligibility requirements relating to age, citizenship, social security number, and residency. We reviewed a sample of 72 case folders (for the Medicaid, AFDC, GA and Food Stamps programs) and noted the following missing documents:

- 18 had no documents to show the recipient's proof of citizenship.
- 10 had no copies of the recipient's social security card.
- 7 had no documents certifying residency in the State of Hawaii.
- 6 had no documents certifying the applicant's age.

DHS should ensure that all files contain the documentation needed. It should identify the standard documents needed and develop a checklist to ensure completeness of file documentation. Eligibility workers should complete and sign the checklist for each case file.

Residency is not verified

To be eligible, welfare recipients and their dependents must reside in the same household. Any difference between the number of residents reported and the number actually residing in the home requires an adjustment to benefit payments. DHS does not verify that recipients and dependents reside in the same household.

Welfare recipients are required to provide a residency address that must be a street address. DHS does not match the address of the welfare recipient with that of dependent. Consequently, a discrepancy in the actual versus reported number of household members is generally found only from unsolicited reports of such discrepancies from other individuals. Matching reported addresses to other available records should be a standard verification process.

Income verification process is inefficient

DHS generates four IEVS reports by recipients' names and by eligibility worker. As noted earlier, the data are from the State Wage Information and Collections Agency (SWICA), Unemployment Compensation (UC), Beneficiary Earning Exchange Records (BEER), and Internal Revenue Service (IRS).

Eligibility workers have case folders organized by case numbers. Each case may have several names. This means that eligibility workers must first match the names on each of the four IEVS reports with a specific case folder. This time-consuming procedure must be performed for each IEVS report. If the case number and the amount of income per income verification source (e.g. SWICA, UC, BEER, IRS) were available on one form, eligibility workers could verify income eligibility much more efficiently. We believe that this can be programmed without too much difficulty. DHS should combine the IEVS reports into a single report and include the case number and the amount of income per income verification source.

Status of income verification is not reported

The federal government requires public assistance agencies to make more accurate eligibility determinations and benefit payments by exchanging information and by obtaining data on unearned income from the Internal Revenue Service (IRS), other income and wage data from the Social Security Administration (SSA,) and from state wage (SWICA) data files and unemployment insurance benefit (UIB) data files. To accomplish this, the DHS Program Development-Income Maintenance office requires each welfare unit to report the status of the income verification process on an IEVS Report Form (DHS 1472). The form was designed to meet federal mandates. It is a single reporting record for actions taken as a result of matches made by the IEVS system with the IRS, SSA, SWICA, and UIB files.

Eligibility workers are supposed to submit the DHS 1472 form to the Program Development-Income Maintenance office on a quarterly basis for SWICA reviews and on a monthly basis for UIB reviews. In addition, workers are required to submit a monthly report for SWICA and UIB reviews performed on-line for new applicants. We found that the welfare units do not always submit the DHS 1472 form and do not always complete the form properly. Failure to follow federal procedures may jeopardize future federal support for programs. To comply with federal regulations, welfare units should complete and submit the DHS 1472 forms properly.

Some Controls Over Electronic Data Processing Are Poor

DHS is not implementing appropriate controls over its HAWI system. The system is currently running on a mainframe computer located at the state data center in the basement of the Kalanimoku building. The HAWI system consists of 2,400 programs written in various programming languages. Certain internal security products have been installed on the HAWI system, but they have not been implemented. These security products would limit access based on user IDs and passwords and allow access to be monitored on-line.

DHS also has a Protection Log Extract Utility (PLEU), that tracks all programs that interact with database files. The PLEU generates a log that gives a before/after picture of the program changes that have modified the data files. DHS does not review the log on a regular basis.

Therefore, improprieties stemming from application modifications could possibly occur and not be detected, verified, or responded to on a timely basis.

$199,000 mini-computer is under-utilized

DHS purchased a mini-computer in 1990 for approximately $117,000 and recently upgraded it at an added cost of $82,000. DHS acquired the new computer to assume certain data processing responsibilities including its ARS billings for welfare overpayments. The new computer is used primarily as storage space for the ARS data files and is very much under-utilized.

An older computer that is still being used to run the ARS is running at capacity and lacks many capabilities of the new computer. Properly programmed, the new computer could enhance DHS's ability to track and recover welfare overpayments.

DHS should fully implement the security products in the HAWI system. In addition, it should regularly review the protection log. DHS should also make better utilization of the mini-computer.

Cost Allocation Process Is Inefficient

DHS allocates indirect costs to the various welfare assistance programs through a cost allocation process that has been approved by the federal government. The DHS allocation process is prone to error and time consuming.

DHS uses individual electronic spreadsheets in its quarterly cost allocation process. These spreadsheets are not fully integrated with one another and require significant manual intervention and redundant data input. We found mathematical errors, as well as errors in transferring numbers from one cost allocation schedule to another. In addition, we found that the accounting office incurs a significant amount of overtime to prepare the reports in time for federal reporting deadlines. Because of the time required to complete the cost allocation process and the tight deadlines for submitting federal reimbursement requests, the schedules are not subject to any supervisory review.

DHS should consider implementing an integrated software package to prepare the cost allocations. Such a package could improve the efficiency of the cost allocation process, minimize errors, and reduce the cost of overtime hours. It would also allow time for proper supervisory reviews of the cost allocation data.

DHS Does Not Know Proper Rents for Office Leases

As of June 30, 1993, DHS had approximately 86 real property leases of which the annual federal share was approximately $2.6 million. The department does not maintain an updated schedule of all executed real property leases. Consequently, the department is unable to determine whether charges for lease expenses are proper.

DAGS pays all real property lease expenses for DHS and charges DHS for the federal share of such expenses. Any lease expenses not budgeted by DAGS prior to the fiscal year are charged directly by the lessor to DHS. DHS simply pays the bills. Certain lease payments are being disputed by the department. It claims that DAGS should be making the payments because DHS had the appropriation for these expenses transferred to DAGS. DHS should maintain an updated schedule of all executed real property leases that it can match to real property lease expenses before it processes payment. It should also coordinate its leasing efforts with DAGS so that it is clear which agency is responsible for making the lease payments.

DHS Has High Staff Vacancy Rate

During the year, DHS had an average staff vacancy rate of approximately 12.7 percent. Table 2.4 shows the extent of vacant positions at June 30, 1993.

Table 2.4
Extent of Vacant Positions
June 30, 1993

Position	Total Positions	Total Vacancies	Vacancy Percentage
Employment Services Specialist	70	24	34.29
Social Worker	402	73	18.16
Social Services Assistant	174	24	13.79
Clerk, Clerk Steno, Clerk Typist	321	44	13.71
Account Clerk and Accountant	46	6	13.04
Vocational Rehab. Specialist	75	9	12.00
Income Maintenance Worker	503	38	7.55

DHS repeatedly cites "lack of personnel" as contributing to the problems we noted. Lack of staffing, however, does not relieve DHS of its fiscal and legal responsibilities. It does, however, require management's attention. DHS needs to identify the causes of chronic staffing shortages and take actions to resolve the problem.

In a department of this size, and a problem of this magnitude, DHS should seek assistance from other state agencies. The Departments of Labor and Industrial Relations, Budget and Finance, and Personnel Services may be able to help identify sources of workers, assist with department budgeting needs, and assist with the proper classification and recruitment of personnel.

In our Report No. 90-12, *Study of the Social Worker Shortage Among State Agencies*, the director of human services responded to our recommendation that agencies work together to solve the shortage of social workers in state government by stating: "We particularly agree that state agencies need to coordinate their efforts in seeking solutions and in developing strategies to address the current shortage of social workers." We encourage DHS to continue to work more vigorously with other departments and agencies to deal with its current staffing problems.

Evaluation Office Is Not Fully Utilized

The DHS Evaluation Office (EVO) consists of program and management evaluation, financial evaluation, and quality control staff. The office reports directly to the director of the department. The functional statements of EVO state that:

> The primary function of this office is to strengthen the department's program evaluation and assessment capabilities so that the department can make rational decisions with respect to implementing public programs; setting program levels; and using human resources, materials, and equipment more effectively.
>
> The program and management evaluation staff conducts in-depth analysis and evaluation of the department's programs and operations; and provides consultation and technical management services relating to organization, procedures, work methods, and resource utilization. The financial evaluation staff is responsible for the examination of financial transactions, records, and statements of the department and entities doing business with the department to attest to and insure their legality, accuracy and reliability. This staff also reviews internal control systems of the department to ensure that such systems are properly designed to safeguard the department's assets against loss from waste, fraud, error, etc.

Instead of in-depth analysis and evaluation of programs and operations, EVO staff are engaged primarily in preparing organization charts and related functional statements, providing analysis on special projects upon request, conducting inventory counts of food stamps, and receiving financial statements from subrecipients of federal financial assistance.

EVO has not initiated any independent reviews of the major DHS programs such as AFDC, Medicaid, Food Stamps, Vocational Rehabilitation, or Title XX of the Social Security Act. Such performance reviews could provide valuable information to management on the use of resources, program management, and the effectiveness of existing policies and procedures. For example, such reviews could have resulted in improvements to data entered into the HAWI system as well as improvements to the format of the Income and Eligibility Verification System (IEVS) reports. These reviews could also have detected that federal grants are not being fully maximized.

EVO has also not initiated any independent reviews of the department's financial transactions and records. Reviews of fiscal controls could have revealed the weaknesses in internal controls for financial transactions and records. The reviews might have revealed the practice of using funds from one appropriation to pay for expenditures of another and the failure to reconcile and replenish imprest bank accounts on a timely basis.

During our audit, we tested thirteen payroll terminations and noted one instance where an individual was inadvertently paid for one extra pay period. As a result of our testwork, the department initiated collection efforts and was able to recover the majority of the overpayment from the accrued vacation due this individual. An independent review of the internal controls and detailed test of the financial transactions might have uncovered this type of error as well as the existence of other types of errors.

Conclusion

The magnitude of the problems at DHS makes it plain that they cannot be fixed overnight. Effective remedies also would be difficult to make on a piecemeal basis. Change must come from the top under the leadership of the governor, the director of finance, the comptroller, and the director of human services. A coordinated and concerted effort must be mounted to address our findings and implement the necessary corrections. The governor should charge the director of finance, the comptroller, and the director of human services with the responsibility of ensuring that DHS adheres to state budgeting and accounting requirements and federal requirements. The director of human services should task a designated group of DHS staff with the responsibility of identifying and developing the steps needed to strengthen the department's internal financial management. The director should establish a timetable for the task force to report on its progress. The Legislature should also be involved by making sure that DHS reports on what it is doing to correct these deficiencies.

Recommendations

1. We recommend that the governor charge the director of human services, the comptroller, and the director of finance with the responsibility for ensuring that the Department of Human Services adheres to state budgeting and accounting requirements on allotments, charging of appropriations, lapsing, and encumbrances.

2. We recommend that the Department of Human Services:

    a. Cease immediately the mischarging of appropriations;

    b. Lapse federal reimbursements to the State's general fund;

    c. Make timely and accurate claims for federal reimbursements;

    d. Reconcile and replenish bank accounts as required;

    e. Cease making questionable encumbrances;

    f. Perform timely reviews of subrecipients;

    g. Present realistic budgets to the Legislature based on expected costs;

    h. Develop better controls for its income maintenance programs and data processing;

    i. Improve its cost allocation process;

    j. Maintain a schedule of the department's real property leases;

    k. Work with other agencies to reduce vacancies in the department; and

    l. Make better use of staff in its Evaluation Office.

3. We recommend that the director of human services appoint a task force to develop a plan to address deficiencies uncovered in this audit. The plan should set priorities for implementation of corrective measures and timetables for implementation.

4. We also recommend that the Legislature require the director of human services to report on the status of its plan 30 days prior to the adjournment of the 1994 legislative session and to submit a status report 20 days prior to the convening of the Regular Session of 1995.

Chapter 3
Financial Audit

This chapter presents the results of the financial audit of the Department of Human Services as of and for the fiscal year ended June 30, 1993. It includes the independent auditors' report and reports on the internal control structure and tests of compliance with laws and regulations. It also displays financial statements of all fund types and account groups administered by the department, together with explanatory notes.

Summary of Findings

In the opinion of KPMG Peat Marwick, based on their audit, except for the general fixed assets account group and the accounting for certain program expenditures, the combined financial statements present fairly, in all material respects, the financial position of the department as of June 30, 1993, and the results of its operations and the cash flows of its proprietary fund types for the year then ended in conformity with generally accepted accounting principles.

KPMG Peat Marwick noted matters involving the internal control structure and its operation that they considered to be reportable conditions, including a material weakness as defined in the report on the internal control structure. They also noted that, with respect to items tested, except for three material instances of noncompliance as defined in the report on compliance, the department has complied, in all material respects, with laws and regulations applicable to the department.

Independent Auditors' Report

The Auditor
State of Hawaii:

We have audited the following combined financial statements of the State of Hawaii, Department of Human Services (department):

Combined Balance Sheet - All Fund Types and Account Groups, June 30, 1993 (Exhibit A);

Combined Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) - Governmental Fund Types and Fiduciary Fund Type, Year ended June 30, 1993 (Exhibit B);

Combined Statement of Revenues and Expenditures—Budget and Actual (Budgetary Basis) - Governmental Fund Types, Year ended June 30, 1993 (Exhibit C);

Combined Statement of Revenues and Expenses - Proprietary Fund Types, Year ended June 30, 1993 (Exhibit D);

Combined Statement of Fund Equity - Proprietary Fund Types, Year ended June 30, 1993 (Exhibit E); and,

Combined Statement of Cash Flows - Proprietary Fund Types, Year ended June 30, 1993 (Exhibit F).

These combined financial statements are the responsibility of the department's management. Our responsibility is to express an opinion on these combined financial statements based on our audit. We did not audit the financial statements of the Hawaii Housing Authority. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Hawaii Housing Authority, is based solely on the report of the other auditors. The financial position and results of operations of the Hawaii Housing Authority are reported in the governmental, proprietary and fiduciary fund types and account groups in the department's combined financial statements as follows:

	Percent of	
	Assets	**Revenues**
General fund	2.5%	2.2%
Special revenue funds	16.2	4.8
Capital projects, enterprise and internal service funds	100.0	100.0
Trust and agency funds	50.3	68.6
Account groups:		
General fixed assets	67.9	-
General long-term obligations	2.7	-

Except as discussed in the following two paragraphs, we conducted our audit in accordance with generally accepted auditing standards. 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 and the report of other auditors provide a reasonable basis for our opinion.

In accordance with the terms of our engagement, the scope of our audit did not include an audit of the general fixed assets account group. As a result, the balance sheet of the general fixed assets account group is included in the accompanying combined balance sheet of the department for informational purposes only. It has been prepared from the department's fixed asset records without audit and we express no opinion on it.

The department has not maintained adequate records to account for the expenditures of certain programs which were paid with moneys appropriated for other programs. It was not practicable to extend our auditing procedures to sufficiently satisfy ourselves as to the extent of these questionable activities and to determine whether program expenditures recorded in the general and special revenue funds were classified properly. Expenditures of the general and special revenue funds reported in the combined statement of revenues, expenditures and changes in fund balances - governmental fund types and fiduciary fund type amounted to $432,593,581 and $340,057,375, respectively, for the year ended June 30, 1993.

As discussed in Note 1, the combined financial statements of the department are intended to present the combined financial position and combined results of operations and cash flows of proprietary fund types of only that portion of the funds and account groups of the State of Hawaii that is attributable to the transactions of the department.

In our opinion, based upon our audit and the report of other auditors, except for the effects of such adjustments, if any, as might have been determined to be necessary had the scope of our audit included the general fixed assets account group and had we been able to apply adequate procedures to certain program expenditures recorded in the general and special revenue funds, as discussed in the fourth and fifth paragraphs above, the combined financial statements referred to above present fairly, in all material respects, the financial position of the State of Hawaii, Department of Human Services, as of June 30, 1993, and the results of its operations and the cash flows of its proprietary fund types for the year then ended in conformity with generally accepted accounting principles.

As discussed in Note 12, the department is subject to liabilities arising from certain circumstances, including possible charges for medical services provided to Medicaid recipients. The ultimate outcome of these items cannot presently be determined. Accordingly, no provision for any liabilities that may result has been made in the accompanying combined financial statements. In addition, the department failed to comply with certain federal financial assistance requirements for programs that may be material to the special revenue fund type. The combined financial statements do not include an adjustment for any liability that may result from the actions of federal agencies relative to these instances of noncompliance.

Our audit and that of the other auditors were made for the purpose of forming an opinion on the combined financial statements taken as a whole. The combining financial statements (Schedule I through Schedule XI) are presented for purposes of additional analysis and are not a required part of the combined financial statements of the State of Hawaii, Department of Human Services. Such additional information has been subjected to the auditing procedures applied in the audit of the combined financial statements and, in our opinion, except for the effects on the combining financial statements of such adjustments, if any, as might have been determined to be necessary had we been able to audit certain program expenditures as discussed in the fifth paragraph above, is fairly stated in all material respects in relation to the combined financial statements taken as a whole.

/s/KPMG Peat Marwick

Honolulu, Hawaii
November 1, 1993

Independent Auditors' Report on Internal Control Structure Based on an Audit of the Combined Financial Statements Performed in Accordance with Government Auditing Standards

The Auditor
State of Hawaii:

We have audited the combined financial statements, except for the general fixed assets account group and certain program expenditures, of the State of Hawaii, Department of Human Services, as of and for the year ended June 30, 1993, and have issued our report thereon dated November 1, 1993.

We did not audit the financial statements of the department's administratively attached division, the Hawaii Housing Authority. Those financial statements were audited by other auditors, whose reports thereon have been furnished to us.

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 Human Services, for the year ended June 30, 1993, 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 Human Services, 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:

Cycles of the Department's Activities:

- Revenues and cash receipts
- Purchases and cash disbursements
- Payroll
- External financial reporting

Accounting Applications:

- Billings and receivables
- Property and equipment
- Encumbrances
- Interfund transfers

Administration of Federal Awards:

General requirements:

- Cash management
- Allowable costs/cost principles
- Administrative requirements

Special requirements:

- Types of expenditures allowed or not allowed
- Cost allocation
- Monitoring subrecipients
- Special requirements

Claims for advances and reimbursements

Amounts claimed or used for matching

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. We did not evaluate the internal control structure over property and equipment reported in the general fixed assets account group because the scope of our engagement did not include the audit of the general fixed assets account group.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the department's ability to record, process, summarize, and report financial data consistent with the assertions of management in the combined financial statements. The reportable conditions that we noted are described in Chapter 2.

A material weakness is a reportable condition in which the design or operation 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.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe that the reportable condition described in Chapter 2 relating to expenditures of certain programs which were paid with moneys appropriated for other programs is also a material weakness.

We also noted other matters involving the internal control structure and its operation that we have reported to the Auditor, State of Hawaii, and the management of the State of Hawaii, Department of Human Services, which are described in Chapter 2.

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

/s/KPMG Peat Marwick

Honolulu, Hawaii
November 1, 1993

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

The Auditor
State of Hawaii:

We have audited the combined financial statements, except for the general fixed assets account group and certain program expenditures, of the State of Hawaii, Department of Human Services, as of and for the year ended June 30, 1993, and have issued our report thereon dated November 1, 1993.

We did not audit the financial statements of the department's administratively attached division, the Hawaii Housing Authority. Those financial statements were audited by other auditors, whose reports thereon have been furnished to us.

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

Material instances of noncompliance consist of failures to follow requirements, or violations of prohibitions, contained in laws, regulations, contracts, or grants that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the combined financial statements. The results of our tests of compliance disclosed three instances of noncompliance relating to (1) expenditures of certain programs which were paid with moneys appropriated for other programs, (2) transfers of federal funds from one federal financial assistance program to another to cover cash shortages, and (3) program expenditures which were paid with moneys that should have lapsed to the State's general fund, that may be material to the combined financial statements, but for which the ultimate resolution cannot presently be determined. Accordingly, no provision for any liability that may result has been recognized in the State of Hawaii, Department of Human Services' 1993 combined financial statements. Material instances of noncompliance are described in Chapter 2.

We considered these instances of noncompliance in forming our opinion on whether the State of Hawaii, Department of Human Services' 1993 combined financial statements are presented fairly, in all material respects, in conformity with generally accepted accounting principles, and this report does not affect our report dated November 1, 1993, on those combined financial statements.

Except as described above, the results of our tests of compliance indicate that, with respect to the items tested, the State of Hawaii, Department of Human Services, complied, in all material respects, with the provisions referred to in the fourth paragraph of this report; and with respect to items not tested, nothing came to our attention that caused us to believe that the State of Hawaii, Department of Human Services, had not complied, in all material respects, with those provisions.

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

/s/KPMG Peat Marwick

Honolulu, Hawaii
November 1, 1993

Descriptions and Definitions

This section describes the combined 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 combined financial statements audited by KPMG Peat Marwick and schedules, which 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 (deficit) 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 (Deficit) - Governmental Fund Types and Fiduciary Fund Type (Exhibit B). This statement presents revenues, expenditures, and changes in fund balances (deficit) for all governmental and fiduciary fund types used by the department on an aggregate basis. Revenues include state appropriations mandated by the General Appropriations Act of 1991 (Act 296, Sessions Laws of Hawaii 1991), as amended and supplemented by other specific appropriations acts. Revenues also include federal grant revenues.

Combined Statement of Revenues and Expenditures - Budget and Actual (Budgetary Basis) - Governmental Fund Types (Exhibit C). This statement summarizes revenues and expenditures by source and type on the budgetary basis and compares such amounts to the budget as adopted by the State Legislature.

Combined Statement of Revenues and Expenses - Proprietary Fund Types (Exhibit D). This statement summarizes revenues and expenses of the proprietary fund types used by the department on an aggregate basis.

Combined Statement of Fund Equity - Proprietary Fund Types (Exhibit E). This statement summarizes the changes in the fund equity of the proprietary fund types used by the department on an aggregate basis.

Combined Statement of Cash Flows - Proprietary Fund Types (Exhibit F). This statement summarizes cash flows of the proprietary fund types used by the department on an aggregate basis.

Combining Balance Sheet - General Fund (Schedule I). This schedule presents assets, liabilities, and fund balances (deficit) of the general fund of the department.

Combining Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) - General Fund (Schedule II). This schedule presents revenues, expenditures, and fund balances (deficit) of the general fund of the department.

Combining Balance Sheet - Special Revenue Funds (Schedule III). This schedule presents assets, liabilities, and fund balances (deficit) of the special revenue funds of the department.

Combining Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) - Special Revenue Funds (Schedule IV). This schedule presents revenues, expenditures, and fund balances (deficit) of the special revenue funds of the department.

Combining Balance Sheet - Enterprise Funds (Schedule V). This schedule presents assets, liabilities, and fund equity of the enterprise funds of the department.

Combining Statement of Revenues and Expenses - Enterprise Funds (Schedule VI). This schedule presents revenues and expenses of the enterprise funds of the department.

Combining Statement of Fund Equity - Enterprise Funds (Schedule VII). This schedule presents changes in fund equity of the enterprise funds of the department.

Combining Statement of Cash Flows - Enterprise Funds (Schedule VIII). This schedule presents cash flows of the enterprise funds of the department.

Combining Balance Sheet - Trust and Agency Funds (Schedule IX). This schedule presents assets, liabilities, and fund balances of the trust and agency funds of the department.

Combining Statement of Revenues, Expenditures and Changes in Fund Balances - Trust Funds (Schedule X). This schedule presents revenues, expenditures, and fund balances of the trust and agency funds of the department.

Combining Statement of Changes in Assets and Liabilities - Agency Funds (Schedule XI). This schedule presents changes in assets and liabilities of the agency funds of the department.

Definition of terms

Technical terms are used in the combined financial statements and in the notes to the combined 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.

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 included in the scope of the audit are discussed in this section.

Note 1 - Financial reporting entity

For financial reporting purposes, the State of Hawaii, Department of Human Services (department), includes all funds and account groups that are controlled by or dependent on the department. Control by or dependence on the department was determined on the basis of statutory authority and moneys flowing through the department to each fund or account group.

The accompanying combined financial statements reflect the combined financial position and combined results of operations of the following divisions of the department:

Family and Adult Services Division: This division operates the Income Maintenance and Social Services programs. Services provided to eligible recipients under those programs include direct financial assistance, food stamps and social services. The division's operations are reported in the general, special revenue, and trust and agency funds.

Vocational Rehabilitation Division: This division provides for the rehabilitation needs of those disabled persons who cannot meet their vocational needs without assistance. The goal of those services, which are provided to mentally, physically and visually handicapped individuals, is to assist recipients toward employment and the enjoyment of full and independent lives. The division's operations are reported in the general, special revenue, and trust and agency funds.

Hawaii Housing Authority: The Hawaii Housing Authority (HHA), which also issues its own separate audited combined financial statements, is organized under the department pursuant to the provisions of Chapter 356, Hawaii Revised Statutes. HHA's mission is to provide safe and sanitary dwelling accommodations for low and moderate income residents of the State of Hawaii (State). To accomplish this objective, HHA provides assistance to low and moderate income families through rent supplement programs and the development and administration of state and federal rental housing projects. HHA's operations are reported in the general, special revenue, capital projects, enterprise, internal service and trust and agency funds, and the general fixed assets and the general long-term obligations account groups.

Health Care Administration Division: This division operates the Medical Assistance Program. Services provided to eligible recipients include medical assistance payments. The division's operations are reported in the general and special revenue funds.

Departmental Administration: Departmental administration includes management, accounting, data processing and other administrative services provided to the department. Those operations are reported in the general, special revenue, and agency funds.

Commission on the Status of Women: This commission is charged with improving the status and well-being of women by promoting equality in government and the workplace. Its operations are reported in the general and trust and agency funds.

Office of Youth Services: The Office of Youth Services is charged with developing and administering programs for preventing, rehabilitating and treating juvenile delinquency in the State. Its operations are reported in the general and special revenue funds.

Note 2 - Summary of significant accounting policies

Basis of Presentation. The financial transactions of the department are recorded in individual funds and account groups which are reported by type in the combined financial statements and are described in the following sections. Each fund and account group is considered a separate accounting entity. The operations of each are accounted for with a separate set of self-balancing accounts. 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. The department accounts for and reports only its portion of those fund types and account groups maintained by the State. The state comptroller maintains the central accounts for all state funds and account groups and publishes financial statements for the State annually. Governmental resources are allocated to and are accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled.

The total columns on the accompanying combined financial statements are captioned "memorandum only" to indicate that they are presented only to facilitate financial analysis. Information in these columns do not purport to present financial position, results of operations or changes in financial position of the department in conformity with generally accepted accounting principles. Such data is not comparable to a consolidation. Interfund balances and transactions have not been eliminated.

The department uses the following fund types, funds and account groups:

Governmental Fund Types:

General Fund: Accounts for all financial resources except those required to be accounted for in another fund.

Special Revenue Funds: Account for the proceeds of specific revenue sources (other than expendable trusts) that are legally restricted to expenditures for specified purposes.

Capital Projects Fund: Accounts for financial resources to be used for the acquisition or construction of major capital facilities other than those financed by proprietary fund types.

Proprietary Fund Types:

Enterprise Funds: Account for operations that are financed and operated in a manner similar to private business enterprises - where the department has decided that periodic determination of revenues earned, expenses incurred and net income is appropriate for management control and public accountability.

Internal Service Funds: Account for the financing of goods or services provided by these funds to other funds or account groups of the department, or to other state units, on a cost-reimbursement basis.

Fiduciary Fund Type:

Trust and Agency Funds: Account for assets held by the department in a trustee capacity or as an agent for other funds.

Account Groups:

General Fixed Assets Account Group: Accounts for all fixed assets of the department, other than those accounted for in the proprietary fund types.

General Long-Term Obligations Account Group: Accounts for the long-term portion of accrued vested vacations, other than the amounts that are specific liabilities of the proprietary fund types.

Basis of Accounting

Governmental Fund Types and Trust and Agency Funds
The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds and expendable trust funds are accounted for using a current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the combined balance sheet. Operating statements of these funds present increases (i.e., revenues and other financial sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

The department uses the modified accrual basis of accounting for the general, special revenue, capital projects and trust and agency funds. Under the modified accrual basis of accounting, revenues and related current assets are recognized in the accounting period when they become both measurable and available to finance operations of the fiscal year or liquidate liabilities existing at year-end. 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. Revenues susceptible to accrual include federal grants and funds appropriated by the state Legislature and allotted by the Governor.

Proprietary Fund Types
All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of those funds are included on the combined balance sheet. Fund equity (i.e., net total assets) is segregated into contributed capital, fund balance and retained earnings 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 types 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.

Inventory
Inventory, principally supplies for HHA-owned projects and administrative offices, is stated at the lower of cost (first-in, first-out method) or market.

Receivables

Receivables in the general and special revenue funds consist primarily of amounts due from recipients of welfare benefit overpayments. The amounts reported as receivables were established based on cash repayments received subsequent to the balance sheet date.

Due from Other Governments

Due from other governments consists of that portion of appropriated or awarded revenues for which cash has not yet been received. Those amounts are due from the State and the federal government, respectively.

Net Property and Equipment

Property and equipment reported in the department's proprietary fund types are recorded at cost, net of accumulated depreciation. Interest costs incurred during construction are capitalized. Depreciation has been provided over the estimated useful lives of those assets using the straight-line method. The estimated useful lives are as follows:

Structures and improvements	10-40	years
Equipment, furniture and fixtures	3-10	years
Vehicles	7-1/2	years

Depreciation recognized on assets acquired or constructed from grants or contributions is transferred to and deducted from contributed capital, to the extent that contributed capital is available.

Property and equipment reported in the general fixed assets account group are recorded at cost. Those assets were acquired or constructed for general governmental purposes and were reported as expenditures in the funds that financed the assets at acquisition. No depreciation is provided on those assets.

Due to Other Governments

Due to other governments consists of cash advances from either the State or the federal government.

Encumbrances

Commitments related to unfilled purchase orders and unperformed contracts are recorded as encumbrances in the governmental fund types. The department records those encumbrances at the time the related purchase orders or contracts are executed or awarded. Encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during a subsequent fiscal year.

Reservations of Fund Balances

Portions of the governmental fund type fund balances are reserved for encumbrances outstanding at year-end. Those amounts are reserved for subsequent fiscal year expenditures. The trust and agency fund balances are reserved for other specific purposes.

HUD Annual Contributions

HHA receives annual contributions and subsidies from the United States Department of Housing and Urban Development (HUD) for operating HHA's housing assistance payment programs and the development and operation of low income housing projects.

HUD provides the annual debt service contributions used to meet principal and interest payments on notes and bonds. The debt service contributions related to principal and interest are recognized in the combined financial statements as contributed capital and nonoperating revenue, respectively. HHA also receives annual subsidies from HUD for housing assistance payments and operating deficits incurred in the operation of the programs. Annual subsidies recorded in the proprietary fund types are recognized as nonoperating revenue upon notification of approval from HUD and are accounted for in the combined statement of revenues and expenses - proprietary fund types as nonoperating revenues - HUD operating subsidy. As explained in Note 6, certain debt service contributions have been discontinued and the related debt has been forgiven or is subject to forgiveness.

Accumulated Vacation

Employees are credited with vacation at the rate of 168 hours per calendar year. Accumulation of such vacation credits is limited to 720 hours at calendar year-end. The employees of the department are entitled to receive cash payments for accumulated vacation leave upon termination of their employment. Such vacation credits are accrued in the general long-term obligations account group.

Note 3 - 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 programs, services and activities to be provided during the fiscal year, (2) the estimated revenue 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 state Legislature at the time of budget consideration and are revised and updated throughout the fiscal year. Amounts reflected as budgeted revenues in the combined statement of revenues and expenditures - budget and actual (budgetary basis) - governmental fund types are those estimates as compiled by the department and reviewed by the Department of Budget and Finance. Budgeted expenditures are derived primarily from the General Appropriations Act of 1991 (Act 296, Session Laws of Hawaii of 1991), as amended by the Supplemental Appropriations Act of 1992 (Act 300, Session Laws of Hawaii of 1992), and from other authorizations contained in the State Constitution, the Hawaii Revised Statutes and other specific appropriation acts in various Session Laws of Hawaii.

All expenditures of these appropriated funds are made pursuant to the appropriations in the biennial budget as amended by subsequent supplemental appropriations. Budgetary control is maintained at the departmental level. Budget revisions and interdepartmental transfers may be effected with certain executive and legislative branch approvals.

Current fiscal year appropriations to the department's governmental fund types and enterprise funds, with the exception of grants-in-aid and certain revolving funds, are subject to a comprehensive appropriated budget. Unbudgeted funds, in addition to prior fiscal year appropriations, grants-in-aid and certain revolving funds, include the internal service and trust and agency funds, as well as those funds for which federal appropriations or private contributions are not known during the budgetary process.

To the extent not expended or encumbered, appropriations generally lapse at the end of the fiscal year or grant period for which the appropriations were made. The state Legislature or federal government specifies the lapse dates and any other contingencies which may terminate the authorization for other appropriations. Known lapses occurring in the fiscal year of appropriation, if any, are included in the amended budgets, and are netted against revenues in the combined statement of revenues and expenditures - budget and actual (budgetary basis) - governmental fund types. Appropriations which lapse in a year subsequent to the fiscal year of appropriation do not affect current fiscal year budgets and are, therefore, excluded from that statement. Transfers of amounts between funds, divisions and departments are not budgeted, and are, therefore, excluded from revenues and expenditures, as applicable, in that statement.

Differences between revenues and expenditures reported on the budgetary basis and those reported in accordance with generally accepted accounting principles (GAAP) are mainly due to revenues and expenditures of unbudgeted funds, the treatment of lapses and transfers for budgeting purposes, and the different methods used to recognize resource uses. For budgeting purposes, resource uses are recognized when cash disbursements are made or funds are encumbered. In financial statements presented in accordance with GAAP, expenditures are recognized when incurred and encumbrances are not reported as resources used.

A summarization of the difference between revenues and expenditures reported on the budgetary basis and those reported in accordance with GAAP for the year ended June 30, 1993 is as follows:

	General	Special Revenue
Excess of revenues over expenditures and other financing uses - actual (budgetary basis)	$ -	$ -
Reserved for encumbrances	11,381,593	4,762,771
Expenditures for liquidation of prior fiscal year encumbrances and reservations	(23,750,582)	(3,295,425)
Accruals related to federal reimbursements for program expenditures	(8,132,204)	8,706,332
Accounts receivable	(92,593)	(50,277)
Accrued medical assistance payable	(10,513,071)	-
Accrued wages and employee benefits payable	-	(2,671,415)
Excess of revenues over (under) expenditures and other financing uses - GAAP basis	$ (31,106,857)	$ 7,451,986

Note 4 - Cash and short-term investments

Cash and short-term investments consists of the following at June 30, 1993:

Cash in State Treasury	$ 76,247,021
Certificates of deposit	5,537,561
Cash in banks	2,246,300
Cash on hand	24,505
	$ 84,055,387

The State maintains a cash pool that is available for all funds. Each fund type's portion of this pool (reported as cash in State Treasury) is displayed on the combined balance sheet within "Cash and short-term investments." Those funds are pooled with funds from other state agencies and departments and deposited in approved financial institutions by the director of the Department of Budget and Finance.

Deposits not covered by federal deposit insurance are fully collateralized by government securities held in the name of the State by third-party custodians.

The department also maintains cash in banks and certificates of deposit, which are held separately from cash in State Treasury. As of June 30, 1993, the carrying amount of total bank deposits (including time certificates of deposit of $5,537,561) was $7,783,861 and the corresponding bank balances which are represented were $7,624,322. Those deposits not covered by federal deposit insurance are also fully collateralized by government securities held in the name of the State by third-party custodians.

Note 5 - Net property and equipment

Net property and equipment in the proprietary fund types consists of the following at June 30, 1993:

	Enterprise funds	Internal service funds
Land	$ 21,164,459	$ -
Structures and improvements	191,061,968	-
Equipment, furniture and fixtures	5,721,283	596,084
Construction in progress	25,661,308	-
Vehicles	-	461,270
	243,609,018	1,057,354
Less accumulated depreciation	97,356,126	768,481
	$ 146,252,892	$ 288,873

Changes in the department's general fixed assets account group (unaudited) for the year ended June 30, 1993 are as follows:

	Balance at July 1, 1992	Additions	Disposals	Balance at June 30, 1993
Land	$ 562,210	$ 16,000	$ -	$ 578,210
Building and improvements	8,548,045	11,715,519	-	20,263,564
Equipment, furniture and fixtures	16,616,130	1,001,230	(168,804)	17,448,556
Construction in progress	15,978,789	2,043,685	(2,314,210)	15,708,264
Vehicles	791,302	11,224	(17,563)	784,963
	$ 42,496,476	$ 14,787,658	$ (2,500,577)	$ 54,783,557

Construction in progress at June 30, 1993 consists primarily of costs relating to various housing projects of HHA.

Note 6 - Liabilities collateralized by HUD annual contributions

Liabilities collateralized by HUD annual contributions at June 30, 1993 are composed of the following:

U. S. government loans, bearing interest at the existing rates charged to HUD by the U. S. Treasury (6.63% to 10% at June 30, 1993), maturing during the year ending June 30, 1994	$ 49,964,458
Federal Financing Bank note, due in decreasing annual payments, maturing at various dates through 2016 and bearing interest at 6.6%	11,219,940
USGI, Inc. mortgage note, bearing interest at 7.5%, principal and interest due monthly, maturing January 1, 2018, collateralized by the Banyan Street Manor Project	1,529,723
Housing bonds payable	22,961,000
	$ 85,675,121

During the year ended June 30, 1987, HHA was notified by HUD that due to certain provisions of the "Consolidated Omnibus Budget Reconciliation Act of 1985", HUD would no longer be making annual contributions for debt service on the U. S. government loans in anticipation of the pending debt forgiveness described below.

On September 11, 1987, HHA adopted a resolution approving an amendment to its consolidated annual contributions contract with HUD in which outstanding U. S. government loans which meet certain criteria will be forgiven. On August 17, 1988, HUD issued a policy statement stating that debt meeting certain criteria would be forgiven. During the year ended June 30, 1989, HHA, based on information supplied by HUD, recorded a forgiveness of $30,750,000 of HHA's debt. In fiscal year 1993, HUD informed HHA that $3,862,698 of the amount of forgiveness recorded in 1989 was still outstanding. The effect of this error on the combined financial statements prior to July 1, 1992 are as follows:

Adjustment for additional amounts due on U. S. government loans	$ 3,862,698
Add interest accruals to July 1, 1992	1,105,017
Reductions for HUD annual contributions to July 1, 1992	(1,105,017)
	$ 3,862,698

As of June 30, 1993, approximately $49,964,000 of outstanding U. S. government loans meet the criteria to be forgiven by HUD. HHA expects that this debt will be forgiven upon action by HUD.

HHA continues to recognize the outstanding principal balance due on U. S. government loans until such time that the debt is actually forgiven. Related interest is accrued and expensed in the period incurred. Accrued interest directly related to the outstanding U. S. government loans amounted to approximately $27,961,000 as of June 30, 1993, of which approximately $4,311,000 was incurred during the current fiscal year. HUD annual contributions receivable was recognized to the extent of accrued interest payable at June 30, 1993.

HHA issued housing bonds pursuant to Chapter 356 of the Hawaii Revised Statutes to provide permanent financing for low income housing projects. These bonds are the obligation of HHA and not of the Federal Low-Rent Program specifically or the State in general. The first five issues are callable after 10 years and the remaining issues are callable after 15 years from the date of issue. The housing bonds require annual level debt service payments and are collateralized by HUD's annual contribution for debt service and the excess of project revenues over project expenses. Housing bonds payable at June 30, 1993 consisted of the following:

Bond issue	Issue date - August 1:	Last maturity date - August 1:	Interest rate	Principal balance
3rd	1955	1996	2.375%	$ 200,000
4th	1957	1998	3.000	266,000
5th	1958	1998	3.500	499,000
6th	1959	1998	3.500	506,000
7th	1961	2002	3.125	200,000
8th	1964	2005	3.375	3,860,000
9th	1964	2005	3.625	780,000
10th	1965	2006	3.625	1,755,000
11th	1966	2007	3.625	980,000
12th	1966	2007	4.500	2,055,000

13th	1968	2009	5.125	1,895,000
14th	1970	2009	5.750	9,965,000
				$ 22,961,000

Maturities of bonds and notes payable in each of the next five years and thereafter are as follows:

Year ending June 30:	
1994	$ 51,592,000
1995	1,682,000
1996	1,768,000
1997	1,868,000
1998	1,899,000
Thereafter	26,866,121
	$ 85,675,121

Note 7 - Contributed capital

The contributed capital of the HUD Subsidized Programs in the enterprise funds includes HUD annual contributions for the payment of principal on debt incurred to finance development and modernization of HHA-owned housing projects.

Note 8 - Excess of expenditures over appropriations, net loss and fund balance deficits and accumulated deficit

In the combined financial statements prepared in conformity with GAAP, expenditures exceeded revenues in the general fund by approximately $31,107,000. The excess of expenditures over revenues in the general fund is due primarily to the accrual of expenditures expected to be paid with future revenues.

During the year ended June 30, 1993, the enterprise funds experienced a net loss of approximately $5,000,000. To a certain extent, this loss is offset by the transfer of depreciation on assets acquired or constructed from grants and contributed capital in the combined statement of fund equity - proprietary fund types. Depreciation on such assets has reduced contributed capital.

The general and special revenue funds have deficits in the unreserved fund balances at June 30, 1993, aggregating to approximately $75,058,000 and $836,000, respectively. These deficits resulted primarily from the fact that under GAAP, expenditures are recorded on the accrual basis when incurred, while revenues are recognized only when the funds are measurable and available. The general fund's deficit also results from the expenditure of moneys which were required to be lapsed to the state's general fund.

The accumulated deficit of approximately $8,600,000 in the enterprise funds results primarily from accumulated depreciation on assets not acquired or constructed from grants and contributions. Depreciation expense on such assets has reduced retained earnings. At June 30, 1993, contributed capital net of the related depreciation approximates $73,000,000. This amount is sufficient to offset the accumulated deficit in total fund equity at June 30, 1993.

Note 9 - Restatement of beginning fund balances (deficit)

The fund balances (deficit) at July 1, 1992 have been restated as follows:

	General fund	Special revenue funds	Enterprise funds
Balances at July 1, 1992, as previously reported	$ 49,195,069	$ (20,471,502)	$ (4,856,771)
Adjustment	(81,764,520)	21,025,759	(3,862,698)
Balances at July 1, 1992, as restated	$ (32,569,451)	$ 554,257	$ (8,719,469)

The general fund's beginning fund balance was restated to recognize amounts due to the state's general fund as of June 30, 1992 for federal reimbursements received subsequent to the department's fiscal year-end which have not been lapsed to the state's general fund. The recognition of amounts due to the state's general fund as of June 30, 1992 had the effect of decreasing the general fund's beginning fund balance by $61,866,841 in the combined financial statements. The general fund's beginning fund balance was also restated to reflect the actual amount of federal reimbursements received and lapsed to the state's general fund and to reflect the actual amount of federal reimbursements received and due from the special revenue funds as of June 30, 1992. These corrections had the effect of decreasing the general fund's beginning fund balance by $7,004,301 and $12,893,378, respectively, as of June 30, 1992 in the combined financial statements.

The special revenue funds' beginning fund deficit was restated to reflect the actual amount of federal reimbursements received and due to the general fund through June 30, 1992. This correction had the effect of decreasing the special revenue funds' beginning fund deficit by $21,025,759 as of June 30, 1992 in the combined financial statements.

The enterprise funds' beginning accumulated deficit was restated to reflect the actual amount of Treasury notes forgiven by HUD (see Note

6). This correction had the effect of increasing the enterprise funds' beginning accumulated deficit by $3,862,698 as of June 30, 1992 in the combined financial statements.

Note 10 - Retirement benefits

Employees' Retirement System

Substantially all eligible employees of the department are members of the Employees' Retirement System of the State of Hawaii (System), a cost-sharing multiple-employer public employee retirement plan covering eligible employees of the State and counties. The System 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 System who are also covered under social security. Persons employed in positions not covered by social security are precluded 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 under the contributory and noncontributory options, respectively.

Required contributions to the System are based upon the frozen initial liability method, and include amortization of the accrued unfunded liability over a period of 50 years beginning July 1, 1964. The state's policy is to fund its required contribution annually. The department was required to make a contribution to the System for the year ended June 30, 1993 of approximately $1,413,000, of which approximately $1,223,000 was paid subsequent to June 30, 1993.

Measurement of assets and actuarial valuations are made for the entire System and are not separately computed for individual participating employers such as the department. The disclosures required by Governmental Accounting Standards Board Statement No. 5 are presented in the System's Comprehensive Annual Financial Report (CAFR). The following data is provided as of June 30, 1992 for the entire System from the disclosures contained in the CAFR for the year then ended, the most recent available information:

Pension benefit obligation	$ 6,092,482,400
Net assets available for benefits (at cost)	(4,502,354,900)
Unfunded pension benefit obligation	$ 1,590,127,500

The pension benefit obligation is a standardized measure of the present value of pension benefits, adjusted for the effects of projected salary increases, estimated to be payable in the future as a result of employee service to date.

The entire System's actuarially determined employer contribution requirements were met as of June 30, 1993.

Post-retirement health care and life insurance benefits

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 share of the post-retirement health care and life insurance benefits for the year ended June 30, 1993 has not been separately computed and is not reflected in the department's general fund financial statements. The department's special revenue funds' and enterprise funds' share of the post-retirement health care and life insurance benefits expense for the year ended June 30, 1993 was approximately $244,000 and is included in those funds' financial statements.

Note 11 - Operating leases

The department leases office facilities on a long-term basis. Those office leases expire on various dates from 1994 through 2000.

HHA leases land as a sublessee under an original contract for 55 years. The assignment of the lease entered into is for the remaining 50 years through 2040. The rent for the last 25 years of this lease is to be negotiated based on the fair market value of the land.

Minimum future rentals on noncancelable operating leases with terms of one year or more at June 30, 1993 are as follows:

Year ending June 30:	
1994	$ 2,023,000
1995	1,323,000
1996	998,000
1997	519,000
1998	467,000
Thereafter	7,015,000
	$ 12,345,000

Note 12 - Contingencies

Medicaid program

The department reimburses providers for medical services provided to Medicaid recipients under a Prospective Payment System (PPS). Under PPS, standard costs and rates are negotiated between the department and the state's Medicaid providers in advance. PPS allows providers to file for standard cost and rate adjustments up to five years subsequent to the rendering of those services. The amount of future adjustments, if any, to be made for services provided through June 30, 1993 cannot be determined at this time. Any adjustments would be funded from future appropriations.

The department is also subject to liabilities arising from charges for medical services provided to Medicaid recipients.

Federal assistance programs

During fiscal year 1993, the department did not maintain adequate records to account for the expenditures of certain programs which were paid with moneys appropriated for other programs. Additionally, the department transferred federal funds from one federal assistance program to another to cover cash shortages. The combined financial statements do not include an adjustment for any liability that may result from the actions of federal agencies relative to these instances of noncompliance with federal assistance requirements.

Note 13 - Commitments and other contingencies

Accumulated sick leave pay

Sick leave for all full-time employees accumulates at the rate of one and three-quarters working days for each month of service without limit, but can be taken only in the event of illness and is not convertible to compensation upon termination of employment. However, a department 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 the System. Accumulated sick leave as of June 30, 1993 aggregated approximately $28,402,000.

Deferred compensation plan

In 1983, the State established a deferred compensation plan which enables state employees to defer a portion of their compensation. The 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 an 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 rights 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.

Litigation

The department is involved in various lawsuits, the outcomes of which, in the opinion of management, will not have a material adverse effect on the department's combined financial position.

Losses, if any, are either covered by insurance or will be paid from legislative appropriations of the state's general fund.

Insurance

The State is self-insured for substantially all perils, including worker's compensation.

Hurricane Iniki

In September 1992, HHA's projects on the island of Kauai suffered significant damage from Hurricane Iniki. Management estimates that the total cost to repair these damages, including certain administrative and relocation costs, is approximately $20,640,000. As of June 30, 1993, HHA, which is insured under the state's $150,000,000 property insurance policy covering all state properties (less a $250,000 deductible), has received approximately $4,670,000 of insurance proceeds from the State. HHA also received approximately $42,000 from the Federal Emergency Management Agency for reimbursement of hurricane related costs. HHA estimates that HUD will reimburse approximately $15,760,000 to HHA for the hurricane damages, and accordingly, HHA has accrued and reflected such amount as due from other governments on the accompanying combined balance sheet - all fund types and account groups as of June 30, 1993. As of June 30, 1993, HHA had outstanding contractual commitments relating to the repair of hurricane damages with various consultants and general contractors in the amount of $15,200,000.

Exhibit A

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combined Balance Sheet - All Fund Types and Account Groups

June 30, 1993

	Governmental Fund Types			Proprietary Fund Types		Fiduciary Fund Type	Account Groups		
Assets	General	Special revenue	Capital projects	Enterprise	Internal service	Trust and agency	General fixed assets (unaudited)	General long-term obligations	Total (memorandum only)
Cash and short-term investments (Note 4)	$ 38,242,905	$ 23,124,421	$ 10,040,709	$ 9,483,248	$ 504,338	$ 2,659,766	$ -	$ -	$ 84,055,387
Inventory	-	-	-	481,756	-	-	-	-	481,756
HUD annual contributions receivable	-	-	-	28,992,325	-	-	-	-	28,992,325
Other receivables	98,325	95,173	-	491,431	130	-	-	-	685,059
Due from other funds	5,674,225	2,948,536	-	3,880,287	4,538	-	-	-	12,507,586
Due from other governments	-	10,947,041	13,466,765	15,797,715	-	-	-	-	40,211,521
Restricted deposits and funded reserves	-	-	-	873,510	-	-	-	-	873,510
Prepayments to landlords	-	998,764	-	-	-	-	-	-	998,764
Other assets	-	31,000	-	303,896	-	-	-	-	334,896
Net property and equipment (Note 5)	-	-	-	146,252,892	288,873	-	54,783,557	-	201,325,322
Amounts to be provided for retirement of general long-term obligations	-	-	-	-	-	-	-	7,964,935	7,964,935
	$ 44,015,455	$ 38,144,935	$ 23,507,474	$ 206,557,060	$ 797,879	$ 2,659,766	$ 54,783,557	$ 7,964,935	$ 378,431,061

(Continued)

Exhibit A

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combined Balance Sheet - All Fund Types and Account Groups, Continued

	Governmental Fund Types			Proprietary Fund Types		Fiduciary Fund Type	Account Groups		
Liabilities and Fund Equity	General	Special revenue	Capital projects	Enterprise	Internal service	Trust and agency	General fixed assets (unaudited)	General long-term obligations	Total (memorandum only)
Liabilities:									
Vouchers and contracts payable	$ 2,371,455	$ 669,504	$ -	$ 1,384,334	$ -	$ -	$ -	$ -	$ 4,425,293
Accrued wages and employee benefits payable	203,702	2,671,415	-	1,267,593	-	-	-	7,964,935	12,107,645
Accrued interest (Note 6)	-	-	-	28,992,324	-	-	-	-	28,992,324
Reserve for Hurricane Iniki repairs	-	-	-	17,565,657	-	-	-	-	17,565,657
Due to individuals	-	-	-	-	-	184,547	-	-	184,547
Due to other funds	1,920,123	6,819,523	-	3,767,940	-	1,103,486	-	-	13,611,072
Due to other governments	-	19,978,250	-	-	-	-	-	-	19,978,250
Due to State Treasury	49,911,369	-	-	-	-	-	-	-	49,911,369
Accrued medical assistance payable	53,285,114	-	-	-	-	-	-	-	53,285,114
Liabilities collateralized by HUD annual contributions (Note 6)	-	-	-	85,675,121	-	-	-	-	85,675,121
Other liabilities	-	-	853,855	2,996,574	-	2,050	-	-	3,852,479
Total liabilities	107,691,763	30,138,692	853,855	141,649,543	-	1,290,083	-	7,964,935	289,588,871
Fund equity:									
Investment in general fixed assets	-	-	-	-	-	-	54,783,557	-	54,783,557
Contributed capital:									
Federal government grants	-	-	-	113,057,517	111,926	-	-	-	113,169,443
State of Hawaii grants	-	-	-	40,248,643	298,655	-	-	-	40,547,298
Other	-	-	-	423,900	-	-	-	-	423,900
	-	-	-	153,730,060	410,581	-	54,783,557	-	208,924,198
Less depreciation on property and equipment acquired or constructed from grants and contributions	-	-	-	80,234,308	332,327	-	-	-	80,566,635
	-	-	-	73,495,752	78,254	-	54,783,557	-	128,357,563
Retained earnings (accumulated deficit)	-	-	-	(8,588,235)	719,625	-	-	-	(7,868,610)
Fund balances (deficit):									
Reserved for encumbrances	11,381,593	4,762,771	5,133,720	-	-	-	-	-	21,278,084
Reserved for other purposes	-	-	-	-	-	1,369,683	-	-	1,369,683
Unreserved	(75,057,901)	3,243,472	17,519,899	-	-	-	-	-	(54,294,530)
	(63,676,308)	8,006,243	22,653,619	64,907,517	797,879	1,369,683	54,783,557	-	88,842,190
	$ 44,015,455	$ 38,144,935	$ 23,507,474	$ 206,557,060	$ 797,879	$ 2,659,766	$ 54,783,557	$ 7,964,935	$ 378,431,061

See accompanying notes to combined financial statements.

Exhibit B

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combined Statement of Revenues, Expenditures and Changes in
Fund Balances (Deficit) - Governmental Fund Types and Fiduciary Fund Type

Year ended June 30, 1993

	Governmental Fund Types			Fiduciary Fund Type	
	General	Special revenue	Capital projects	Trust and agency	Total (memorandum only)
Revenues:					
State allotted appropriations	$ 419,997,026	$ -	$ 9,903,967	$ -	$ 429,900,993
Intergovernmental - federal	-	330,683,519	-	1,259,222	331,942,741
Other	-	16,825,842	-	-	16,825,842
	419,997,026	347,509,361	9,903,967	1,259,222	778,669,576
Expenditures:					
Healthcare	225,277,511	192,099,070	-	-	417,376,581
Welfare	196,058,868	125,096,059	-	519,755	321,674,682
Vocational rehabilitation	2,254,817	6,219,830	-	-	8,474,647
Housing	9,002,385	16,642,416	-	-	25,644,801
Capital outlays	-	-	18,771,667	-	18,771,667
	432,593,581	340,057,375	18,771,667	519,755	791,942,378
Excess of revenues over (under) expenditures	(12,596,555)	7,451,986	(8,867,700)	739,467	(13,272,802)
Other financing uses - operating transfers out to State Treasury	(18,510,302)	-	-	-	(18,510,302)
Excess of revenues over (under) expenditures and other financing uses	(31,106,857)	7,451,986	(8,867,700)	739,467	(31,783,104)
Fund balances (deficit) at July 1, 1992, as restated (Note 9)	(32,569,451)	554,257	31,521,319	630,216	136,341
Fund balances (deficit) at June 30, 1993	$ (63,676,308)	$ 8,006,243	$ 22,653,619	$ 1,369,683	$ (31,646,673)

See accompanying notes to combined financial statements.

Exhibit C

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combined Statement of Revenues and Expenditures - Budget and Actual (Budgetary Basis) - Governmental Fund Types

Year ended June 30, 1993

	General Fund			Special Revenue Funds			Capital Projects Fund			Total (memorandum only)		
	Budget	Budgetary actual	Variance favorable (unfavorable)	Budget	Budgetary actual	Variance favorable (unfavorable)	Budget	Budgetary actual	Variance favorable (unfavorable)	Budget	Budgetary actual	Variance favorable (unfavorable)
Revenues:												
State allotted appropriations	$ 436,498,552	$ 432,263,001	$ (4,235,551)	$ -	$ -	$ -	$ 19,953,000	$ 19,953,000	$ -	$ 456,451,552	$ 452,216,001	$ (4,235,551)
Intergovernmental - federal	-	-	-	329,430,141	329,238,110	(192,031)	-	-	-	329,430,141	329,238,110	(192,031)
	436,498,552	432,263,001	(4,235,551)	329,430,141	329,238,110	(192,031)	19,953,000	19,953,000	-	785,881,693	781,454,111	(4,427,582)
Expenditures:												
Healthcare	213,020,197	212,725,633	294,564	185,668,967	184,415,253	1,253,714	-	-	-	398,689,164	397,140,886	1,548,278
Welfare	209,815,966	196,835,700	12,980,266	133,431,669	122,629,459	10,802,210	-	-	-	343,247,635	319,465,159	23,782,476
Vocational rehabilitation	4,143,454	3,989,890	153,564	10,329,505	9,735,729	593,776	-	-	-	14,472,959	13,725,619	747,340
Housing	9,518,935	9,107,809	411,126	-	-	-	-	-	-	9,518,935	9,107,809	411,126
Capital outlays	-	-	-	-	-	-	19,953,000	10,758,000	9,195,000	19,953,000	10,758,000	9,195,000
	436,498,552	422,659,032	13,839,520	329,430,141	316,780,441	12,649,700	19,953,000	10,758,000	9,195,000	785,881,693	750,197,473	35,684,220
Excess of revenues over expenditures	-	9,603,969	9,603,969	-	12,457,669	12,457,669	-	9,195,000	9,195,000	-	31,256,638	31,256,638
Other financing uses - operating transfers out	-	(9,603,969)	(9,603,969)	-	(12,457,669)	(12,457,669)	-	-	-	-	(22,061,638)	(22,061,638)
Excess of revenues over expenditures and other financing uses	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 9,195,000	$ 9,195,000	$ -	$ 9,195,000	$ 9,195,000

See accompanying notes to combined financial statements.

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combined Statement of Revenues and Expenses - Proprietary Fund Types

Year ended June 30, 1993

	Enterprise	Internal service	Total (memorandum only)
Operating revenues:			
Rental	$ 18,230,363	$ 132,545	$ 18,362,908
Other	678,904	14,966	693,870
	18,909,267	147,511	19,056,778
Operating expenses:			
Personal services	8,016,859	-	8,016,859
Utilities	5,863,781	-	5,863,781
Depreciation	5,235,643	100,710	5,336,353
Repairs and maintenance	3,528,163	-	3,528,163
Payments in lieu of taxes	1,159,853	-	1,159,853
Insurance	849,983	-	849,983
Other	2,065,448	-	2,065,448
	26,719,730	100,710	26,820,440
Operating income (loss)	(7,810,463)	46,801	(7,763,662)
Nonoperating revenues and expenses:			
Insurance proceeds	20,476,022	-	20,476,022
Loss from Hurricane Iniki damages	(20,640,239)	-	(20,640,239)
HUD accrued contribution for interest (Note 6)	5,284,983	-	5,284,983
HUD operating subsidy	3,006,571	-	3,006,571
Interest expense (Note 6)	(5,480,091)	-	(5,480,091)
Interest income	203,485	12,768	216,253
	2,850,731	12,768	2,863,499
Net income (loss)	$ (4,959,732)	$ 59,569	$ (4,900,163)

See accompanying notes to combined financial statements.

Exhibit E

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combined Statement of Fund Equity - Proprietary Fund Types

Year ended June 30, 1993

	Enterprise Funds			Internal Service Funds			
	Contributed capital	Retained earnings (accumulated deficit)	Total fund equity	Contributed capital	Retained earnings	Total fund equity	Total (memorandum only)
Balances at July 1, 1992, as previously reported	$ 40,557,359	$ (4,856,771)	$ 35,700,588	$ 85,203	$ 632,990	$ 718,193	$ 36,418,781
Adjustment (Notes 6 and 9)	-	(3,862,698)	(3,862,698)	-	-	-	(3,862,698)
Balances at July 1, 1992, as restated	40,557,359	(8,719,469)	31,837,890	85,203	632,990	718,193	32,556,083
Net income (loss)	-	(4,959,732)	(4,959,732)	-	59,569	59,569	(4,900,163)
Transfer of depreciation on property and equipment acquired or constructed from grants and contributions to contributed capital	(5,090,966)	5,090,966	-	(27,066)	27,066	-	-
Contributions:							
Federal government	459,586	-	459,586	19,207	-	19,207	478,793
HUD annual contributions (Notes 6 and 7)	19,716,156	-	19,716,156	-	-	-	19,716,156
State of Hawaii	17,853,617	-	17,853,617	910	-	910	17,854,527
Balances at June 30, 1993	$ 73,495,752	$ (8,588,235)	$ 64,907,517	$ 78,254	$ 719,625	$ 797,879	$ 65,705,396

See accompanying notes to combined financial statements.

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combined Statement of Cash Flows - Proprietary Fund Types

Year ended June 30, 1993

	Enterprise	Internal service	Total (memorandum only)
Cash flows from operating activities:			
Operating income (loss)	$ (7,810,463)	$ 46,801	$ (7,763,662)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:			
Depreciation	5,235,643	100,710	5,336,353
Loss from Hurricane Iniki damages (net of proceeds)	(164,217)	-	(164,217)
Gain on disposal of fixed assets	-	(5,017)	(5,017)
HUD operating subsidy	3,006,571	-	3,006,571
Other	24,727	-	24,727
Increase in assets:			
Inventory	(69,022)	-	(69,022)
Other receivables	(101,872)	-	(101,872)
Due from other funds	(95,530)	(4,538)	(100,068)
Due from other governments	(15,806,726)	-	(15,806,726)
Other assets	(5,784)	-	(5,784)
Increase (decrease) in liabilities:			
Vouchers and contracts payable	362,286	-	362,286
Accrued expenses	49,323	-	49,323
Reserve for Hurricane Iniki repairs	17,565,657	-	17,565,657
Due to other funds	(18,699)	-	(18,699)
Other liabilities	1,255,274	-	1,255,274
Total adjustments	11,237,631	91,155	11,328,786
Net cash provided by operating activities	3,427,168	137,956	3,565,124
Cash flows from capital and related financing activities:			
Payments for capital acquisition	(17,287,786)	(47,189)	(17,334,975)
Principal payments on mortgage loan	(30,713)	-	(30,713)
Receipts from capital grants	19,091,832	-	19,091,832
Receipts from transfer	253,500	-	253,500
Proceeds from transfer of equipment	-	25	25
Net cash provided by (used in) capital and related financing activities	2,026,833	(47,164)	1,979,669

(Continued)

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combined Statement of Cash Flows - Proprietary Fund Types, Continued

	Enterprise	Internal service	Total (memorandum only)
Cash flows from investing activities:			
Receipts of interest	$ 203,307	$ 12,887	$ 216,194
Payments of interest	(195,108)	-	(195,108)
Net mortgage escrow deposits	(1,973)	-	(1,973)
Net deposits into reserve for replacement	(11,365)	-	(11,365)
Net deposits into residual receipts reserve	(430,397)	-	(430,397)
Capital expenditures	(438)	-	(438)
Net cash provided by (used in) investing activities	(435,974)	12,887	(423,087)
Net increase in cash and short-term investments	5,018,027	103,679	5,121,706
Cash and short-term investments at beginning of year	4,465,221	400,659	4,865,880
Cash and short-term investments at end of year	$ 9,483,248	$ 504,338	$ 9,987,586

Schedule of noncash investing, capital and financing activities:

During the current fiscal year, the Federal Low-Rent Program incurred $5,284,983 of interest expense on HUD collateralized debt of which $1,769,622 was paid by HUD. The remaining balance of the interest expense is expected to be forgiven by HUD (see Note 6). The Federal Low-Rent Program also had a reduction in HUD collateralized debt of $1,523,199 which was retired by HUD.

During the current fiscal year, the enterprise funds and the internal service funds acquired $18,313,203 and $20,117, respectively, of certain capital assets that were contributed to the funds by federal and state agencies.

See accompanying notes to combined financial statements.

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Balance Sheet - General Fund

June 30, 1993

Assets	Family and Adult Services Division	Vocational Rehabilitation Division	Hawaii Housing Authority	Health Care Administration Division	Departmental Administration	Commission on the Status of Women	Office of Youth Services	Total
Cash	$ 18,245,023	$ 479,441	$ 1,113,367	$ 17,683,827	$ 704,900	$ 15,947	$ 400	$ 38,242,905
Receivables	80,831	-	-	17,494	-	-	-	98,325
Due from other funds	3,088,548	2,585,677	-	-	-	-	-	5,674,225
	$ 21,414,402	$ 3,065,118	$ 1,113,367	$ 17,701,321	$ 704,900	$ 15,947	$ 400	$ 44,015,455
Liabilities and Fund Balances (Deficit)								
Liabilities:								
Vouchers and contracts payable	1,658,560	174,649	39,218	499,028	-	-	-	2,371,455
Accrued wages and employee benefits payable	126,418	-	-	19,183	58,101	-	-	203,702
Due to other funds	1,915,390	-	4,733	-	-	-	-	1,920,123
Due to State Treasury	17,911,164	2,607,429	-	29,382,276	10,450	50	-	49,911,369
Accrued medical assistance payable	-	-	-	53,285,114	-	-	-	53,285,114
Total liabilities	21,611,532	2,782,078	43,951	83,185,601	68,551	50	-	107,691,763
Fund balances (deficit):								
Reserved for encumbrances	7,953,686	283,040	1,113,367	1,378,854	636,349	15,897	400	11,381,593
Unreserved	(8,150,816)	-	(43,951)	(66,863,134)	-	-	-	(75,057,901)
Total fund balances (deficit)	(197,130)	283,040	1,069,416	(65,484,280)	636,349	15,897	400	(63,676,308)
	$ 21,414,402	$ 3,065,118	$ 1,113,367	$ 17,701,321	$ 704,900	$ 15,947	$ 400	$ 44,015,455

Schedule II

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) - General Fund

Year ended June 30, 1993

	Family and Adult Services Division	Vocational Rehabilitation Division	Hawaii Housing Authority	Health Care Administration Division	Departmental Administration	Commission on the Status of Women	Office of Youth Services	Total
Revenues - State allotted appropriations	$ 181,201,277	$ 3,940,516	$ 9,137,095	$ 212,770,718	$ 12,797,220	$ 135,468	$ 14,732	$ 419,997,026
Expenditures:								
Healthcare	-	-	-	225,277,511	-	-	-	225,277,511
Welfare	183,840,068	-	-	-	12,113,971	193,815	(88,986)	196,058,868
Vocational rehabilitation	-	2,254,817	-	-	-	-	-	2,254,817
Housing	-	-	9,002,385	-	-	-	-	9,002,385
	183,840,068	2,254,817	9,002,385	225,277,511	12,113,971	193,815	(88,986)	432,593,581
Excess of revenues over (under) expenditures	(2,638,791)	1,685,699	134,710	(12,506,793)	683,249	(58,347)	103,718	(12,596,555)
Other financing sources (uses):								
Intrafund transfers, net	549,404	-	-	-	(549,404)	-	-	-
Operating transfers out to State Treasury	(1,900,415)	(1,508,081)	-	(15,101,806)	-	-	-	(18,510,302)
	(1,351,011)	(1,508,081)	-	(15,101,806)	(549,404)	-	-	(18,510,302)
Excess of revenues and other financing sources over (under) expenditures and other financing uses	(3,989,802)	177,618	134,710	(27,608,599)	133,845	(58,347)	103,718	(31,106,857)
Fund balances (deficit) at July 1, 1992, as restated	3,792,672	105,422	934,706	(37,875,681)	502,504	74,244	(103,318)	(32,569,451)
Fund balances (deficit) at June 30, 1993	$ (197,130)	$ 283,040	$ 1,069,416	$ (65,484,280)	$ 636,349	$ 15,897	$ 400	$ (63,676,308)

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Balance Sheet - Special Revenue Funds

June 30, 1993

Assets	Family and Adult Services Division	Vocational Rehabilitation Division	Hawaii Housing Authority	Health Care Administration Division	Departmental Administration	Office of Youth Services	Total
Cash and short-term investments	$ 5,624,237	$ 1,380,033	$ 3,937,764	$ 11,216,892	$ 820,595	$ 144,900	$ 23,124,421
Receivables	78,456	-	-	16,717	-	-	95,173
Due from other funds	1,915,390	-	1,033,146	-	-	-	2,948,536
Due from other governments	6,142,973	2,989,941	169,736	1,445,689	-	198,702	10,947,041
Prepayments to landlords	-	-	998,764	-	-	-	998,764
Other	-	-	31,000	-	-	-	31,000
	$ 13,761,056	$ 4,369,974	$ 6,170,410	$ 12,679,298	$ 820,595	$ 343,602	$ 38,144,935
Liabilities and Fund Balances (Deficit)							
Liabilities:							
Vouchers and contracts payable	118,012	99,337	452,155	-	-	-	669,504
Accrued wages and employee benefits payable	2,095,872	-	-	433,111	142,432	-	2,671,415
Due to other funds	3,088,548	2,585,677	1,145,298	-	-	-	6,819,523
Due to other governments	4,669,775	1,284,085	493,730	12,598,589	820,595	111,476	19,978,250
Total liabilities	9,972,207	3,969,099	2,091,183	13,031,700	963,027	111,476	30,138,692
Fund balances (deficit):							
Reserved for encumbrances	4,065,778	400,875	-	63,992	-	232,126	4,762,771
Unreserved	(276,929)	-	4,079,227	(416,394)	(142,432)	-	3,243,472
Total fund balances (deficit)	3,788,849	400,875	4,079,227	(352,402)	(142,432)	232,126	8,006,243
	$ 13,761,056	$ 4,369,974	$ 6,170,410	$ 12,679,298	$ 820,595	$ 343,602	$ 38,144,935

Schedule IV

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) - Special Revenue Funds

Year ended June 30, 1993

	Family and Adult Services Division	Vocational Rehabilitation Division	Hawaii Housing Authority	Health Care Administration Division	Departmental Administration	Office of Youth Services	Total
Revenues:							
Intergovernmental - federal	$ 132,514,171	$ 5,091,680	$ -	$ 191,684,371	$ 756,042	$ 637,255	$ 330,683,519
Other	-	-	16,825,842	-	-	-	16,825,842
	132,514,171	5,091,680	16,825,842	191,684,371	756,042	637,255	347,509,361
Expenditures:							
Healthcare	-	-	-	192,099,070	-	-	192,099,070
Welfare	123,836,927	-	-	-	854,003	405,129	125,096,059
Vocational rehabilitation	-	6,219,830	-	-	-	-	6,219,830
Housing	-	-	16,642,416	-	-	-	16,642,416
	123,836,927	6,219,830	16,642,416	192,099,070	854,003	405,129	340,057,375
Excess of revenues over (under) expenditures	8,677,244	(1,128,150)	183,426	(414,699)	(97,961)	232,126	7,451,986
Fund balances (deficit) at July 1, 1992, as restated	(4,888,395)	1,529,025	3,895,801	62,297	(44,471)	-	554,257
Fund balances (deficit) at June 30, 1993	$ 3,788,849	$ 400,875	$ 4,079,227	$ (352,402)	$ (142,432)	$ 232,126	$ 8,006,243

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Balance Sheet - Enterprise Funds

June 30, 1993

Assets	Federal Low-Rent Program	Other funds	Total
Cash and short-term investments	$ 7,896,493	$ 1,586,755	$ 9,483,248
Inventory	481,756	-	481,756
HUD annual contributions receivable	28,992,325	-	28,992,325
Other receivables	390,605	100,826	491,431
Due from other funds	3,674,227	206,060	3,880,287
Due from other governments	15,797,715	-	15,797,715
Other assets	163,377	1,014,029	1,177,406
Net property and equipment	112,628,643	33,624,249	146,252,892
	$ 170,025,141	$ 36,531,919	$ 206,557,060
Liabilities and Fund Equity			
Liabilities:			
Vouchers and contracts payable	1,379,047	5,287	1,384,334
Accrued wages and employee benefits payable	1,097,591	170,002	1,267,593
Accrued interest	28,992,324	-	28,992,324
Reserve for Hurricane Iniki repairs	17,565,657	-	17,565,657
Due to other funds	3,751,880	16,060	3,767,940
Liabilities collateralized by HUD annual contributions	84,145,398	1,529,723	85,675,121
Other liabilities	2,800,244	196,330	2,996,574
Total liabilities	139,732,141	1,917,402	141,649,543
Fund equity:			
Contributed capital:			
Federal government grants	112,954,793	102,724	113,057,517
State of Hawaii grants	759,917	39,488,726	40,248,643
Other	-	423,900	423,900
	113,714,710	40,015,350	153,730,060
Less depreciation on property and equipment acquired or constructed from grants and contributions	73,158,270	7,076,038	80,234,308
	40,556,440	32,939,312	73,495,752
Retained earnings (accumulated deficit)	(10,263,440)	1,675,205	(8,588,235)
Total fund equity	30,293,000	34,614,517	64,907,517
	$ 170,025,141	$ 36,531,919	$ 206,557,060

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Statement of Revenues and Expenses - Enterprise Funds

Year ended June 30, 1993

	Federal Low-Rent Program	Other funds	Total
Operating revenues:			
Rental	$ 14,153,600	$ 4,076,763	$ 18,230,363
Other	418,566	260,338	678,904
	14,572,166	4,337,101	18,909,267
Operating expenses:			
Personal services	6,713,657	1,303,202	8,016,859
Utilities	4,919,074	944,707	5,863,781
Depreciation	4,490,993	744,650	5,235,643
Repairs and maintenance	2,711,322	816,841	3,528,163
Payments in lieu of taxes	1,159,853	-	1,159,853
Insurance	730,361	119,622	849,983
Other	1,498,669	566,779	2,065,448
	22,223,929	4,495,801	26,719,730
Operating loss	(7,651,763)	(158,700)	(7,810,463)
Nonoperating revenues and expenses:			
Insurance proceeds	20,476,022	-	20,476,022
Loss from Hurricane Iniki damages	(20,640,239)	-	(20,640,239)
HUD accrued contribution for interest	5,284,983	-	5,284,983
HUD operating subsidy	3,006,571	-	3,006,571
Interest expense	(5,284,983)	(195,108)	(5,480,091)
Interest income	148,895	54,590	203,485
	2,991,249	(140,518)	2,850,731
Net loss	$ (4,660,514)	$ (299,218)	$ (4,959,732)

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Statement of Fund Equity - Enterprise Funds

Year ended June 30, 1993

	Contributed Capital			Retained Earnings (Accumulated Deficit)		
	Federal Low-Rent Program	Other funds	Total	Federal Low-Rent Program	Other funds	Total
Balances at July 1, 1992, as previously reported	$ 24,134,441	$ 16,422,918	$ 40,557,359	$ (6,231,221)	$ 1,374,450	$ (4,856,771)
Adjustment	-	-	-	(3,862,698)	-	(3,862,698)
Balances at July 1, 1992, as restated	24,134,441	16,422,918	40,557,359	(10,093,919)	1,374,450	(8,719,469)
Net loss	-	-	-	(4,660,514)	(299,218)	(4,959,732)
Transfer of depreciation on property and equipment acquired or constructed from grants and contributions to contributed capital	(4,490,993)	(599,973)	(5,090,966)	4,490,993	599,973	5,090,966
Contributions:						
Federal government	459,586	-	459,586	-	-	-
HUD annual contributions	19,716,156	-	19,716,156	-	-	-
State of Hawaii	737,250	17,116,367	17,853,617	-	-	-
Balances at June 30, 1993	$ 40,556,440	$ 32,939,312	$ 73,495,752	$ (10,263,440)	$ 1,675,205	$ (8,588,235)

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Statement of Cash Flows - Enterprise Funds

Year ended June 30, 1993

	Federal Low-Rent Program	Other funds	Total
Cash flows from operating activities:			
Operating loss	$ (7,651,763)	$ (158,700)	$ (7,810,463)
Adjustments to reconcile operating loss to net cash provided by operating activities:			
Depreciation	4,490,993	744,650	5,235,643
Loss from Hurricane Iniki damages (net of proceeds)	(164,217)	-	(164,217)
HUD operating subsidy	3,006,571	-	3,006,571
Other	-	24,727	24,727
Decrease (increase) in assets:			
Inventory	(69,022)	-	(69,022)
Other receivables	(91,539)	(10,333)	(101,872)
Due from other funds	(34,470)	(61,060)	(95,530)
Due from other governments	(15,778,726)	(28,000)	(15,806,726)
Other assets	(21,848)	16,064	(5,784)
Increase (decrease) in liabilities:			
Vouchers and contracts payable	386,583	(24,297)	362,286
Accrued expenses	3,836	45,487	49,323
Reserve for Hurricane Iniki repairs	17,565,657	-	17,565,657
Due to other funds	(32,422)	13,723	(18,699)
Other liabilities	1,243,899	11,375	1,255,274
Total adjustments	10,505,295	732,336	11,237,631
Net cash provided by operating activities	2,853,532	573,636	3,427,168
Cash flows from capital and related financing activities:			
Payments for capital acquisition	(17,276,069)	(11,717)	(17,287,786)
Principal payments on mortgage loan	-	(30,713)	(30,713)
Receipts from capital grants	19,091,832	-	19,091,832
Receipts from transfer	-	253,500	253,500
Net cash provided by capital and related financing activities	1,815,763	211,070	2,026,833

(Continued)

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Statement of Cash Flows - Enterprise Funds, Continued

		Federal Low-Rent Program		Other funds		Total
Cash flows from investing activities:						
Receipts of interest	$	148,895	$	54,412	$	203,307
Payments of interest		-		(195,108)		(195,108)
Net mortgage escrow deposits		-		(1,973)		(1,973)
Net deposits into reserve for replacement		-		(11,365)		(11,365)
Net deposits into residual receipts reserve		-		(430,397)		(430,397)
Capital expenditures		-		(438)		(438)
Net cash provided by (used in) investing activities		148,895		(584,869)		(435,974)
Net increase in cash and short-term investments		4,818,190		199,837		5,018,027
Cash and short-term investments at beginning of year		3,078,303		1,386,918		4,465,221
Cash and short-term investments at end of year	$	7,896,493	$	1,586,755	$	9,483,248

Schedule of noncash investing, capital and financing activities:

During the current fiscal year, the Federal Low-Rent Program incurred $5,284,983 of interest expense on HUD collateralized debt of which $1,769,622 was paid by HUD. The remaining balance of the interest expense is expected to be forgiven by HUD. The Federal Low-Rent Program also had a reduction in HUD collateralized debt of $1,523,199 which was retired by HUD.

During the current fiscal year, the Housing Revolving Fund, Federal Low-Rent Program, Banyan Street Manor Project and the Teacher Housing Revolving Fund (collectively referred to as the Funds) acquired $2,780,964, $164,605, $2,149,605 and $95,802, respectively, of certain capital assets that were contributed to the Funds by the Capital Projects Fund. In addition, the Housing For Elders Revolving Fund, Teacher Housing Revolving Fund, Federal Low-Rent Program and Housing Revolving Fund acquired $10,967,524, $985,222, $572,645 and $137,250, respectively, of capital assets that were contributed to the Funds by the Housing Finance and Development Corporation. The Federal Low-Rent Program also acquired $459,586 of equipment that was contributed by the Section 8 Existing Fund.

Note 1: Other funds include the Housing Revolving Fund, Teacher Housing Revolving Fund, Housing for Elders Revolving Fund, and Banyan Street Manor Project.

Schedule IX

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Balance Sheet - Trust and Agency Funds

June 30, 1993

	Trust Funds									Agency Funds			
	Donations for Sight Conservation	Helen Keller Affiliation Grant	McInerny Foundation	Nursing Home Long-Term Care	Recruitment of Foster Parents	Commission on the Status of Women	Youth Residential Program	Vocational Rehabilitation Court Appointed Master	Hawaii Housing Authority	Special Deposit	Temporary Deposit	Hawaii Housing Authority	Total
Assets - cash	$ 4,274	$ -	$ 431	$ 11,862	$ 610	$ 2,708	$ 1,179	$ 12,277	$ 1,336,342	$ 184,547	$ 1,103,486	$ 2,050	$ 2,659,766
Liabilities:													
Due to individuals	-	-	-	-	-	-	-	-	-	184,547	-	-	184,547
Due to other funds	-	-	-	-	-	-	-	-	-	-	1,103,486	-	1,103,486
Other liabilities	-	-	-	-	-	-	-	-	-	-	-	2,050	2,050
Total liabilities	-	-	-	-	-	-	-	-	-	184,547	1,103,486	2,050	1,290,083
Reserved fund balances	4,274	-	431	11,862	610	2,708	1,179	12,277	1,336,342	-	-	-	1,369,683
	$ 4,274	$ -	$ 431	$ 11,862	$ 610	$ 2,708	$ 1,179	$ 12,277	$ 1,336,342	$ 184,547	$ 1,103,486	$ 2,050	$ 2,659,766

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Statement of Revenues, Expenditures and Changes in Fund Balances - Trust Funds

Year ended June 30, 1993

	Donations for Sight Conservation	Helen Keller Affiliation Grant	McInerny Foundation	Nursing Home Long-Term Care	Recruitment of Foster Parents	Commission on the Status of Women	Youth Residential Program	Vocational Rehabilitation Court Appointed Master	Hawaii Housing Authority	Total
Intergovernmental revenues - federal	$ 4,844	$ 11,622	$ -	$ -	$ -	$ -	$ 908	$ 378,343	$ 863,505	$ 1,259,222
Expenditures - welfare	5,174	29,598	-	-	-	-	259	366,066	118,658	519,755
Excess of revenues over (under) expenditures	(330)	(17,976)	-	-	-	-	649	12,277	744,847	739,467
Fund balances at July 1, 1992	4,604	17,976	431	11,862	610	2,708	530	-	591,495	630,216
Fund balances at June 30, 1993	$ 4,274	$ -	$ 431	$ 11,862	$ 610	$ 2,708	$ 1,179	$ 12,277	$ 1,336,342	$ 1,369,683

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

Combining Statement of Changes in Assets and Liabilities - Agency Funds

Year ended June 30, 1993

	Balance at July 1, 1992	Additions	Deductions	Balance at June 30, 1993
Special deposit fund:				
Assets - cash	$ 173,132	$ 42,051	$ 30,636	$ 184,547
Liabilities - due to individuals	$ 173,132	$ 42,051	$ 30,636	$ 184,547
Temporary deposit fund:				
Assets - cash	$ 781,405	$ 399,232	$ 77,151	$ 1,103,486
Liabilities - due to other funds	$ 781,405	$ 399,232	$ 77,151	$ 1,103,486
Hawaii Housing Authority:				
Assets - cash	$ 2,941	$ -	$ 891	$ 2,050
Liabilities:				
Due to other funds	1,000	-	1,000	-
Other liabilities	1,941	109	-	2,050
Total liabilities	$ 2,941	$ 109	$ 1,000	$ 2,050
Total - all agency funds:				
Assets - cash	$ 957,478	$ 441,283	$ 108,678	$ 1,290,083
Liabilities:				
Due to individuals	173,132	42,051	30,636	184,547
Due to other funds	782,405	399,232	78,151	1,103,486
Other liabilities	1,941	109	-	2,050
Total liabilities	$ 957,478	$ 441,392	$ 108,787	$ 1,290,083

Responses of the Affected Agencies

Comments on Agency Responses

We transmitted a draft of this report to the Department of Human Services on January 19, 1994. Drafts of the report were transmitted also to the governor, director of finance, and state comptroller. A copy of the transmittal letter to the Department of Human Services is included as Attachment 1. Similar letters were sent to the governor, director of finance, and state comptroller. The response of the Department of Human Services is included as Attachment 2. The responses of the governor, director of finance, and state comptroller are included as Attachments 3, 4, and 5, respectively.

The department generally concurs with our findings and recommendations. It states that it stopped improperly charging appropriations to other programs after receiving the governor's letter dated June 30, 1993. Based on our observations and representations made by department personnel, we believe that the practice still continues. DHS contends that its accounting department has now identified all of these transactions and, had time permitted, KPMG would not have had to declare an exception to the financial statements. The department misses the point—the point is that because of the department's intentional override of controls over its expenditure classifications, its records could not reasonably be verified during the audit. The department does not agree with our findings and recommendations relating to controls over income maintenance programs. It believes that the controls in place are sufficient for its purposes and says that it is not necessary to photocopy all documents reviewed for eligibility. Again, the department misses the point. Our finding is that documentation of the review is not standardized. A standard checklist of documents reviewed would suffice. The department also believes that controls exercised over the HAWI system at ICSD are sufficient and that it relies on ICSD to help maintain security over the system. We believe the additional safeguards available should be used.

The governor has directed the director of finance and the state comptroller to work with the director of human services in addressing the problems noted. The director of finance believes that DHS has discontinued the practice of mischarging program expenditures and will be working with the other departments to address and correct problems noted. The state comptroller also is involved in these efforts and will work to help correct procedural problems.

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

January 19, 1994

COPY

The Honorable Winona E. Rubin, Director
Department of Human Services
1390 Miller Street
Honolulu, Hawaii 96813

Dear Mrs. Rubin:

Enclosed for your information are three copies, numbered 6 to 8 of our draft report, *Financial Audit of the Department of Human Services*. We ask that you telephone us by Friday, January 21, 1994, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Wednesday, January 26, 1994.

The Departments of Accounting and General Services and Budget and Finance, 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

Marion M. Higa
State Auditor

Enclosures

JOHN WAIHEE
GOVERNOR

WINONA E. RUBIN
DIRECTOR

LYNN N. FALLIN
DEPUTY DIRECTOR

LESLIE S. MATSUBARA
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES

P. O. Box 339
Honolulu, Hawaii 96809

January 26, 1994

RECEIVED
JAN 26 4 48 PM '94
OFC. OF THE AUDITOR
STATE OF HAWAII

Ms. Marion Higa
State Auditor
Office of the Auditor
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917

Dear Ms. Higa:

Thank you for the opportunity to review and respond to the report on the Financial Audit of the Department of Human Services prepared by your office. One of the primary objectives of the audit is to assess the adequacy, effectiveness, and efficiency of departmental systems and procedures relative to financial accounting, reporting, and internal controls; and to recommend improvements in these areas. In Fiscal Year 1993, the department experienced major difficulties in ensuring the delivery of timely financial assistance payments and benefits to its clients, and took extraordinary measures to adequately fulfill this departmental mission. Your report has identified the problems and deficiencies that occurred in the past fiscal year, and has presented solid recommendations, many of which the department has already begun to pursue. We are pleased that the auditor has recognized that some of the problems the department has faced relative to budgeting and personnel shortages, which have significantly contributed to some of the deficiencies described in the report, and require the cooperative involvement of the Departments of Budget and Finance, Accounting and General Services, and Personnel.

It should be noted that due to the significance and nature of some of the audit findings, we do need to provide our responses to clarify and expand upon the department's perspective relative to the findings presented in Chapter 2 of the audit report. The department's responses which are presented in the following sections are intended to be constructive in nature, focusing on the improvements we have effected or will effect.

MISCHARGED PROGRAM EXPENDITURES (Page 7)

In order to ensure that the department's clients who depend upon DHS services to sustain at least a minimal quality of life, receive financial assistance on a timely basis, it became of urgent necessity to take drastic measures and charge certain program expenditures to another program. However, the health and welfare of DHS clients were of priority consideration. We recognize that we did not obtain prior approval before making such changes.

The department's primary obligation to deliver essential social and welfare services to recipients is complicated by budgeting and funding constraints. Pages 15 through 17 of the audit report explain how the Medicaid program budget did not adequately provide for the real expenditures of the program. As a parallel, our financial assistance or payment programs also did not receive sufficient appropriations to cover the programs' actual financial requirements. As a result, DHS requested $6,175,152 GF and $4,736,586 FF in emergency appropriations (Act 3, 1993) to carry us through the remainder of the fiscal year. To avoid the same situation for FY 1994, we have allotted a substantial portion of the payment program appropriations to the first three fiscal quarters of this fiscal year and anticipating a shortfall in the fourth quarter, have requested an additional $10,300,139 GF and $7,208,668 FF for our payment programs. On this basis, it is expected that sufficient appropriations will be available to provide for client payments for the entire fiscal year.

It should be noted that we have already implemented the necessary internal fiscal and budgetary procedures, and for this fiscal year, we have not transacted any program charges as described in the audit report. **In this respect, your statement on Page 9 that "despite the Governor's warning and our discussions with DHS, it continues the practice of improperly charging appropriations meant for other programs," is not correct. As of July 1993, we have complied with the Governor's directions stipulated in his letter dated June 30, 1993**.

In regards to the report observation that no records or schedules were kept for the charges, we would like to point out that **our existing regular records were adequate. Through the use of these fiscal documents and reports, the Accounting Staff has accounted for and properly adjusted all significant program charges**. (For example, the transactions related to the temporary use of approximately $3.3 million in Medicaid program funds to cover cash shortages in AFDC were completely reversed by the end of the fiscal year.) As a result, these transactions had no effect on the final expenditures for the quarter and the proper expenditures were reported to the federal agencies.

Although the auditor was of the opinion that the transactions and expenditure totals could not be verified, **we believe that had the circumstances permitted, the determination would be that the program expenditures are reliable and correct**.

<u>**FEDERAL REIMBURSEMENTS**</u> (Page 10)

With respect to lapsing of the federal reimbursements, the Accounting Staff currently has instituted accounting procedures which are performed on a quarterly basis to ensure timely lapsing of federal funds at the conclusion of the fiscal year. We intend to complete the lapsing for FY 1993 by March 15, 1994.

<u>**WELFARE OVERPAYMENTS**</u> (Page 10)

We agree that the DHS efforts regarding the pursuit of welfare overpayments need to be strengthened. We have not effectively implemented a coordinated recovery program focused on aggressive collections. A summary history of the welfare overpayment recovery program shows that we have been placing our attention and efforts mainly on trying to maintain updated account information through our main automated systems (HAWI, ARS), to provide for reporting requirements to federal agencies and to support existing recovery activities such as our state tax intercept program. These efforts include resolving the hardware capacity problems of the IBM System 36, and fixing the interface complications between the Hawaii Automated Welfare Information and Automated Recovery System (HAWI and ARS). The department is aware of the magnitude and composition of the welfare overpayment accounts and we have for the past several years been attempting to conduct a detailed analysis of the information recorded in the two automated systems, to accurately assess the nature and scope of overpayment accounts and generate required data such as accurate accounts receivable aging schedules. The systems, especially the ARS, do have the capability to produce such information and reports. However, at this time, with limited in-house resources and related workload factors, we have not been successful. Our Investigations Office (INVO) has concentrated its limited staff on fraud investigations. Recovery collections of aged accounts have taken a lesser priority for this unit. We realize that we need to refocus and reprioritize our efforts to concentrate on effectively dealing with the substantial overpayment balances that have accumulated since the inception of our welfare programs.

Consequently, the DHS will establish a management team comprised of key decision-making administrators to review the current overpayment recovery activities and policies, and the applicable state and federal regulations and requirements. This team will be tasked to present definitive recommendations and plans to the Director of Human Services by May 1994. Due to the legal aspects involved in overpayment recoveries, we also will be requesting the assistance of the Department of the Attorney General.

CLAIMING OF FEDERAL REIMBURSEMENTS (Page 12)

We agree that we must improve our procedures and processes regarding the claiming of federal reimbursements. During the past fiscal years, the Accounting Staff has experienced high staff turnover in not only key accountant positions but also supporting clerical staff. The audit finding on Page 23 of the report points out that there was a 13.04% vacancy rate for account clerk and accountant positions. Previous auditors of the DHS have observed that the department has one of the most complex and demanding systems of accounting requirements to manage. Under the combination of these circumstances, accounting priorities have been placed upon mandatory federal and state financial reporting requirements, and the management of cash flows to ensure timely payments to clients. Nevertheless, we do concur that the maximization of federal funds must be effectively performed.

The Accounting Staff has already implemented procedures to more efficiently track federal fund drawdowns, claims and expenditures on an individual grant basis. We realize that this represents initial efforts and continuous improvements in this area will be pursued.

IMPREST BANK ACCOUNTS (Page 12)

We agree that, as stated in the audit report, the reconciliation of the welfare imprest bank accounts has not been timely, due to staff vacancies. **However, as of the date of this letter, the major portion of all the bank accounts has been reconciled up to December 1993. This was accomplished mainly by the hiring of emergency hire personnel.**

Regarding the finding on timely replenishments of the bank accounts, we concur with the finding. The imprest funds are used to address emergency situations to provide immediate assistance to the client or the family. The extent of usage of the fund differs from unit to unit. Because of the costs involved in the processing of replenishments, such as staff time to prepare and process replenishment purchase orders at the unit, departmental, and DAGS levels, **we**

will review staffing and other resources to comply with the quarterly replenishment requirement.

QUESTIONABLE ENCUMBRANCES (Page 13)

We generally concur with the finding and have issued budget execution policies and procedures regarding year-end encumbrances effective this fiscal year.

SUBRECIPIENT REVIEWS (Page 14)

We agree that the reviews of the subrecipients have only been partly completed. We have experienced problems relative to timely submittal of audit reports by the subrecipients. For example, one subrecipient suffered damages from a fire on its premises, and therefore the audit reports for two years were not submitted. The department has been pursuing a continuous effort to improve the subrecipient contracting process. **We will be including a requirement in future subrecipient contracts that independent audits be conducted.**

MEDICAID BUDGET (Page 15)

The department concurs with the finding. The DHS will provide to the Department of Budget and Finance (B&F) the actual anticipated Medicaid program expenditures for the next and all future biennium budget periods.

CONTROLS FOR INCOME MAINTENANCE PROGRAMS (Page 18)

Audit Finding 1: Data entry not checked for accuracy. Inaccurate information entered into the HAWI system has resulted in overpayments.

The department does not concur with the finding and recommendation.

Reviewing a budget print does not ensure accuracy of data. Based upon our quality control findings, the department has not experienced problems with the worker entering incorrect data. Rather, the errors and resulting overpayment are caused by incorrect application of policy, failure on the part of the worker to follow up on reported changes, and client's failure to report changes.

The HAWI system limits registration of applications to clerical staff and authorization of payments to income maintenance staff as a security measure for the HAWI system. Similarly, the Action History retained by the system will identify staff who authorized payments or entered data on the client's record and serves as an audit trail.

The AFDC and Food Stamp programs have a high accuracy rate, i.e., 97.3% for AFDC and 96.5% for the food stamp program in FY 1993. The food stamp program has been number one in the nation for accuracy over the past three years and received federal enhanced funding of $3.84 million for this achievement. <u>This accuracy rate is an indicator that staff are making accurate determinations</u>.

There are several on-going periodic reviews conducted for the financial and food stamp programs:

1. Evaluation Office/Quality Control (EVO/QC) is the designated office to conduct quality control reviews on randomly selected cases. The sampling methodology is approved by the federal agencies with oversight for the Aid to Families with Dependent Children (AFDC) and Food Stamp programs to ensure that a representative sample of the population is reviewed. The EVO/QC also conducts quality control reviews for the General Assistance program utilizing similar sampling methodology. Their review includes a review of the case record, an interview with the family, and a review of the HAWI system data;

2. The Income Maintenance supervisors review the work of all unauthorized eligibility workers. Supervisors are also required to review a minimum of one case per authorized Income Maintenance Worker (IMW) each month and may review more cases, if warranted; and

3. The Food Stamp program staff complete management evaluation reviews on selected branches and units on a scheduled basis. The management evaluation includes case reviews.

The above reviews are designed to verify the accuracy of payments and whether staff are correctly implementing policies and procedures. These reviews would identify any irregularities. Similarly, the INVO receives and follows up on complaints. Their investigation includes, a review of the case situation and worker's action. The Program Development Office also conducts periodic reviews on specific eligibility items and would identify irregularities.

The existing staff and fiscal situation precludes the department from implementing a procedure to have all of the estimated 42,000 monthly payment actions reviewed. The recommended caseload size is 170 cases per worker and three applications per day for each application worker. Currently, the department's IM staff are assigned an estimated caseload of 270 to 300 or more cases each month and the application workers are assigned more than three applications per day to process approximately 6,900 applications each month.

By June 1994, the Family and Adult Services Division (FASD) will implement an integrated management evaluation system that will include both the financial and food stamp programs. We are in the process of developing the procedures and forms based on the Alaska integrated management reviews. This will be a more comprehensive review of unit operations and implementation of policies.

Audit Finding 2: Documentation is not standardized as case folders did not contain copies of all documents needed to show compliance with eligibility requirements.

The department does not concur with the finding and recommendation.

FASD has determined that it is not necessary for staff to photocopy verifications submitted by clients. Information is entered on the HAWI system and the verification code will identify the source document. Photocopying of verification is limited to only permanent verification deemed essential and all other verification is documented on agency forms such as the DHS 1266, DHS 1246, and DHS 1241 (HAWI Standard Operating Procedure, D-VI Case File Folder Procedures). **In addition to the instructions in the procedures manual covering the types of records and forms to maintain, an internal memorandum dated April 17, 1991 was issued to instruct staff to "thin out" case files and included guideline for discarding copies of birth verifications and social security numbers**.

The clients declare their citizenship status on the application form and provide documents to verify their citizenship. **In 1993, the financial, food stamp, and medical programs received approval to stop implementing the systematic alien verification to entitlements (SAVE) match with the U. S. Immigration computer file**. It should be noted that the department did not identify any individuals ineligible due to their citizenship status via the SAVE system. This has not been a problem area for the department and we believe staff are verifying the information and documenting on the HAWI system. Staff is discouraged from photocopying clients' identification documents such as immigration papers and passports.

There is no requirement to photocopy documents that prove an individual is residing in Hawaii. The presence of the individual and the information provided by the recipient verify residency. This information is generally obtained during the interview process and coded in the HAWI system. **The elimination of photocopying unnecessary documents is part of the department's efforts to streamline procedures, reduce operational costs, and remove barriers to client's accessing the department's programs**.

Audit Finding 3: Residency is not verified. DHS does not verify that recipients and dependents reside in the same household. DHS does not match the address of the welfare recipient with that of a dependent.

The department is not in full agreement with the finding and recommendation.

The eligibility staff does verify student status for children sixteen years of age or older. Part of the verification includes a request for general information on the child's residence. This is done with the client's consent and cooperation.

There is no known database to match minor dependents against. FASD has tried to implement an automated match with the Department of Education but has been unsuccessful because the data fields and requirements are not compatible. Similarly, many programs do not routinely update addresses as clients move. The DHS updates the address as it affects the mailing of the benefits and notices.

When the eligibility worker does the wage, motor vehicle, and real property checks, the address of the recipients and other adults such as the absent parent is routinely reviewed. When the absent parent uses the same address as the recipient, the department investigates the situation. Further, the FASD had implemented the use of a form DHS 1317, Verification of Household Composition, to verify the continued absence of a parent, but found that this was not an effective process and discontinued the use of the form. Further, when the food stamp program utilized this form, the United States Department of Agriculture, Food and Nutrition Service determined that this exceeded program requirements and could not be used for the food stamp program.

The staff's follow up on suspected misrepresentation of household composition adequately addresses this concern. This has not been an error prone area for the department since the 1980's. Due to fiscal constraints, it would not be practical to incur further administrative expenses related to this issue.

Audit Finding 4: Income verification process is inefficient as four separate Income Eligibility Verification System (IEVS) reports are utilized.

The department concurs with the finding but does not concur with the recommendation.

These reports are generated at different times during the month due to the date the data is received from other agencies. The staff must take action within forty-five days from the date the information is provided to the department. The department cannot delay in sending the information to the staff. Further, there are batch times scheduled to generate the report which may affect the HAWI availability for the IM staff. It is not feasible to consolidate the report, e.g., the staff require immediate information on continuous income such as the unemployment compensation and to delay this report until all the other compensation reports are ready would adversely impact the workload of the staff.

The Program Development-Income Maintenance Section (PD-IMS) has a committee that is reviewing the IEVS requirements with the intent of improving the interface and streamlining the report process. Plans include bringing the data on-line and having the worker input on-line the action taken by the use of codes. The review should be completed by the end of FY 1994 with a determination as to how much automation is needed and what would remain a batch job.

Audit Finding 5: Status of income verification is not reported. The welfare units do not always submit the form DHS 1472, IEVS Report Form, and do not always complete the form properly.

The department concurs with the finding and recommendation in principle.

This is a federal requirement that has generated paperwork and additional workload on an already overburdened staff since implementation in the 1980s. To date, no federal agency has audited the state or provided guidance on the implementation and monitoring requirements.

Although form DHS 1472 is required to monitor the unit's compliance with the IEVS requirements, it has been difficult to do because of the staffing and workload situations at the branches. Generally, completion of the form is a low priority because staff is more focused on providing accurate benefits rather than completing reports.

The corrective action already undertaken by the department includes continued monitoring by the PD-IM staff. A reminder notice will be sent to units that do not report timely. This reporting and monitoring requirement is part of the automation enhancement previously discussed under Audit Finding 4.

ELECTRONIC DATA PROCESSING CONTROLS (Page 21)

We do not concur totally with the audit findings concerning the HAWI System internal security and the use of Protection Log Extract Utility (PLEU) to detect possible improprieties.

There are four (4) types of security software installed on the HAWI System and three (3) are actively utilized. These are the Resource Access Control Facility (RACF), Software AG's Natural System Security, and the HAWI Application System security. All three (3) incorporate utilization of valid user-ID's for access, passwords for authorization, and profiles for clearance levels. The fourth software is the database file level security software, which protects against any access to a specific database file by unauthorized application programs that did not have the correct password. This software is used by mainframes that have multiple application systems within a single CPU, such as the State mainframe. The HAWI system is a single application system within a dedicated mainframe; therefore, this software will not increase the level of security against unauthorized access. **There is only one application system staff who develops and maintains all of the computer programs for the HAWI System and this staff is the only one authorized to know and utilize the file security passwords. Should another application system reside with the HAWI System on this dedicated mainframe, the use of the database file level security software will be expanded to protect the respective application files from authorized use by the other application programs.**

The Protection Log facility is a database management tracking and recovery file. The primary feature of this log is to aid in the recovery of a database file when a system failure occurs. This log is capable of recording before and after images of a data record within a database file. The PLEU is a mainframe based software utilized only by the Database Administrator at the

Department of Budget and Finance, Information and Communication Services Division, Systems Software Branch. The PLEU is executed by the Database Administrator to provide information on how, when, or where recovery is required. The PLEU feature is not accessible to DHS and requests to review this log on a regular basis are not feasible as this log accumulates upwards of a million records per day.

Similarly, the HAWI system does utilize an on-line Action History Screen that is reviewed on a regular basis. This software tracks application modifications and could be utilized to detect any improprieties on a timely basis. The Action History records such as who (security-key), what (which welfare case number and actions taken), and when (date and time) changes were made for auditing purposes.

We agree that the AS/400 is currently under-utilized while being upgraded. In its original purchase state, the amount of disk storage on the AS/400 limited any major application development. Since the IBM System 36 was reaching saturation point, the AS/400 was looked at as a possible replacement for the ARS. The ARS files were transferred to the AS/400. With only the copies of the ARS data files, the AS/400 was at 75% utilization and had to be upgraded. The process to gain proper approvals, funding, and procurement took more than 18 months.

Subsequent upgrades have been made to make the machine more functional. At this time, development and redesign of the ARS is under consideration. but the DHS Information Systems Office has lost two programmer positions that were assigned to the ARS project. We will continue to pursue the use of the AS/400 as the probable replacement for the System 36 that presently houses the ARS, and as the system for the departmental accounting and budget variance reporting applications.

COST ALLOCATION PROCESS (Page 22)

We agree that the present cost allocation procedures are unwieldy and time consuming, even though electronic spreadsheets are utilized. **DHS intends to actively pursue the acquisition and implementation of an integrated software package, as recommended by the audit**.

RENTS FOR OFFICE SPACE (Page 23)

DHS concurs in general with this finding. Under the existing procedures for office space leases and pursuant to HRS 171-30, DHS relies upon the Department of Accounting and General Services (DAGS) to approve all leases and to make the payments. DAGS presently furnishes to DHS a schedule of all active leases which DHS verifies and uses to process reimbursement payments to DAGS. **We maintain our own record of leases and recognize that it should be maintained on a current basis, and this is being done**. Regarding the budgeting of lease rent payments, it should be noted that during the budget process, funding for lease rents were budgeted for by the programs and were removed from the department's budget to be transferred to DAGS. Inadequate documentation among the DHS, DB&F, and DAGS to support the budget transfers contributed to the discrepancies in defining budgeted and non-budgeted lease rents. **We agree that we need to coordinate with DAGS to clearly determine the proper payments and we are pursuing this matter with DAGS**.

STAFF VACANCIES (Page 23)

DHS generally concurs with the findings and recommendations.

EVALUATION OFFICE (Page 24)

DHS concurs in part with the findings and recommendations.

EVO/QC functions have been described earlier on Page 6 of this letter. In addition, the Evaluation Office (EVO) provides program management and fiscal review of the divisions and offices of the department. Its focus in FY 1993 was on the FASD and its branches prior to reorganization steps and the new Self-Sufficiency and Supports Services Division in its early implementation.

The EVO annually contracts with a CPA firm to conduct a financial and compliance audit of the DHS as required by the Single Audit Act of 1984. These audits encompass the financial transactions and internal control systems of the DHS. Additionally, the Evaluation Office-Financial Evaluation (EVO-FE) initiated a review of the imprest funds in December 1993. Also, at the request of the Director, in January 1994 the EVO-FE staff initiated a review of the system of internal controls within the Administrative Services Office.

We recognize that EVO can play a greater role in directly assisting the departmental offices in effecting improvements in fiscal and program operations. Accordingly, we will be pursuing the development of plans in this area.

In closing, we thank you for the opportunity to provide our responses to the audit report. We believe that the audit will constructively serve as a basis to strengthen and improve the DHS's administrative and operational processes.

Sincerely,

Winona E. Rubin

Winona E. Rubin
Director

EXECUTIVE CHAMBERS

HONOLULU

JOHN WAIHEE
GOVERNOR

January 26, 1994

JOSHUA C. AGSALUD
ADMINISTRATIVE DIRECTOR

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

RECEIVED
JAN 26 3 22 PM '94
OFC. OF THE AUDITOR
STATE OF HAWAII

Dear Ms. Higa:

This responds to your letter of January 19, 1994, to Governor Waihee transmitting the draft Financial Audit of the Department of Human Services.

We share your concerns regarding the findings delineated in the report, and we are advised that positive, corrective actions have already been taken to address some of these findings. In addition, the Governor has directed the State Comptroller, the Director of Finance, and the Director of Human Services (see enclosed memoranda) to form a task force to address those identified areas of the audit report which require further discussion and action to resolve.

We appreciate the opportunity to comment on the report. Since the Governor has asked me to assist with the coordination of this inter-departmental effort, please call me if you have any questions regarding this response.

Sincerely,

Joshua C. Agsalud

JOSHUA C. AGSALUD

Enclosures

EXECUTIVE CHAMBERS

HONOLULU

JOHN WAIHEE
GOVERNOR

January 20, 1994

TO: The Honorable Robert P. Takushi, Comptroller
Department of Accounting and General Services

The Honorable Eugene S. Imai, Director
Department of Budget and Finance

The Honorable Winona E. Rubin, Director
Department of Human Services

SUBJECT: Financial Audit of the Department of Human Services Prepared by the Office of the Auditor

As you may be aware, the Office of the Auditor has released a draft "Financial Audit of the Department of Human Services" report. The report noted numerous deficiencies relating to various budgeting, leasing, and accounting practices followed by the Department of Human Services.

In view of the audit findings, I am directing the Departments of Accounting and General Services, Budget and Finance, and Human Services to immediately form a task force to address and correct the deficiencies raised in the report. I am to be periodically apprised of the activities of the task force with respect to specific actions taken to address the deficiencies noted.

Thank you for your cooperation in this matter.

/S/ John Waihee
JOHN WAIHEE

EXECUTIVE CHAMBERS

HONOLULU

JOHN WAIHEE
GOVERNOR

January 20, 1994

TO: The Honorable Winona E. Rubin, Director
Department of Human Services

SUBJECT: Draft "Financial Audit of the Department of Human Services" Report Prepared by the Legislative Auditor

It has come to my attention that certain deficiencies and issues raised by the Auditor in the draft "Financial Audit of the Department of Human Services" have been addressed by your department.

Specifically, I am apprised that the following corrective actions have been taken:

1. Internal fiscal and budgetary procedures have been implemented to prohibit the practice of charging certain program expenditures to another program.

2. Accounting procedures have been instituted which will be conducted on a quarterly basis to ensure the timely lapsing of federal reimbursements.

3. Accounting procedures have been implemented to more efficiently track federal fund drawdowns, claims, and expenditures on an individual grant basis.

4. The acquisition and implementation of an integrated software package for cost allocation procedures is being pursued.

In addition, I am informed that the following areas need further discussion and action to resolve:

1. The aggressive pursuit of welfare overpayments with respect to resolving the hardware capacity problems of the IBM System 36 and the interface complications between the Hawaii Automated Welfare Information System and the Accounts Recovery System.

2. The use of questionable encumbrances to avoid lapsing of funds.

3. The need to submit program budget requests which more closely reflect anticipated Medicaid program expenditures.

4. The coordination of lease agreements with respect to lease rental payments.

I have directed the Departments of Accounting and General Services and Budget and Finance to provide assistance in resolving the aforementioned areas which still need to be addressed.

Your cooperation in this matter is appreciated.

/S/ John Waihee

JOHN WAIHEE

c: Honorable Robert P. Takushi
Honorable Eugene S. Imai

ATTACHMENT 4

JOHN WAIHEE
GOVERNOR

EUGENE S. IMAI
DIRECTOR

BARBARA KIM STANTON
DEPUTY DIRECTOR

CELIA L. JACOBY
DEPUTY DIRECTOR

EMPLOYEES' RETIREMENT SYSTEM
HAWAII INC
HAWAII PUBLIC EMPLOYEES HEALTH FUND
HOUSING FINANCE AND DEVELOPMENT CORPORATION
OFFICE OF THE PUBLIC DEFENDER
PUBLIC UTILITIES COMMISSION

STATE OF HAWAII
DEPARTMENT OF BUDGET AND FINANCE
STATE CAPITOL
P.O. BOX 150
HONOLULU, HAWAII 96810-0150

BUDGET, PROGRAM PLANNING AND MANAGEMENT DIVISION
FINANCIAL PLANNING AND POLICY DEVELOPMENT DIVISION
INFORMATION AND COMMUNICATION SERVICES DIVISION
TREASURY OPERATIONS DIVISION

January 26, 1994

RECEIVED
JAN 26 3 59 PM '94
OFC. OF THE AUDITOR
STATE OF HAWAII

Ms. Marion M. Higa
State Auditor
Office of the Auditor
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917

Dear Ms. Higa:

Subject: Comments on "Financial Audit of the Department of Human Services"

Thank you for the opportunity to comment on the recommendations made in your draft "Financial Audit of the Department of Human Services, A Report to the Governor and the Legislature of the State of Hawaii."

With respect to your first recommendation that the Governor charge the Director of Human Services, the Comptroller, and the Director of Finance with the responsibility for ensuring that the Department of Human Services adheres to State budgeting and accounting requirements, please be informed that the Governor has directed the Departments of Human Services (DHS), Accounting and General Services (DAGS), and Budget and Finance (B&F) to form a task force to address the issues raised in the report.

In addition, this office would like to make the following comments regarding the text of the report:

1. It is our understanding that the practice of mischarging program expenditures (as described beginning on page 7 of the report) has been discontinued by the DHS as of July 1, 1993. Any funding shortages in the DHS programs will be covered through transfers of funds pursuant to provisions of the General Appropriations Act. Shortfalls in FY 1994 in the Aid to Families with Dependent Children and General Assistance payment programs have been identified and the administration is submitting legislation to address these deficits.

2. The DHS has indicated that they plan to implement internal controls to mitigate the practice of using federal reimbursements to finance program expenditures as described on page 10 of the report.

3. With respect to controlling welfare overpayments (page 10), this department's Information and Communication Services Division (ICSD) has discussed, with the DHS, the matter of developing a computerized system to identify overpayments made to welfare recipients. Based on this discussion, it appears that the DHS' Information Systems Office (ISO) will be able to develop the necessary computer software based on the report requirements identified by the DHS. Development of such a software should lend to the DHS' ability to identify overpayments on a timely basis and to subsequently pursue such overpayments. The ICSD will assist the ISO in developing the software.

4. With respect to the Medicaid budget request for the FB 1993-95, page 17 of the report states that the Executive request to fund a projected shortfall of $55 million in FY 1994 and $82 million in FY 1995 should have been included as part of the Executive Budget for FB 1993-95 and not submitted as a message item to the 1993 Legislature. It is noted that the Governor's message, which prefaces the "Multi-Year Program and Financial Plan and Executive Budget For the Period 1993-1999," (submitted to the Legislature on December 21, 1992) indicated that at the time the budget document was prepared, the shortfalls were projected to be $73 million in FY 1994 and $117.6 million for FY 1995. These figures were not included in the Governor's FB 1993-95 budget as this office was working with the staff of the DHS to refine the budget requirements based on several cost saving measures which the DHS was considering at the time. These discussions resulted in the lower amounts ($55 million/$82 million) submitted in the message to the Legislature. We will also be working with the DHS in reviewing their methodology of projecting Medicaid and AFDC requirements.

5. The DHS' ISO staff is working with the staff of the ICSD to review, evaluate, and identify security levels and options in addressing the concerns noted beginning on page 21 of the report.

It is apparent that the DHS has already taken, or is in the process of taking, positive actions to address the deficiencies identified in the Auditor's report. As noted earlier, however, this department and the DAGS will work with the DHS in implementing the corrective actions to ensure future compliance with applicable administrative and statutory requirements.

Thank you again for the opportunity to comment on the draft "Financial Audit of the Department of Human Services."

Sincerely,

Eugene S. Imai

EUGENE S. IMAI
Director of Finance

JOHN WAIHEE
GOVERNOR

ROBERT P. TAKUSHI
COMPTROLLER

LLOYD I. UNEBASAMI
DEPUTY COMPTROLLER

STATE OF HAWAII
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES
P.O. BOX 119
HONOLULU, HAWAII 96810-0119

January 26, 1994

RECEIVED
JAN 26 5 01 PM '94
OFC. OF THE AUDITOR
STATE OF HAWAII

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

Dear Ms. Higa:

Thank you for the opportunity to review and respond to the report on the Financial Audit of the Department of Human Services (DHS) as it relates to the Department of Accounting and General Services (DAGS).

The DAGS' Leasing Services Branch provides DHS with original copies of all executed office leases for DHS' use in monitoring leases.

Regarding lease payments, DAGS allocates budgeted lease rents to the appropriate DHS programs and makes the payments. In cases of new leases executed after the initial budget cycle, DHS pays lessors directly out of its own funds until such time that funds are transferred to and budgeted in DAGS. DAGS provides a quarterly schedule of all leases to DHS and the bill for reimbursements due DAGS.

DAGS recognizes this dual procedure appears confusing and we intend to take steps to better communicate and coordinate with the appropriate DHS and Department of Budget and Finance (B&F) staff. To ensure proper allocations and timely payments and to better track the status of lease payments, DAGS is part of a task force that has been formed with B&F and DHS and is meeting to discuss and implement ways to correct procedural differences.

Again, thank you for the opportunity to provide our comments. If you or your staff have any questions on this matter, please call me at 586-0400.

Very truly yours,

Robert P. Takushi
State Comptroller