

**State of Hawaii**  
**Department of Health**  
Financial and Compliance Audit  
June 30, 2009

**Submitted by**  
**The Auditor**  
**State of Hawaii**

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Department of Health  
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## Report of Independent Auditors

The Auditor  
State of Hawaii

In our opinion, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Hawaii, Department of Health (the "Department") which collectively comprise the Department's basic financial statements as listed in the index, present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Department at June 30, 2009, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Department's management. Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the basic financial statements of the Department are intended to present the financial position and the changes in financial position and cash flows, where applicable, of only that portion of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Hawaii that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State of Hawaii as of June 30, 2009, or the changes in its financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 10 to the basic financial statements, certain errors resulting in the overstatement of the previously reported governmental activities' net assets and governmental funds' fund balance as of June 30, 2008, were discovered by management of the Department during fiscal year 2009. Accordingly, the fiscal year 2008 financial statements have been restated and an adjustment has been made to the department-wide net assets and governmental funds' fund balance as of July 1, 2008 to correct the errors.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 25, 2010 on our consideration of the Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The accompanying management's discussion on pages 3 through 13 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. As described in Note 1 to the Schedule of Expenditures of Federal Awards, the accompanying Schedule of Expenditures of Federal Awards was prepared on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects on the basis of accounting described in Note 1, in relation to the basic financial statements taken as a whole.

*Accuity LLP*

Honolulu, Hawaii  
March 25, 2010

**State of Hawaii**  
**Department of Health**  
**Management's Discussion and Analysis (Unaudited)**  
**June 30, 2009**

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This Management Discussion and Analysis ("MD&A") presents a narrative overview and analysis of the financial activities and performance of the State of Hawaii, Department of Health (the "Department") during the fiscal year that ended on June 30, 2009. Please read it in conjunction with the Department's Financial Statements including its related notes (which follow this section) as well as the subsequent Schedule of Expenditures of Federal Awards ("SEFA"). The following is a brief description of the contents of those three sections:

**Overview of the Financial Statements**

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

***Department-wide Financial Statements***

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

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

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

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

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

***Fund Financial Statements***

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

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

The fund financial statements also include the budgetary comparison statements, which include reconciliations for the general fund, tobacco settlement fund, and deposit beverage container fund, comparing the excess of revenues over expenditures presented on a budgetary basis to the excess (deficiency) of revenues over expenditures presented in conformity with generally accepted accounting principles ("GAAP") as presented in the governmental fund financial statements.

To reiterate, the Department has three types of funds:

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

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

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

**Notes to Financial Statements**

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

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**Schedule of Expenditures of Federal Awards**

Other information consists of the Schedule of Expenditures of Federal Awards and the Notes to the Schedule of Expenditures of Federal Awards. The SEFA reports federal awards to the Department expended on the cash basis of accounting for the year ended June 30, 2009.

**Financial Highlights**

- The financial information for fiscal year ("FY") 2008 has been restated to correct the deposit beverage container liability as previously reported in the Department's FY 2008 financial statements. The FY 2008 amounts in the MD&A are the restated balances (see Note 10).
- The Department's total net assets increased from \$613.1 million (as restated) as of June 30, 2008 to \$625.6 million as of June 30, 2009, or by approximately \$12.5 million. The total increase in net assets was attributed to an increase in the Department's business type activities' net assets of \$23.3 million and offset by a decrease in governmental activities' net assets of \$10.8 million during the year.
- The Department's governmental funds reported an aggregate decrease in fund balance of approximately \$4.9 million during the year totaling \$118.4 million at June 30, 2009. Note that this is based on the adjusted fund balance at July 1, 2008 of \$123.3 million.
- The Department's proprietary funds, consisting of two revolving loan funds, reported an increase in net assets of \$23.3 million for FY 2009. Total net assets were \$457.1 million at June 30, 2009 compared to the FY 2008 year end total of \$433.8 million.

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**Department-Wide Financial Analysis**

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

**Statement of Net Assets**  
**June 30, 2009**  
**(\$000)**

	<b>Governmental Activities</b>		<b>Business-Type Activities</b>		<b>Total</b>	
	<b>2009</b>	<b>2008 (restated)</b>	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008 (restated)</b>
Current assets	\$ 262,115	\$ 279,749	\$ 172,610	\$ 208,285	\$ 434,725	\$ 488,034
Capital assets	64,144	64,173	272	365	64,416	64,538
Loans receivable, noncurrent	-	-	285,151	226,015	285,151	226,015
<b>Total assets</b>	<b>\$ 326,259</b>	<b>\$ 343,922</b>	<b>\$ 458,033</b>	<b>\$ 434,665</b>	<b>\$ 784,292</b>	<b>\$ 778,587</b>
Current liabilities	\$ 140,118	\$ 148,336	\$ 305	\$ 429	\$ 140,423	\$ 148,765
Long term liabilities	17,628	16,295	599	377	18,227	16,672
<b>Total liabilities</b>	<b>157,746</b>	<b>164,631</b>	<b>904</b>	<b>806</b>	<b>158,650</b>	<b>165,437</b>
<b>Net assets</b>						
Invested in capital assets	64,144	64,173	272	365	64,416	64,538
Restricted	123,714	136,536	456,857	433,494	580,571	570,030
Unrestricted	(19,345)	(21,418)	-	-	(19,345)	(21,418)
<b>Total net assets</b>	<b>168,513</b>	<b>179,291</b>	<b>457,129</b>	<b>433,859</b>	<b>625,642</b>	<b>613,150</b>
<b>Total liabilities and net assets</b>	<b>\$ 326,259</b>	<b>\$ 343,922</b>	<b>\$ 458,033</b>	<b>\$ 434,665</b>	<b>\$ 784,292</b>	<b>\$ 778,587</b>

As noted earlier, changes in net assets may serve over time as a useful indicator of the Department's financial position. As of June 30, 2009, the Department's total net assets were approximately \$625.6 million.

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At June 30, 2009, in addition to cash in the state treasury approximating \$298.5 million, the Department had total loans receivable from county governments in the amount of \$309.5 million arising from its two revolving loan funds. The Department had total liabilities of \$158.6 million at June 30, 2009 of which \$11.5 million relates to accrued wages and employee benefits payable. Approximately \$68.2 million in liabilities relate to vouchers and contracts payable. At June 30, 2009, restricted net assets were \$580.6 million. The restrictions arise from legal and contractual agreements.

**Statement of Activities**  
**June 30, 2009**  
**(\$000)**

	<b>Governmental Activities</b>		<b>Business-Type Activities</b>		<b>Total</b>	
	<b>2009</b>	<b>2008 (restated)</b>	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008 (restated)</b>
<b>Revenue</b>						
<b>Program revenues</b>						
Charges for services	\$ 54,458	\$ 54,055	\$ 6,936	\$ 6,582	\$ 61,394	\$ 60,637
Operating grants and contributions	81,235	118,465	16,134	21,407	97,369	139,872
<b>General revenues</b>						
State appropriated funds	441,046	463,574	-	-	441,046	463,574
Non imposed fringe benefits	53,273	48,308	-	-	53,273	48,308
Tobacco settlement funds	60,008	55,713	-	-	60,008	55,713
Environmental fees and taxes	29,293	25,264	-	-	29,293	25,264
Total revenues	<u>719,313</u>	<u>765,379</u>	<u>23,070</u>	<u>27,989</u>	<u>742,383</u>	<u>793,368</u>
<b>Expenses</b>						
General administration	32,461	31,899	-	-	32,461	31,899
Environmental health	72,848	64,825	3,126	3,771	75,974	68,596
Behavior health	300,377	297,791	-	-	300,377	297,791
Health resources	285,163	294,437	-	-	285,163	294,437
Total expenses	<u>690,849</u>	<u>688,952</u>	<u>3,126</u>	<u>3,771</u>	<u>693,975</u>	<u>692,723</u>
Excess before transfers	28,464	76,427	19,944	24,218	48,408	100,645
Transfers	<u>(39,242)</u>	<u>(86,220)</u>	<u>3,326</u>	<u>2,666</u>	<u>(35,916)</u>	<u>(83,554)</u>
Change in net assets	(10,778)	(9,793)	23,270	26,884	12,492	17,091
<b>Net assets</b>						
Beginning of year, as restated	<u>179,291</u>	<u>189,084</u>	<u>433,859</u>	<u>406,975</u>	<u>613,150</u>	<u>596,059</u>
End of year	<u>\$ 168,513</u>	<u>\$ 179,291</u>	<u>\$ 457,129</u>	<u>\$ 433,859</u>	<u>\$ 625,642</u>	<u>\$ 613,150</u>

Governmental activities decreased the Department's net assets by \$10.8 million in FY 2009. There was a decrease in the State appropriated funds of \$22.5 from FY 2008 to FY 2009. The decrease was due in part to the emergency appropriations the Department received in FY 2008 in the amount of \$10 million for the adult mental health program to cover increased service costs, and a decrease of approximately \$8.0 million related to the reduction in revenues from capital projects funds. Also in FY 2009, the Department was assessed approximately \$5.9 million in restrictions.

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Revenues of the Department's business-type activities, which decreased by \$4.9 million from 2008, consist of the Department's environmental loan programs — one for water pollution control and the other for drinking water treatment — were generated from charges for services, program investment income, and federal assistance program funds as well as state matching funds. Charges for services consist primarily of administration loan fees and interest income on loans related to the Department's two revolving loan programs. The majority of the programs investment loss is from the Department's participation in the State Treasury Investment Pool System.

For the fiscal year ended June 30, 2009, business-type activities increased the Department's net assets by \$19.9 million before transfers whereas in FY 2008, the increase was \$24.2 million before transfers.

Total Department-wide expenses for FY 2009 were \$694.0 million of which \$690.8 million was for governmental activities. Overall the Department is organized into four major administrations.

Financially, the largest administration is the Behavioral Health Services Administration that expended a significant 43.5% of departmental funds with an increase of \$2.6 million over FY 2008. This administration is responsible for providing available and coordinated mental health and substance abuse treatment and prevention programs. Programs within this administration are:

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

A portion of the increase in expenditures is attributed to the AMHD's continuing efforts to identify, place and treat eligible clients. In FY 2009, AMHD serviced 15,722 clients as compared to the 15,586 clients serviced in FY 2008. AMHD's Access Line continues to provide the community with a resource site for information as well as a referral point for possible clients. CAMHD continues to respond to the ongoing requirements of the settled Felix case, while ADAD is still responsible for implementing the "Ice" (nickname for methamphetamine) initiative.

The Health Resources Administration expended approximately 41.3% of all expenses. FY 2009 expenditures for this Administration decreased \$9.3 million over FY 2008. Major programs included in this administration include:

- Developmental Disabilities Division ("DDD") that services disabled clients in Hawaii while addressing the conditions of the Makin Settlement;
- Family Health Services Division ("FHSD") that administers the State's Early Intervention program for children zero to three in compliance with the Federal Individual with Disabilities Education Act, Part C as well as serving children, youth and families through its three branches, namely, Children with Special Health Needs, Maternal and Child Health, and Women Infants and Children;
- Community Health Division that provides Public Health Nursing Services, which in concert with the two programs of the FHSD continues to provide services necessary to meet the requirements of the settled Felix lawsuit, and the chronic disease management and control program;

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- Emergency Medical Services and Injury Prevention System Branch that includes the State's mandated Emergency Medical Services, which operates the State's emergency ambulance service in the four major counties, and the injury prevention program;
- Tobacco Settlement Project/Healthy Hawaii Initiative ("TSP/HHI") program which seeks to prevent chronic diseases such as heart disease, cancer and diabetes utilizing tobacco settlement funds for programs that work to decrease tobacco use, improve nutrition and promote physical activities;
- Communicable Disease Division which provides tuberculosis control, Hansen's disease control programs in the community and at Kalaupapa, and STD/AIDS prevention services;
- Disease Outbreak Control Division which provides immunization and disease investigation services as well as provides emergency response to disease outbreaks and potential acts of bioterrorism;
- Dental Health Division which is the smallest division in this administration and implements a dental hygiene program in the public schools and provides public health dental services to the State's disabled clientele.

This administration provides a wide array of public health services in addition to meeting the court settlement conditions, which results in the expenditure of a high percentage of departmental funds. The decrease in expenditures in FY 2009 as compared to FY 2008 resulted primarily from the \$4.7 million restriction assessed against programs in this administration. Further, the expenditures for the DDD decreased by \$6.4 million in FY 2009 as compared to FY 2008 due in part to an increase in the Federal Medical Assistance Percentage ("FMAP") and reductions in the clients' waiver budgets.

The Environmental Health Administration is responsible for the management of the clean air, clean water, solid and hazardous waste, public health sanitation, vector control, and purity of food and drugs. It expended approximately 10.5% of the departmental funds with an increase of \$8.0 million expended over FY 2008. This increase in expenditures is mainly due to the public's continued acceptance and increasing participation in the Deposit Beverage Container Program. This program continues to expand every year with increasing amounts being recycled resulting in related costs increasing. This increase is reflected in the rising redemption rates for recycling beverage containers. In FY 2009, the redemption rate increased to 79% with 705,156,511 beverage containers redeemed as compared to a 72% redemption rate in FY 2008, with 681,706,599 beverage containers redeemed. Other programs in this administration are heavily federally funded through the Environmental Protection Agency. This administration also manages both the Water Pollution Control Revolving and the Drinking Water Treatment Revolving Loan Funds.

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

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The following table presents revenues and expenditures of the governmental funds for FY 2009 and FY 2008 (\$000):

	<b>2009</b>	<b>2008</b> <b>(restated)</b>
<b>Revenues</b>		
State general fund allotments	\$ 441,046	\$ 463,574
Nonimposed fringe benefits	53,273	48,308
Tobacco settlement funds	60,109	56,891
Deposit beverage container program	17,789	18,919
Intergovernmental	123,579	114,325
Taxes, fees, fines and other	28,255	62,730
Investment loss	<u>(5,592)</u>	<u>2,027</u>
Total revenues	<u>718,459</u>	<u>766,774</u>
<b>Expenditures</b>		
General administration	31,893	32,459
Environmental health	71,205	64,041
Behavioral health	298,491	296,744
Health resources	<u>283,881</u>	<u>385,889</u>
Total expenditures	<u>685,470</u>	<u>779,133</u>
Excess (deficiency) of revenues over expenditures before transfers	<u>\$ 32,989</u>	<u>\$ (12,359)</u>

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

During the fiscal year ended June 30, 2009, general fund revenues were \$490.7 million, including \$53.3 million for fringe benefits paid directly from the State general fund. General fund expenditures were \$481.3 million, including the \$53.3 million for fringe benefits discussed above.

For FY 2009, the tobacco settlement fund earned revenues of \$58.2 million, including an investment loss of \$1.9 million. \$43.7 million was transferred to other State departments and agencies of which \$10.6 million was for the State's Emergency and Budget Reserve Fund (a.k.a. Rainy Day Fund), \$11.9 million was for the University of Hawaii to pay debt service on revenue bonds to support construction of a new health and wellness center, to include a new medical school and bio research center in Kakaako, and \$20.0 million was required to be transferred to the State's General Fund in accordance with Act 79/90.

In FY 2009, the deposit beverage container fund earned \$17.8 million in beverage container deposit administrative fees and unredeemed containers. Of this amount received, \$24.5 million was paid to recycling centers, or utilized to fund the program. The bottle bill fund collected \$44.4 million in deposits from distributors and repaid \$37.5 million in deposits to consumers during FY 2009.

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

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The Water Pollution Control Revolving Fund accounts for federal and state funds used to provide loans to county governments for the construction of wastewater treatment facilities and the repayment of principal, interest and fees from such loans and investment of such monies. During FY 2009, this fund received \$12.1 million and \$1.7 million of federal and state funds, respectively. The fund also disbursed \$76.0 million in loan proceeds and collected \$21.0 million in principal repayments in 2009. As compared to 2008, the fund collected \$8.8 million and \$1.0 million in federal and state contributions, and disbursed \$24.4 million in loan proceeds and collected \$15.5 million in principal payments.

The Drinking Water Treatment Revolving Loan Fund accounts for federal and state match funds used to provide loans and other types of financial assistance to public water systems for drinking water infrastructure and the repayment of principal interest and fees from such loans and the investment of such monies. During FY 2009, this fund received \$9.1 million and \$1.7 million of federal and state funds, respectively. The fund also disbursed \$10.0 million in loan proceeds and collected \$3.1 million in principal repayments in 2009. As compared to 2008, the fund disbursed \$11.1 million in loan proceeds and collected \$2.3 million in principal payments.

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

**Budgetary Analysis**

The following budget information relates to the general fund, tobacco settlement fund, and deposit beverage container fund for 2009:

	<b>Budgeted Amounts (\$000)</b>		<b>Actual on a Budgetary Basis (\$000)</b>
	<b>Original</b>	<b>Final</b>	
<b>General fund</b>			
Revenues	\$ 444,944	\$ 456,535	\$ 441,314
Expenditures			
General administration	17,644	20,505	18,015
Environmental health	20,368	20,102	19,576
Behavioral health	205,752	210,842	208,060
Health resources	201,180	205,086	195,663
<b>Tobacco settlement fund</b>			
Revenues	53,847	53,900	61,154
Expenditures	53,847	53,900	56,211
<b>Deposit beverage container fund</b>			
Revenues	71,106	71,124	53,950
Expenditures	71,106	71,124	63,800

The differences between the original budgeted appropriation and actual expenditures for the general fund were due mainly to the restrictions imposed upon the Department in FY 2009.

For the tobacco settlement fund, the actual expenditures of \$56.2 million in FY 2009 were \$5.0 million less than the actual revenues received. The Tobacco Settlement Project received an increase in revenues in FY 2009 from the Master Settlement Agreement due to Hawaii's participation in the strategic contribution fund.

**State of Hawaii**  
**Department of Health**  
**Management's Discussion and Analysis (Unaudited)**  
**June 30, 2009**

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The deposit beverage container program recognized revenues from the program's beverage container deposit administrative fees and unredeemed deposits of \$17.8 million, which is based on the actual number of containers sold. In fiscal year 2008, there were 947,692,357 containers sold. The amount of containers sold decreased to 895,737,097 in fiscal year 2009.

**Capital Assets**

As of June 30, 2009, the Department's governmental activities had invested approximately \$64.1 million (net of accumulated depreciation) in a broad range of capital assets. See Note 4 to the Department's financial statements for a description of capital assets activities for the fiscal year ended June 30, 2009.

<b>Capital Assets</b>		
<b>Governmental Activities</b>		
<b>June 30, 2009</b>		
<b>(\$000)</b>		
	<b>2009</b>	<b>2008</b>
Land	\$ 1,018	\$ 1,018
Land and building improvements	138,312	134,145
Furniture and equipment	22,272	21,704
Total	161,602	156,867
Accumulated depreciation	97,458	92,694
Total capital assets, net	\$ 64,144	\$ 64,173

**Currently Known Facts, Decisions, or Conditions**

The effects of the slow down in the State's economy compounded the Department's challenge to continue to provide needed services to ensure the overall health and safety of the people of our state, especially in the areas of mental health and developmental disabilities.

The Department has continued to evaluate and monitor the statewide service delivery system of the adult mental health program in order to improve service delivery and to contain operational costs. However, the number of consumers with severe and persistent mental illness continues to increase. The number of adult consumers increased from 15,586 in FY 2008 to 15,722 in FY 2009.

In the developmental disabilities program, the number of clients increased by 55 clients in FY 2009. In FY 2009, the program served 2,581 clients in the home and community-based waiver program. Further, the Federal Medical Assistance Percentage ("FMAP") decreased from 56.50% to 55.11% effective October 1, 2008. The FMAP was later amended to 66.13% retroactively for the period October 1, 2008 through March 31, 2009. For the period April 1, 2009 through September 30, 2009, the FMAP was increased to 67.35%. The FY 2009 year-end Average Cost per Client ("APC") decreased to \$41,527 as compared to the FY 2008 year-end APC of \$42,316. Faced with the prospect of serving more clients with reduced funding due to the State's economic downturn, program management reevaluated the program and its services to achieve operational efficiencies.

**State of Hawaii**  
**Department of Health**  
**Management's Discussion and Analysis (Unaudited)**  
**June 30, 2009**

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And lastly, the Water Pollution Control Revolving Fund ("WPCRF") and the Drinking Water Treatment Revolving Loan Fund ("DWTRLF") executed a total of 8 loan agreements in the amount of \$30.3 million and 4 loan agreements for \$12 million, respectively, during FY 2009. Also, in FY 2010, the WPCRF executed 7 American Recovery and Reinvestment Act ("ARRA") loan agreements in the amount of \$29.8 million and the DWTRLF executed 9 loan agreements for \$19.5 million. Further, the WPCRF expects to execute a total of 8 loan agreements in the amount of \$50.3 million while the DWTRLF expects to execute a total of 14 loan agreements for \$51.4 million in FY 2010.

**State of Hawaii**  
**Department of Health**  
**Department-wide – Statement of Net Assets**  
**June 30, 2009**

	<b>Governmental Activities</b>	<b>Business-Type Activities</b>	<b>Total</b>
<b>Assets</b>			
Current assets			
Equity in cash and cash equivalents and investments in State Treasury	\$ 153,411,626	\$ 145,030,272	\$ 298,441,898
Receivables			
Due from State Treasury	53,509,625	-	53,509,625
Due from other State agencies	19,970,000	-	19,970,000
Accrued interest and loan fees	1,407,800	3,231,949	4,639,749
Accounts receivable	1,647,161	-	1,647,161
Due from Federal government	5,269,245	20,677	5,289,922
Tobacco settlement receivable	26,900,000	-	26,900,000
Current maturities of loans receivable	-	24,326,690	24,326,690
	<u>108,703,831</u>	<u>27,579,316</u>	<u>136,283,147</u>
Total current assets	262,115,457	172,609,588	434,725,045
Loans receivable, net of current maturities	-	285,150,636	285,150,636
Capital assets, net of accumulated depreciation	<u>64,143,715</u>	<u>272,366</u>	<u>64,416,081</u>
Total assets	<u>\$ 326,259,172</u>	<u>\$ 458,032,590</u>	<u>\$ 784,291,762</u>
<b>Liabilities and Net Assets</b>			
Current liabilities			
Vouchers and contracts payable	\$ 68,042,625	\$ 139,970	\$ 68,182,595
Accrued wages and employee benefits payable	11,406,475	100,826	11,507,301
Accrued vacation, current portion	9,392,557	63,772	9,456,329
Workers' compensation liability	403,758	-	403,758
Deferred income	1,333,606	-	1,333,606
Due to State of Hawaii	37,040	-	37,040
Due to other State Agencies	29,816,296	-	29,816,296
Beverage container deposits	<u>19,685,339</u>	<u>-</u>	<u>19,685,339</u>
Total current liabilities	140,117,696	304,568	140,422,264
Accrued vacation, net of current portion	17,627,793	222,632	17,850,425
Other postemployment benefits	<u>-</u>	<u>376,038</u>	<u>376,038</u>
Total liabilities	157,745,489	903,238	158,648,727
Commitments and contingencies			
Net assets			
Investment in capital assets	64,143,715	272,366	64,416,081
Restricted for			
Loans	-	456,856,986	456,856,986
Tobacco prevention and control	37,627,722	-	37,627,722
Capital projects	7,972,142	-	7,972,142
Other purposes	78,114,686	-	78,114,686
Unrestricted	<u>(19,344,582)</u>	<u>-</u>	<u>(19,344,582)</u>
Total net assets	<u>168,513,683</u>	<u>457,129,352</u>	<u>625,643,035</u>
Total liabilities and net assets	<u>\$ 326,259,172</u>	<u>\$ 458,032,590</u>	<u>\$ 784,291,762</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii  
Department of Health  
Department-wide – Statement of Activities  
Year Ended June 30, 2009**

Functions/Programs	Program Revenues			Net (Expense) Revenue and Changes in Net Assets		
	Expenses	Charges for Services	Operating Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Primary government						
Governmental activities						
General administration	\$ 32,461,373	\$ 382,989	\$ 8,801,069	\$ (23,277,315)	\$ -	\$ (23,277,315)
Environmental health administration	72,848,175	5,451,967	9,183,536	(58,212,672)	-	(58,212,672)
Behavioral health services administration	300,377,024	38,642,607	18,275,511	(243,458,906)	-	(243,458,906)
Health resources administration	285,162,734	9,980,370	44,974,949	(230,207,415)	-	(230,207,415)
Total governmental activities	690,849,306	54,457,933	81,235,065	(555,156,308)	-	(555,156,308)
Business-type activities						
Environmental health loan programs	3,126,025	6,936,502	16,134,221	-	19,944,698	19,944,698
Total business-type activities	3,126,025	6,936,502	16,134,221	-	19,944,698	19,944,698
Total primary government	\$ 693,975,331	\$ 61,394,435	\$ 97,369,286	(555,156,308)	19,944,698	(535,211,610)
General revenues						
State general fund allotments, net				441,045,812	-	441,045,812
Nonimposed employee fringe benefits				53,273,241	-	53,273,241
Environmental response tax				1,441,439	-	1,441,439
Deposit beverage container fee				17,789,475	-	17,789,475
Advance glass disposal fee				653,406	-	653,406
Tobacco tax				9,408,869	-	9,408,869
Tobacco settlement funds				60,008,380	-	60,008,380
Transfers				(39,242,033)	3,326,000	(35,916,033)
Total general revenues and transfers				544,378,589	3,326,000	547,704,589
Change in net assets				(10,777,719)	23,270,698	12,492,979
Net assets at July 1, 2008, as previously reported				185,271,217	433,858,654	619,129,871
Prior period adjustment				(5,979,815)	-	(5,979,815)
Net assets at July 1, 2008, as restated				179,291,402	433,858,654	613,150,056
Net assets at June 30, 2009				\$ 168,513,683	\$ 457,129,352	\$ 625,643,035

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Governmental Funds – Balance Sheet**  
**June 30, 2009**

	General	Tobacco Settlement	Deposit Beverage Container	Other Funds	Total Governmental
<b>Assets</b>					
Equity in cash and cash equivalents and investments in State Treasury	-	\$ 40,006,724	\$ 32,902,320	\$ 80,502,582	\$ 153,411,626
Due from State Treasury	45,336,390	-	-	8,173,235	53,509,625
Due from other State agencies	-	-	-	14,678,000	14,678,000
Internal balances	7,985,000	-	-	(7,985,000)	-
Accounts receivable	-	-	1,647,161	-	1,647,161
Due from Federal government	-	-	-	5,269,245	5,269,245
Total assets	<u>\$ 53,321,390</u>	<u>\$ 40,006,724</u>	<u>\$ 34,549,481</u>	<u>\$ 100,638,062</u>	<u>\$ 228,515,657</u>
<b>Liabilities and Fund Balances</b>					
<b>Liabilities</b>					
Vouchers and contracts payable	\$ 35,008,513	\$ 6,923,609	\$ 4,046,037	\$ 18,701,966	\$ 64,680,125
Accrued wages and employee benefits	9,249,899	76,671	28,802	2,051,103	11,406,475
Deferred income	-	-	-	1,333,606	1,333,606
Due to State of Hawaii	37,040	-	-	-	37,040
Due to other State agencies	6,470,464	2,103,722	-	4,429,610	13,003,796
Beverage container deposits	-	-	19,685,339	-	19,685,339
Total liabilities	<u>50,765,916</u>	<u>9,104,002</u>	<u>23,760,178</u>	<u>26,516,285</u>	<u>110,146,381</u>
<b>Fund balance (deficit)</b>					
Reserved for encumbrances	24,217,822	12,566,906	10,184,376	47,973,546	94,942,650
Unreserved, reported in					
General fund	(21,662,348)	-	-	-	(21,662,348)
Tobacco settlement fund	-	18,335,816	-	-	18,335,816
Deposit beverage container fund	-	-	604,927	-	604,927
Special revenue funds	-	-	-	26,148,231	26,148,231
Total fund balance	<u>2,555,474</u>	<u>30,902,722</u>	<u>10,789,303</u>	<u>74,121,777</u>	<u>118,369,276</u>
Total liabilities and fund balance	<u>\$ 53,321,390</u>	<u>\$ 40,006,724</u>	<u>\$ 34,549,481</u>	<u>\$ 100,638,062</u>	<u>\$ 228,515,657</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Reconciliation of the Governmental Funds' Fund Balance to the**  
**Governmental Activities' Net Assets**  
**June 30, 2009**

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Total fund balance – governmental funds	\$ 118,369,276
Amounts reported for governmental activities in the statement of net assets are different because	
Tobacco settlement receivable (net of vouchers payable and Due to State of Hawaii amounts) is not available for current financial resources and therefore is not reported as an asset in the governmental funds.	6,725,000
Capital assets used in governmental activities are not financial resources and therefore not reported as an asset in the governmental funds.	64,143,715
Compensated absences reported in the statement of net assets do not require the use of current financial resources and therefore are not reported as liabilities in the governmental funds.	(27,020,350)
Workers' compensation liability reported in the statement of net assets does not require the use of current financial resources and therefore is not reported as a liability in the governmental funds.	(403,758)
Receivables from other State agencies are not available to pay for current-period expenditures and therefore are not reported as an asset in the governmental funds.	6,699,800
Net assets of governmental activities	<u>\$ 168,513,683</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii  
Department of Health  
Governmental Funds – Statement of Revenues, Expenditures and Changes in Fund Balance  
Year Ended June 30, 2009**

	General	Tobacco Settlement	Deposit Beverage Container	Other Funds	Total
<b>Revenues</b>					
State allotment, net	\$ 437,444,812	-	-	\$ 3,601,000	\$ 441,045,812
Intergovernmental	-	-	-	123,579,290	123,579,290
Tobacco settlement	-	60,109,113	-	-	60,109,113
Deposit beverage container program	-	-	17,789,475	-	17,789,475
Nonimposed employee fringe benefits	53,273,241	-	-	-	53,273,241
Taxes, fees, fines and other	-	-	-	28,254,658	28,254,658
Investment loss	-	(1,895,455)	(1,397,779)	(2,299,251)	(5,592,485)
Total revenues	490,718,053	58,213,658	16,391,696	153,135,697	718,459,104
<b>Expenditures</b>					
General administration	22,537,216	-	-	9,355,947	31,893,163
Environmental health	26,346,030	-	24,547,618	20,311,461	71,205,109
Behavioral health services	230,650,548	-	-	67,840,175	298,490,723
Health resources	201,794,585	16,631,298	-	65,455,440	283,881,323
Total expenditures	481,328,379	16,631,298	24,547,618	162,963,023	685,470,318
Excess (deficiency) of revenues over expenditures	9,389,674	41,582,360	(8,155,922)	(9,827,326)	32,988,786
<b>Other financing sources (uses)</b>					
Transfers in	-	214,232	-	116,318,622	116,532,854
Transfers out	(5,515,943)	(43,688,147)	-	(105,281,894)	(154,485,984)
Total other financing sources (uses)	(5,515,943)	(43,473,915)	-	11,036,728	(37,953,130)
Net change in fund balance	3,873,731	(1,891,555)	(8,155,922)	1,209,402	(4,964,344)
Fund balance at July 1, 2008, as previously reported	(1,318,257)	32,794,277	24,925,040	72,912,375	129,313,435
Prior period adjustment	-	-	(5,979,815)	-	(5,979,815)
Fund balance at July 1, 2008, as restated	(1,318,257)	32,794,277	18,945,225	72,912,375	123,333,620
Fund balance at June 30, 2009	\$ 2,555,474	\$ 30,902,722	\$ 10,789,303	\$ 74,121,777	\$ 118,369,276

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Reconciliation of the Governmental Funds' Changes in Fund Balance to the**  
**Governmental Activities' Change in Net Assets**  
**Year Ended June 30, 2009**

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Net change in fund balance – total governmental funds	\$ (4,964,344)
Amounts reported for governmental activities in the statement of activities are different because	
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation exceeded capital outlays for the year.	(29,505)
Increase in compensated absences reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds.	(1,784,718)
Decrease in the noncurrent portion of workers' compensation liability reported in the statement of activities do not require the use of current financials resources and therefore is not reported as an expenditure in the governmental funds.	48,462
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the governmental funds.	<u>(4,047,614)</u>
Change in net assets of governmental activities	<u>\$ (10,777,719)</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**General Fund – Budgetary Comparison Statement**  
**Year Ended June 30, 2009**

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	<b>Budgeted Amounts</b>		<b>Actual Amounts (Budgetary Basis)</b>
	<b>Original</b>	<b>Final</b>	
<b>Revenues</b>			
Current-year appropriations	\$ 444,944,447	\$ 456,534,814	\$ 441,313,656
Total revenues	444,944,447	456,534,814	441,313,656
<b>Expenditures</b>			
General administration	17,643,719	20,505,146	18,015,445
Environmental health administration	20,368,051	20,102,225	19,575,846
Behavioral health services administration	205,752,097	210,841,411	208,059,769
Health resources administration	201,180,580	205,086,032	195,662,596
Total expenditures	444,944,447	456,534,814	441,313,656
Excess of revenues over expenditures	\$ -	\$ -	\$ -

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Tobacco Settlement Fund – Budgetary Comparison Statement**  
**Year Ended June 30, 2009**

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	<b>Budgeted Amounts</b>		<b>Actual Amounts (Budgetary Basis)</b>
	<b>Original</b>	<b>Final</b>	
<b>Revenues</b>			
Current-year funds	\$ 53,847,266	\$ 53,900,241	\$ 61,154,489
Total revenues	53,847,266	53,900,241	61,154,489
<b>Expenditures</b>			
Health resources administration	53,847,266	53,900,241	56,211,442
Total expenditures	53,847,266	53,900,241	56,211,442
Excess of revenues over expenditures	\$ -	\$ -	\$ 4,943,047

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Deposit Beverage Container Fund – Budgetary Comparison Statement**  
**Year Ended June 30, 2009**

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	<u>Budgeted Amounts</u>		<u>Actual Amounts (Budgetary Basis)</u>
	<u>Original</u>	<u>Final</u>	
<b>Revenues</b>			
Current-year funds	<u>\$ 71,105,960</u>	<u>\$ 71,123,943</u>	<u>\$ 53,950,101</u>
Total revenues	<u>71,105,960</u>	<u>71,123,943</u>	<u>53,950,101</u>
<b>Expenditures</b>			
Environmental health administration	<u>71,105,960</u>	<u>71,123,943</u>	<u>63,800,260</u>
Total expenditures	<u>71,105,960</u>	<u>71,123,943</u>	<u>63,800,260</u>
Excess of expenditures over revenues	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (9,850,159)</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Proprietary Funds – Statement of Net Assets**  
**June 30, 2009**

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	<b>Water Pollution Control Revolving Fund</b>	<b>Drinking Water Treatment Revolving Loan Fund</b>	<b>Total</b>
<b>Assets</b>			
Current assets			
Equity in cash and cash equivalents and investments in State Treasury	\$ 120,167,747	\$ 24,862,525	\$ 145,030,272
Loan fees receivable	400,159	530,655	930,814
Accrued interest receivable	764,508	56,366	820,874
Other accrued interest	1,260,359	219,902	1,480,261
Due from federal government	-	20,677	20,677
Current portion of loans receivable	<u>20,844,288</u>	<u>3,482,402</u>	<u>24,326,690</u>
Total current assets	143,437,061	29,172,527	172,609,588
Loans receivable, net of current portion	232,113,655	53,036,981	285,150,636
Capital assets, net of accumulated depreciation, at cost	<u>-</u>	<u>272,366</u>	<u>272,366</u>
Total assets	<u>\$ 375,550,716</u>	<u>\$ 82,481,874</u>	<u>\$ 458,032,590</u>
<b>Liabilities</b>			
Current liabilities			
Accounts payable and other accrued liabilities	\$ 143,214	\$ 161,354	\$ 304,568
Total current liabilities	143,214	161,354	304,568
Accrued vacation, net of current portion	186,736	35,896	222,632
Other postemployment benefits	<u>291,777</u>	<u>84,261</u>	<u>376,038</u>
Total liabilities	621,727	281,511	903,238
<b>Net Assets</b>			
Invested in capital assets	-	272,366	272,366
Restricted – expendable	<u>374,928,989</u>	<u>81,927,997</u>	<u>456,856,986</u>
Total net assets	<u>374,928,989</u>	<u>82,200,363</u>	<u>457,129,352</u>
Total liabilities and net assets	<u>\$ 375,550,716</u>	<u>\$ 82,481,874</u>	<u>\$ 458,032,590</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Proprietary Funds – Statement of Revenues, Expenses and**  
**Changes in Fund Net Assets**  
**Year Ended June 30, 2009**

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	<b>Water Pollution Control Revolving Fund</b>	<b>Drinking Water Treatment Revolving Loan Fund</b>	<b>Total</b>
<b>Operating revenues</b>			
Interest income from loans	\$ 3,252,434	\$ 229,316	\$ 3,481,750
Administrative loan fee	<u>1,679,986</u>	<u>1,774,766</u>	<u>3,454,752</u>
Total revenues	4,932,420	2,004,082	6,936,502
<b>Expenses</b>			
Administrative	1,619,087	468,216	2,087,303
State program management	-	639,626	639,626
Water protection	-	62,205	62,205
Small systems	-	336,891	336,891
Total expenses	<u>1,619,087</u>	<u>1,506,938</u>	<u>3,126,025</u>
Operating income	3,313,333	497,144	3,810,477
<b>Nonoperating revenues and expenses</b>			
State contributions	1,655,000	1,671,000	3,326,000
Federal contributions	12,143,089	8,704,715	20,847,804
Other interest loss	<u>(4,114,807)</u>	<u>(598,776)</u>	<u>(4,713,583)</u>
Total nonoperating revenues and expenses	<u>9,683,282</u>	<u>9,776,939</u>	<u>19,460,221</u>
Change in net assets	12,996,615	10,274,083	23,270,698
<b>Net assets</b>			
Beginning of year	<u>361,932,374</u>	<u>71,926,280</u>	<u>433,858,654</u>
End of year	<u>\$ 374,928,989</u>	<u>\$ 82,200,363</u>	<u>\$ 457,129,352</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Proprietary Funds – Statement of Cash Flows**  
**Year Ended June 30, 2009**

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	<b>Water Pollution Control Revolving Fund</b>	<b>Drinking Water Treatment Revolving Loan Fund</b>	<b>Total</b>
<b>Cash flows from operating activities</b>			
Interest income from loans	\$ 3,607,102	\$ 228,453	\$ 3,835,555
Administrative loan fees	1,872,790	1,710,973	3,583,763
Principal repayments on loans	21,036,414	3,128,123	24,164,537
Disbursement of loan proceeds	(76,012,545)	(9,984,387)	(85,996,932)
Payments to employees	(1,299,578)	(420,188)	(1,719,766)
Payments rendered by other State agencies	-	(40,952)	(40,952)
Payments to vendors	(135,209)	(1,035,822)	(1,171,031)
Net cash used in operating activities	(50,931,026)	(6,413,800)	(57,344,826)
<b>Cash flows from noncapital financing activities</b>			
State contributions	1,655,000	1,671,000	3,326,000
Federal contributions	12,143,089	9,092,888	21,235,977
Net cash provided by noncapital financing activities	13,798,089	10,763,888	24,561,977
<b>Cash flows from capital and related financing activities</b>			
Purchase of equipment	-	(5,268)	(5,268)
Net cash used in capital and related financing activities	-	(5,268)	(5,268)
<b>Cash flows from investing activities</b>			
Other interest loss	(4,542,119)	(709,640)	(5,251,759)
Net cash used in investing activities	(4,542,119)	(709,640)	(5,251,759)
Net increase (decrease) in cash	(41,675,056)	3,635,180	(38,039,876)
<b>Equity in cash and cash equivalents and investments in State Treasury</b>			
Beginning of year	161,842,803	21,227,345	183,070,148
End of year	\$ 120,167,747	\$ 24,862,525	\$ 145,030,272

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Proprietary Funds – Statement of Cash Flows**  
**Year Ended June 30, 2009**

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	Fund	Loan Fund	Total
<b>Reconciliation of operating income to net cash used in operating activities</b>			
Operating income	\$ 3,313,333	\$ 497,144	\$ 3,810,477
Adjustments to reconcile operating income to net cash used in operating activities			
Depreciation expense	7,475	90,397	97,872
Change in assets and liabilities			
Loans receivable	(54,976,130)	(6,856,263)	(61,832,393)
Accrued interest on loans receivables	354,668	(863)	353,805
Loan fees receivable	192,803	(63,793)	129,010
Accounts payable and other accrued liabilities	28,449	(129,791)	(101,342)
Other postemployment benefits	148,376	49,369	197,745
	<u>148,376</u>	<u>49,369</u>	<u>197,745</u>
Net cash used in operating activities	<u>\$ (50,931,026)</u>	<u>\$ (6,413,800)</u>	<u>\$ (57,344,826)</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Fiduciary Funds – Statement of Fiduciary Net Assets**  
**June 30, 2009**

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	<b>Agency Funds</b>
<b>Assets</b>	
Cash and cash equivalents	\$ 421,460
Total assets	<u>\$ 421,460</u>
<b>Liabilities</b>	
Due to others	\$ 421,460
Total liabilities	<u>\$ 421,460</u>

The accompanying notes are an integral part of this statement.

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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**1. Organization and Summary of Significant Accounting Policies**

**Financial Reporting Entity**

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

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

The Department is part of the executive branch of the State of Hawaii (the "State"). The financial statements of the Department are intended to present the financial position and the changes in financial position and cash flows, where applicable, of only that portion of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2009, and the changes in its financial position and cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America. The State Comptroller maintains the central accounts for all State funds and publishes a comprehensive annual financial report for the State annually, which includes the Department's financial activities.

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

**Department-wide Financial Statements**

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

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

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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**Fund Financial Statements**

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Department considers revenues to be available if they are collected within 60 days of the end of the current fiscal year end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, expenditures related to compensated absences and claims and judgments are recorded only when payment is due.

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

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

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

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

**Governmental Funds (Governmental Activities):**

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

**Proprietary Funds (Business-Type Activities):**

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

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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**Fiduciary Funds:**

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

**Equity in Cash and Cash Equivalents and Investments in State Treasury**

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

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

GASB Statement No. 40, *Deposit and Investment Risk Disclosures* ("Statement No. 40"), requires disclosures over common deposit and investment risks related to credit risk, interest rate risk, and foreign currency risk. Investments can be categorized by type, maturity and custodian to determine the level of interest rate, credit, and custodial risk assumed by the Department. However, as all of the Department's monies are held in the State cash pool, the Department does not manage its own investments and the types of investments and related interest rate, credit, and custodial risks are not determinable at the department level. The risk disclosures of the State's cash pool are included in the State's Comprehensive Annual Financial Report ("CAFR") which may be obtained from the Department of Accounting and General Services' ("DAGS") website:  
<http://hawaii.gov/dags/rpts>.

In February 2010, DAGS issued guidance informing State agencies participating in the State Treasury Investment Pool that the State's investments in auction rate securities were impaired as of and for the year ended June 30, 2009 and that each participating State agency would be allocated a portion of the impairment. The Department's total allocated impairment loss for fiscal 2009 amounted to \$16,224,391.

**Due from State Treasury**

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

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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**Due from Other State Agencies**

Receivables due from other State agencies consist of reimbursements from the Department of Human Services (“DHS”) for Medicaid payments that the Department makes to providers of health services. The Department is responsible to pay the State portion of the Medicaid claims, and DHS reimburses the Department for the Federal portion of the claims. The receivable of \$19.9 million is comprised of \$8.0 million for the Developmental Disabilities/Mental Retardation Waiver program and \$11.9 for other Medicaid rehabilitation option claims.

Payments made to providers and received from DHS for the Federal portion of the Medicaid claims are classified as transfers out and transfers in, respectively, for financial statement purposes.

**Tobacco Settlement**

In November 1998, the State settled its tobacco lawsuit as part of a nationwide settlement involving 46 other states and various tobacco industry defendants. Under the settlement, those tobacco companies that have joined in the Master Settlement Agreement will pay the State approximately \$1.3 billion over a 25-year period. The Department is responsible for administering the Hawaii Tobacco Settlement Special Fund. The Department receives all tobacco settlement monies and then allocates and appropriates 75% of the funds to other State agencies and other entities in accordance with Hawaii Revised Statutes (“HRS”) 328L-2. The Department receives annual payments on April 15 of each year for tobacco settlements earned for the preceding calendar year.

The Department received approximately \$60,000,000 in tobacco settlement proceeds during the year ended June 30, 2009 for the calendar year ended December 31, 2008. In accordance with GASB Technical Bulletin No. 04-01, *Tobacco Settlement Recognition and Financial Reporting Entity Issues*, the Department has recorded a tobacco settlement receivable for \$26,900,000 in the statement of net assets representing tobacco settlements earned for the period January 1, 2009 through June 30, 2009.

**Reserved for Encumbrances**

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

**Capital Assets**

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

Land	All capitalized
Land improvements	\$100,000
Building and building improvements	\$100,000
Furniture and equipment	\$5,000

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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

	<b>Governmental- Type Activities</b>	<b>Business- Type Activities</b>
Land improvements	15	Not applicable
Building and building improvements	30	Not applicable
Furniture and equipment	5–7	5–7

**Deferred Income**

Deferred income at the fund level and department-wide level arise when the Department receives resources before it has a legal claim to them. In subsequent periods, when the revenue recognition criteria is met, or when the Department has a legal claim to the resources, the liability for deferred income is removed from the statement of net assets and balance sheet, and revenue is recognized. Deferred income at June 30, 2009 consisted primarily of Federal grant funds for which all eligibility requirements had not yet been met.

**Beverage Container Deposits**

Deposits of \$0.05 are made by distributors to the deposit beverage container fund for each qualifying container. The deposit beverage container fund maintains all deposits until the recycling centers claim reimbursement for the deposits that they pay out to the consumers. The deposit beverage container fund maintains the deposits that are expected to be redeemed.

Amounts paid out to the consumers are based on containers redeemed or a predetermined weight per type of container redeemed (i.e., aluminum, mixed plastics, etc.). These weights are determined based on the mix of containers redeemed and are reviewed when necessary. Management estimates, based on past collections and success of recycling in other states, that 80% of the containers will be recycled every year. The remaining 20% of the containers are expected to be unredeemed; therefore, 20% of the deposits collected are recognized into revenue each year.

**Accrued Vacation**

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

**Accumulated Sick Leave**

Sick leave accumulates at the rate of one and three-quarters working days for each month of service without limit, but may be taken only in the event of illness and is not convertible to pay upon termination of employment. However, a State employee who retires or leaves government service in good standing with 60 days or more of unused sick leave is entitled to additional service credit in the State's Employees' Retirement System ("ERS"). At June 30, 2009, accumulated sick leave was approximately \$73,500,000.

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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**Intrafund and Interfund Transactions**

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

**Use of Estimates**

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

**Use of Restricted and Unrestricted Net Assets**

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

**New Accounting Pronouncements**

In March 2009, the GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. This Statement provides clearer fund balance classifications that can be more consistently applied and clarifies the existing governmental fund type definitions. This Statement also establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds and provides for additional classifications such as restricted, committed, assigned, and unassigned fund balance. The provisions of this Statement are effective for the fiscal year beginning after June 15, 2010. Management does not expect this Statement to have a material effect on the Department's financial statements.

In March 2009, the GASB issued Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to identify the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of state and local governmental entities that are presented in conformity with GAAP. The requirements of this Statement became effective upon its issuance and did not materially impact the Department's financial statements.

In March 2009, the GASB issued Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*. The objective of this Statement is to incorporate certain accounting and financial reporting guidance presented in the American Institute of Certified Public Accountants' Statement on Auditing Standards into GASB's authoritative literature. This statement is intended to improve financial reporting by bringing the authoritative accounting and financial reporting literature together in one place. The requirements of this Statement became effective upon its issuance and did not materially impact the Department's financial statements.

In January 2010, the GASB issued Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*. The objective of this Statement is to permit an agent employer that has an individual-employer OPEB plan with fewer than 100 total plan members to use the alternative measurement method, as an option, regardless of the number of total plan members in the agent multiple-employer OPEB plan in which it participates. The requirements of this Statement are effective for periods beginning after June 15, 2011. Management does not expect that this Statement will have a material effect on the Department's financial statements as the Department participates in the State's plan, which has more than 100 members.

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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In January 2010, the GASB also issued Statement No. 58, *Accounting and Financial Reporting for Chapter 9 Bankruptcies*. The objective of this Statement is to provide accounting and financial reporting guidance for governments that have petitioned for protection from creditors by filing for bankruptcy under Chapter 9 of the United States Bankruptcy Code. It requires governments to remeasure liabilities that are adjusted in bankruptcy when the bankruptcy court confirms a new payment plan. The requirements of this Statement are effective for reporting periods beginning after June 15, 2009. Currently, management does not expect that this Statement will apply to the Department.

**2. Budgeting and Budgetary Control**

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

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

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

Budgets are adopted for the General Fund of the Department and are prepared on the basis of cash receipts and amounts disbursed, which is a basis of accounting other than GAAP.

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

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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Since budgetary basis differs from GAAP, budget and actual amounts in the budgetary comparison statements are presented on the budgetary basis. A reconciliation of revenues in excess of (less than) expenditures on a budgetary basis at June 30, 2009, to revenues in excess of (less than) expenditures presented in conformity with GAAP follows:

	<b>General Fund</b>	<b>Tobacco Settlement Fund</b>	<b>Deposit Beverage Container Fund</b>
Excess of revenues over expenditures (expenditures over revenues) – actual on a budgetary basis	\$ -	\$ 4,943,047	\$ (9,850,159)
Reserve for encumbrances at year end	24,217,822	12,566,906	10,184,376
Expenditures for liquidation of prior year's encumbrances	(42,128,381)	(28,332,370)	(10,374,420)
Accruals and other adjustments	<u>27,300,233</u>	<u>52,404,777</u>	<u>1,884,281</u>
Excess of revenues over expenditures (expenditures over revenues) – GAAP basis	<u>\$ 9,389,674</u>	<u>\$ 41,582,360</u>	<u>\$ (8,155,922)</u>

**3. Loans Receivable**

At June 30, 2009, the proprietary funds loans receivable consisted of loans to county governmental units for the water pollution control and drinking water treatment programs. The loans require annual, semi-annual or quarterly payments, including interest at 0.00% to 3.02%, commencing not later than one year after project completion, notice to proceed, or loan agreement date. Final payment is due not later than twenty years after project completion. Accrued interest receivable on the loans amounted to approximately \$821,000 at June 30, 2009.

The following is a schedule of principal payments due on loans for projects completed or in progress as of June 30, 2009:

<b>Year ending June 30,</b>	
2010	\$ 24,326,690
2011	24,939,490
2012	25,296,707
2013	25,681,458
2014	23,181,673
Thereafter	<u>186,051,308</u>
	<u>\$ 309,477,326</u>

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

**4. Capital Assets**

Capital asset activity for the year ended June 30, 2009 was as follows:

	Beginning Balance	Additions	Dispositions	Ending Balance
<b>Governmental activities</b>				
Capital assets, not being depreciated				
Land	\$ 1,018,080	\$ -	\$ -	\$ 1,018,080
Total capital assets not being depreciated	1,018,080	-	-	1,018,080
Capital assets, being depreciated				
Land improvements	1,862,927	-	-	1,862,927
Building and building improvements	132,282,276	4,166,511	-	136,448,787
Furniture and equipment	21,704,057	1,727,834	(1,159,474)	22,272,417
Total capital assets being depreciated	155,849,260	5,894,345	(1,159,474)	160,584,131
Less: Accumulated depreciation				
Land improvements	1,850,417	8,340	-	1,858,757
Building and building improvements	76,653,548	3,897,115	-	80,550,663
Furniture and equipment	14,190,155	1,714,645	(855,724)	15,049,076
Total accumulated depreciation	92,694,120	5,620,100	(855,724)	97,458,496
Governmental activities capital assets, net	<u>\$ 64,173,220</u>	<u>\$ 274,245</u>	<u>\$ (303,750)</u>	<u>\$ 64,143,715</u>
<b>Business-type activities</b>				
Capital assets being depreciated				
Furniture and equipment	\$ 1,180,995	\$ 5,268	\$ (28,959)	\$ 1,157,304
Total capital assets being depreciated	1,180,995	5,268	(28,959)	1,157,304
Less: Accumulated depreciation for equipment	816,025	97,872	(28,959)	884,938
Total accumulated depreciation	816,025	97,872	(28,959)	884,938
Business-type activities capital assets, net	<u>\$ 364,970</u>	<u>\$ (92,604)</u>	<u>\$ -</u>	<u>\$ 272,366</u>

Current period depreciation expense was charged to functions as follows:

<b>Governmental activities</b>	
General administration	\$ 494,523
Environmental health	2,049,657
Behavioral health	1,766,658
Health resources	1,309,262
Total depreciation expense – governmental activities	<u>\$ 5,620,100</u>
<b>Business-type activities</b>	
Environmental health	\$ 97,872
Total depreciation expense – business-type activities	<u>\$ 97,872</u>

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
**June 30, 2009**

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**5. Accrued Vacation**

The changes to the accrued vacation liability during 2009 were as follows:

<b>Balance at July 1, 2009</b>	\$ 25,514,343
Increase	12,701,937
Decrease	<u>(10,909,526)</u>
<b>Balance at June 30, 2009</b>	27,306,754
Less: Current portion	<u>9,456,329</u>
Noncurrent portion	<u><u>\$ 17,850,425</u></u>

**6. Beverage Container Deposits**

The changes to the beverage container deposit liability during 2009 were as follows:

<b>Balance at July 1, 2009, as restated</b>	\$ 21,650,903
Increase: Deposits received from distributor	44,369,984
Decrease: Payments made to recycling centers, net of refunds	(37,461,550)
Decrease: Unredeemed deposits recognized as revenues	<u>(8,873,998)</u>
<b>Balance at June 30, 2009</b>	<u><u>\$ 19,685,339</u></u>

**7. Non-Imposed Employee Fringe Benefits**

Non-imposed employee fringe benefits related to General Fund salaries are funded by the State. These costs, totaling approximately \$53,300,000 for the fiscal year ended June 30, 2009, have been reported as revenues and expenditures of the Department's General Fund.

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

**8. Employee Benefit Plans**

Substantially all employees of the Fund participate in the State's various employee benefit plans, including the ERS, post-employment healthcare and life insurance plan, and a deferred compensation plan. For more information on the State's benefit plans, refer to the State ERS' CAFR. The State's CAFR can be found on the DAGS website. The ERS CAFR can be found at the ERS website: <http://www4.hawaii.gov/ers/default.htm>.

**Employees' Retirement System**

The ERS is a cost-sharing, multiple-employer public employee retirement plan. The ERS provides retirement benefits as well as death and disability benefits. All contributions, benefits and eligibility requirements are established by Chapter 88, HRS, and can be amended by legislative action.

**State of Hawaii**  
**Department of Health**  
**Notes to Financial Statements**  
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**Post-Employment Healthcare and Life Insurance Benefits**

The State contributes to the Hawaii Employer-Union Health Benefits Trust Fund (“EUTF”), an agent multiple-employer defined benefit plan. The EUTF was established to provide a single delivery system of health benefits for state and county workers, retirees, and their dependents. The eligibility requirements for retiree health benefits are based on date of hire.

*State Policy*

The actuarial valuation of the EUTF does not provide other postemployment benefits (“OPEB”) information by department or agency. Accordingly, the State’s policy on the accounting and reporting for OPEB is to allocate a portion of the State’s Annual Required Contribution (“ARC”), interest, and any adjustment to the ARC, to component units and proprietary funds that are reported separately in stand-alone departmental financial statements or in the State’s CAFR. The basis for the allocation is the proportionate share of contributions made by each component unit and proprietary fund for retiree health benefits.

*Allocated OPEB Cost*

The following table shows the components of the annual OPEB cost that have been allocated to the two proprietary funds of the Department for the year ended June 30, 2009:

	<b>Water Pollution Control Revolving Fund</b>	<b>Drinking Water Treatment Revolving Loan Fund</b>	<b>Total</b>
Annual required contribution	\$ 231,052	\$ 76,879	\$ 307,931
Interest on OPEB obligation	7,096	2,361	9,457
Adjustment to annual required contribution	(6,031)	(2,007)	(8,038)
Annual OPEB expense	232,117	77,233	309,350
Contributions made	(83,741)	(27,864)	(111,605)
Increase in net OPEB obligation	148,376	49,369	197,745
Net OPEB obligation, beginning of year	143,401	34,892	178,293
Net OPEB obligation, end of year	<u>\$ 291,777</u>	<u>\$ 84,261</u>	<u>\$ 376,038</u>

*Amount of Contributions Made*

Contributions are financed on a pay-as-you-go basis and the Department’s contributions for the years June 30, 2009, 2008, and 2007 were approximately \$2,751,000, \$2,915,000, and \$2,267,000, respectively.

*Required Supplementary Information and Disclosures*

The State’s CAFR includes the required footnote disclosures and supplementary information on the State’s OPEB plan.

**Deferred Compensation Plan**

The State offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all State employees, permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or an unforeseeable emergency.

All plan assets are held in a trust fund to protect them from claims of general creditors. The State has no responsibility for loss due to the investment or failure of investment of funds and assets in the plan, but has the duty of due care that would be required of an ordinary prudent investor.

**State of Hawaii**  
**Department of Health**  
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**9. Commitments and Contingencies**

**Operating Leases**

The Department leases various office facilities and equipment through fiscal year 2012 on a long-term basis as provided for in the lease agreements. The following is a schedule of minimum future rent payments on noncancelable operating leases at June 30, 2009:

<b>Year ending June 30,</b>	
2010	\$ 479,000
2011	433,000
2012	97,000
	<u>\$ 1,009,000</u>

Rent expenditures for the fiscal year ended June 30, 2009 approximated \$2,900,000.

**Insurance Coverage**

The State maintains certain insurance coverage to satisfy bond indenture agreements as well as for other purposes, but is substantially self-insured for all other perils including workers' compensation. The State records a liability for risk financing and insurance related losses, including incurred but not reported, if it is determined that a loss has been incurred and the amount can be reasonably estimated. The State retains various risks and insures certain excess layers with commercial insurance companies. At June 30, 2009, the State recorded estimated losses for workers' compensation, automobile, and general liability claims as long-term liabilities as the losses will not be liquidated with currently expendable available financial resources. The estimated losses will be paid from legislative appropriations of the State's General Fund. The Department's portion of the State's workers' compensation expense for the year ended June 30, 2009 was approximately \$175,000.

**Litigation**

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

**Ceded Lands**

The Office of Hawaiian Affairs ("OHA") and the State are involved in litigation regarding the State's alleged failure to properly account for and pay to OHA monies due to OHA under the provisions of the Hawaii State Constitution and Chapter 10 of the Hawaii Revised Statutes for use by the State of certain ceded lands. The ultimate outcome of this matter is still unknown. Full discussion of this matter and other legal matters between OHA and the State are disclosed in the State's CAFR.

**State of Hawaii  
 Department of Health  
 Notes to Financial Statements  
 June 30, 2009**

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**10. Restatements to the Department-wide Net Assets and Governmental Funds' Fund Balance**

The Department has restated its June 30, 2008 department-wide net assets and governmental funds' fund balance to correct an error in accounting for the deposit beverage container liability. The restatement adjustment records additional deposit beverage container liabilities that were improperly recognized as revenues in the prior year.

As a result of the correction, the Department made the following adjustments to its previously reported June 30, 2008 department-wide net assets and governmental funds' fund balance.

	<b>Governmental Activities</b>
<b>Net assets at June 30, 2008, as previously reported</b>	\$ 185,271,217
Adjustments attributable to the understatement of liabilities	<u>(5,979,815)</u>
<b>Net assets at June 30, 2008, as restated</b>	<u>\$ 179,291,402</u>

	<b>Deposit Beverage Container</b>	<b>Total Governmental Funds</b>
<b>Fund balances at June 30, 2008, as previously reported</b>	\$ 24,925,040	\$ 129,313,435
Adjustments attributable to the understatement of liabilities	<u>(5,979,815)</u>	<u>(5,979,815)</u>
<b>Fund balances at June 30, 2008, as restated</b>	<u>\$ 18,945,225</u>	<u>\$ 123,333,620</u>

**Schedule of  
Expenditures of Federal Awards**

**State of Hawaii**  
**Department of Health**  
**Schedule of Expenditures of Federal Awards**  
**Year Ended June 30, 2009**

Federal Grantor/Pass-Through Grantor/Program Title	Project Number	CFDA Contract, Award or Assistance ID Number	Federal Expenditures	Amount Provided to Subrecipient
<b>U.S. Department of Health and Human Services ("DHHS")</b>				
Direct Programs				
Special Programs for Aging – Title VII Chapter 3	468	93.041	\$ 17,610	\$ -
Special Programs for Aging – Title VII Chapter 2	468	93.042	80,819	-
Special Programs for Aging – Title III Part D	401	93.043	85,893	85,893
Special Programs for Aging – Title III Part B	401,468	93.044	1,959,056	1,906,170
Special Programs for Aging – Title III Part C1 & C2	401	93.045	2,591,595	2,081,286
Nutrition Services Incentive Program	406	93.053	577,078	577,078
Subtotal Aging Cluster			5,127,729	4,564,534
Special Programs for Aging – Title IV	357,405, 478	93.048	477,902	326,508
Special Programs for Aging – Title III Part E	401	93.052	652,535	652,535
Public Health Emergency Preparedness	various	93.069	6,206,851	-
Project Ho'omohala – Transition to Adulthood	229	93.104	1,026,259	-
Maternal and Child Health Federal Consolidated Programs	various	93.110	1,268,298	-
Project Grants and Cooperative Agreements for Tuberculosis Control Programs	247	93.116	899,637	-
Emergency Medical Services for Children	388	93.127	94,968	59,385
Primary Care Services – Resource Coordination and Development	298	93.130	197,518	-
Injury Prevention and Control Research and State and Community Based Programs	various	93.136	352,872	-
Projects for Assistance in Transition from Homelessness ("PATH")	208	93.150	222,633	55,207
Hansen's Disease National Ambulatory Care Program	264	93.215	767,404	-
Family Planning – Services	239	93.217	1,726,520	911,500
Traumatic Brain Injury State Demonstration Grant Program	434	93.234	101,701	-
Abstinence Education Initiative	273	93.235	47,773	35,734
Rural Hospital Flexibility Program	415	93.241	638,288	6,311
Substance Abuse and Mental Health Services – Projects of Regional and National Significance	various	93.243	3,084,979	1,023,499 *
Universal Newborn Hearing Screening	416	93.251	81,944	-
State Planning Grants Health Care Access for the Uninsured	437	93.256	82,040	-
Immunization Grants	457	93.268	13,700,481	10,938,942 *
Substance Abuse and Mental Health Services – Access to Recovery Centers for Disease Control and Prevention	396	93.275	3,327,483	2,886,438 *
Small Rural Hospital Improvement	various	93.283	3,121,309	272,627 *
Community-Based Family Resource and Support Grants	454	93.301	84,205	83,915
Development Disabilities Basic Support and Advocacy Grants	270	93.590	465,160	63,459
State Survey and Certification of Health Care Providers and Suppliers	240	93.630	406,755	-
Centers for Medicare and Medicaid Services Research, Demonstrations and Evaluations	various	93.777	1,833,944	-
National Bioterrorism Hospital Preparedness Program	various	93.779	229,975	106,695
Grants to States for Operation of Offices of Rural Health	435	93.889	2,085,164	-
HIV Care Formula Grants	299	93.913	154,927	-
Cooperative Agreements for State-Based Comprehensive Breast and Cervical Early Detection Programs	293	93.917	3,326,484	1,260,098 *
Healthy Start Initiative	448	93.919	802,037	802,037
Special Projects of National Significance	286	93.926	898,359	647,160
HIV Prevention Project	269	93.928	145,000	-
HIV / AIDS Surveillance	266	93.940	2,032,123	-
Cooperative Agreements to Support State-Based Safe Motherhood and Infant Health Initiative Programs	272	93.944	189,381	-
Block Grants for Community Mental Health Services	319	93.946	151,672	-
Substance Abuse Prevention and Treatment Block Grants	various	93.958	1,460,525	752,329
Preventive Health Services – Sexually Transmitted Diseases Control Grants	various	93.959	7,325,736	6,995,184 *
Programs and Evaluation of Surveillance System	268	93.977	396,573	-
Preventive Health and Health Services Block Grant	261	93.988	300,133	-
Maternal and Child Health Services Block Grant	various	93.991	663,402	-
Vital Statistics Cooperative Program	various	93.994	2,312,723	22,701
Subtotal Direct Programs	285	93.200-2000-07211	223,414	-
Pass-through from the State Department of Human Services			68,879,138	32,552,691
Temporary Assistance for Needy Families	various	93.558	1,256,186	1,134,486
Child Care and Development Block Grant	various	93.575	236,838	-
Child Abuse and Neglect State Grants	various	93.669	84,498	-
Subtotal Pass-through Programs			1,577,522	1,134,486
Total Department of Health and Human Services			70,456,660	33,687,177

\* Denotes Major Federal Program

**State of Hawaii**  
**Department of Health**  
**Schedule of Expenditures of Federal Awards**  
**Year Ended June 30, 2009**

Federal Grantor/Pass-Through Grantor/Program Title	Project Number	CFDA Contract, Award or Assistance ID Number	Federal Expenditures	Amount Provided to Subrecipient
<b>U.S. Department of Agriculture</b>				
Direct Program				
Food Safety Cooperative Agreements	203	10.479	476,063	-
Special Supplemental Nutrition Program for Women, Infants, and Children	275, 295	10.557	36,310,357	2,305,400 *
Other	392	10.	29,195	-
Subtotal Direct Programs			<u>36,815,615</u>	<u>2,305,400</u>
Pass-through from the State Department of Human Services				
State Administrative Matching Grants for the Supplemental Nutrition Assistance Program	various	10.561	517,709	-
Subtotal Pass-through Programs			<u>517,709</u>	<u>-</u>
Total Department of Agriculture			<u>37,333,324</u>	<u>2,305,400</u>
<b>Environmental Protection Agency ("EPA")</b>				
Direct Program				
Air Pollution Control Program Support	233	66.001	637,050	581
Surveys, Studies, Investigations, Demonstrations and Special Purpose Activities Relating to the Clean Air Act	294	66.034	55,495	-
Water Pollution Control – State and Interstate Program Support	various	66.419	1,839,316	227,810
State Public Water System Supervision	232	66.432	400,147	-
Water Quality Management Program	12284-14284	66.454	67,024	56,404
Capitalization Grants for Clean Water State Revolving Funds	15206-20206	66.458	12,143,089	12,143,089 *
Nonpoint Source Implementation Grants	3290-8291	66.460	1,089,488	23,705
Capitalization Grants for Drinking Water State Revolving Funds	3207-9207	66.468	8,704,715	7,202,484 *
Beach Monitoring and Notification Program	various	66.472	226,954	8,471
Water Protection Coordination	449	66.474	309	-
Environmental Information Exchange Grant Program	various	66.608	104,575	47,241
Toxic Substances Compliance Monitoring Cooperative Agreements	243	66.701	156,091	-
TSCA Title IV State Lead Grants	330	66.707	163,616	-
Hazardous Waste Management State Program Support	230	66.801	539,874	51,476
Superfund State Site Specific Cooperative Agreements	various	66.802	220,320	-
State Underground Storage Tanks Program ("UST" Program)	various	66.804	150,413	3,482
Leaking Underground Storage Tank ("LUST") Trust Fund Program	258	66.805	538,756	15,133
State Response Program Grants	469	66.817	1,188,944	-
Total Environmental Protection Agency			<u>28,226,176</u>	<u>19,779,876</u>
<b>U.S. Department of Education</b>				
Direct Program				
Special Education – Grants for Infants and Families	213	84.181A	2,004,946	-
Pass-through from the State Department of Education				
State Improvement Grant II – Early Intervention	481	84.323	6,161	-
Special Parent Information Network	various	84.	196,808	-
Subtotal Pass-through Programs			<u>202,969</u>	<u>-</u>
Total Department of Education			<u>2,207,915</u>	<u>-</u>
<b>U.S. Department of Defense</b>				
Direct Program				
Defense Environmental Restoration Program	245	12.113	438,571	-
Total Department of Defense			<u>438,571</u>	<u>-</u>
<b>U.S. Department of Justice</b>				
Direct Program				
Enforcing Underage Drinking Laws Program	various	16.727	733,281	525,390
Total Department of Justice			<u>733,281</u>	<u>525,390</u>
<b>U.S. Department of Homeland Security</b>				
Direct Program				
Crisis Counseling	390	97.032	364,169	364,169
Pass-through from the State Department of Homeland Security				
Homeland Security Grant Program	various	97.067	14,680	-
Total Department of Homeland Security			<u>378,849</u>	<u>364,169</u>
<b>U.S. Department of Labor</b>				
Pass-through from the State Department of Labor and Industrial Relations				
WIA Pilots, Demonstrations, and Research Projects	various	17.261	277,695	65,306
Total Department of Labor			<u>277,695</u>	<u>65,306</u>
<b>Total Expenditures of Federal Awards</b>			<u>\$ 140,052,471</u>	<u>\$ 56,727,318</u>

\* Denotes Major Federal Program

**State of Hawaii**  
**Department of Health**  
**Notes to the Schedule of Expenditures of Federal Awards**  
**Year Ended June 30, 2009**

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**1. Basis of Presentation**

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the State of Hawaii, Department of Health (the "Department"), and is presented on the cash basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

**2. Loans Outstanding**

The Department had the following loan balances outstanding at June 30, 2009. Loans made during the year are included in the federal expenditures presented in the schedule of expenditures of federal awards.

<b>Program Title</b>	<b>Federal CFDA Number</b>	<b>Amount Outstanding</b>
Capitalization Grants for Clean Water State Revolving Funds	66.458	\$ 51,872,108
Capitalization Grants for Drinking Water State Revolving Funds	66.468	27,919,966

**3. Noncash Awards**

The Department also receives noncash awards in the form of vaccines that are provided to children for the Immunization Grants program. The Department expended approximately \$10,940,000 in vaccines for the fiscal year ended June 30, 2009.

**PART II**  
**Government Auditing Standards**

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

The Auditor  
State of Hawaii

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Hawaii, Department of Health (the "Department") as of and for the year ended June 30, 2009, which collectively comprise the Department's basic financial statements and have issued our report thereon dated March 25, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

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

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying schedule of findings and questioned costs as Finding Nos. 09-01 through 09-03 to be significant deficiencies in internal control over financial reporting.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider Finding Nos. 09-01 through 09-03 to be material weaknesses.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we will report to the State Auditor and management of the Department in a separate letter.

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

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

*Accuity LLP*

Honolulu, Hawaii  
March 25, 2010

**PART III**  
**OMB Circular A-133**

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

The Auditor  
State of Hawaii

**Compliance**

We have audited the compliance of the State of Hawaii, Department of Health (the "Department") with the types of compliance requirements described in the U.S. Office of Management and Budget ("OMB") *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2009. The Department's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Department's management. Our responsibility is to express an opinion on the Department's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Department's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Department's compliance with those requirements.

In our opinion, the Department complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009. The results of our auditing procedures disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as Finding Nos. 09-04 through 09-07. We also noted certain other matters that we will report to the State Auditor and management of the Department in a separate letter.

## Internal Control Over Compliance

The management of the Department is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Department's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over compliance.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the entity's internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

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

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

*Accuity LLP*

Honolulu, Hawaii  
March 25, 2010

## **PART IV**

### **Schedule Of Findings and Questioned Costs**

**State of Hawaii  
 Department of Health  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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**Section I – Summary of Auditor’s Results**

**Financial Statements**

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

**Federal Awards**

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

**Identification of major programs:**

<b>CFDA Number</b>	<b>Name of Federal Program or Cluster</b>
	<b>U.S. Department of Health &amp; Human Services</b>
93.243	Substance Abuse and Mental Health Services – Projects of Regional and National Significance
93.268	Immunization Grants
93.275	Substance Abuse and Mental Health Services – Access to Recovery
93.283	Centers for Disease Control and Prevention
93.917	HIV Care Formula Grants
93.959	Substance Abuse Prevention and Treatment Block Grants
	<b>U.S. Department of Agriculture</b>
10.557	Special Supplemental Nutrition Program for Women, Infants & Children
	<b>U.S. Environmental Protection Agency</b>
66.458	Capitalization Grants for Clean Water State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds

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

**State of Hawaii  
 Department of Health  
 Financial Statement Findings  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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**II. Financial Statement Findings**

		<b>Questioned Cost</b>
<b>Finding No. 09-01:</b>	<b>Restatement of Beginning Fund Balance / Net Assets (Material Weakness)</b>	<b>\$ _____ -</b>
<b>Federal Agency:</b>	Finding is not specific to a Federal Agency.	
<b>CFDA Number and Title:</b>	Finding is not specific to a Federal Agency.	
<b>Award Number and Award Year:</b>	Not applicable	Not applicable

**Finding and Cause and Effect**

During our current year financial statement audit of the Department's deposit beverage container fund, we identified an accounting error that resulted in the understatement of liabilities as of June 30, 2008 and overstatement of revenues for the year ended June 30, 2008. The error resulted from the lack of oversight by fiscal management over the accrual of liabilities and reconciliation of differences between the deposit beverage container fund's accounting system ("Quickbooks") and the State's Financial Accounting Management and Information System ("FAMIS"). FAMIS is maintained on the cash basis of accounting and Quickbooks is maintained on the accrual basis. Therefore, the differences were not properly reflected in the Department's financial statements.

The Department restated its opening net assets attributable to governmental activities and governmental funds' fund balances as of July 1, 2008 to correct the error. The following table reconciles the net assets attributable to governmental activities at June 30, 2008, as previously reported, to the opening net assets attributable to governmental activities at July 1, 2008, as restated:

	<b>Governmental Activities</b>
<b>Net assets at June 30, 2008, as previously reported</b>	<b>\$ 185,271,217</b>
Adjustments attributable to understatement of liabilities	<u>(5,979,815)</u>
<b>Net assets at June 30, 2008, as restated</b>	<b><u>\$ 179,291,402</u></b>

**State of Hawaii  
 Department of Health  
 Financial Statement Findings  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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The following table reconciles the governmental funds' fund balances at June 30, 2008, as previously reported, to the opening governmental funds fund balances at July 1, 2008, as restated:

	<b>Deposit Beverage Container</b>	<b>Total Governmental Funds</b>
<b>Fund balances at June 30, 2008, as previously reported</b>	\$ 24,925,040	\$ 129,313,435
Adjustments attributable to understatement of liabilities	<u>(5,979,815)</u>	<u>(5,979,815)</u>
<b>Fund balances at June 30, 2008, as restated</b>	<u>\$ 18,945,225</u>	<u>\$ 123,333,620</u>

**Criteria**

§\_\_\_.310 of OMB Circular A-133 requires the auditee to prepare financial statements that reflect its financial position, results of operations or changes in net assets and, where appropriate, cash flows for the fiscal year audited.

§\_\_\_.320 requires the auditee to submit a reporting package that includes:

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

Although audited financial statements were prepared and submitted as of and for the year ended June 30, 2008, the financial statements submitted were misstated, and restated beginning balances are reported in the financial statements as of and for the year ended June 30, 2009.

**Recommendation**

We recommend that, and the Department has already, restated the beginning balances in its basic financial statements for the year ended June 30, 2008 to correct the error identified. We also recommend that fiscal management of the Department provide greater oversight to ensure that the basic financial statements are prepared and presented in accordance with generally accepted accounting principles ("GAAP").

**State of Hawaii  
 Department of Health  
 Financial Statement Findings  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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		<b>Questioned Cost</b>
<b>Finding No. 09-02:</b>	<b>Capital Assets (Material Weakness)</b>	<b>\$ _____ -</b>
<b>Federal Agency:</b>	Finding is not specific to a Federal Agency.	
<b>CFDA Number and Title:</b>	Finding is not specific to a Federal Agency.	
<b>Award Number and Award Year:</b>	Not applicable	Not applicable

**Finding and Cause and Effect**

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

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

In the current year, we noted that completed construction projects administered by another State entity on behalf of the Department were not properly recorded in the FAIS system.

We also noted that the Department is not reporting assets in accordance with the State Inventory Manual, resulting in other audit adjustments. In the current year, we noted the following errors, which resulted in adjustments:

- Expenditures where an asset was charged under a non-fixed asset object code, resulting in the asset not being properly classified in FAMIS, hindering audit testing.
- An instance where assets were recorded twice in the same program.
- Instances where assets were recorded using the wrong acquisition dates.
- Discrepancies between the fixed asset summary and detail reports.

**State of Hawaii**  
**Department of Health**  
**Financial Statement Findings**  
**Schedule of Findings and Questioned Costs**  
**Year Ended June 30, 2009**

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- Improper recording of transfers between programs:
  - An instance where the asset being transferred was properly recorded as a transfer out, however, the transfer-in was not recorded by the other program.
  - An instance where assets were recorded with the incorrect decals resulting in the double counting of the asset in two programs.
  - An instance where assets were recorded by the program under the wrong classification (i.e., equipment vs. vehicle).
  - An instances where the assets were recorded at the wrong net book value amount.

**Criteria**

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

**Recommendation**

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

**State of Hawaii  
 Department of Health  
 Financial Statement Findings  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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		Questioned Cost
<b>Finding No. 09-03:</b>	<b>Department of Health and Human Services Transactions (Material Weakness)</b>	<b>\$ _____</b>
<b>Federal Agency:</b>	Finding is not specific to a Federal Agency.	
<b>CFDA Number and Title:</b>	Finding is not specific to a Federal Agency.	
<b>Award Number and Award Year:</b>	Not applicable	Not applicable

**Finding and Cause and Effect**

In prior audits, it was noted that the Department had difficulty determining the amounts due to and due from the Department of Human Services (“DHS”) related to the Medicaid funds. Certain of the Department’s programs are eligible to receive Medicaid funds for the Federal share of the services they provide if the services are provided to Medicaid eligible patients in the State programs.

We noted that there are several different programs within the Department that receive Medicaid funds to pay for the Federal share of the Medicaid eligible patients that are seen by the providers. Each program has a different way of tracking funds received from DHS, and each program receives different amounts of Medicaid funds depending on the agreements established with DHS.

Because of these issues, the Department continually struggles with DHS to determine amounts they are entitled to receive or need to pay. Also, because DHS did not reconcile its payment data to various data reports, the Department was overpaid which required the Department to return the overpayments to DHS. When the Department becomes aware that it may have received an overpayment, it should ensure that those funds are available to be returned to DHS when requested.

**Criteria**

In accordance with GASB 34, paragraph 12e, the Department is required to:

*“Measure and report all assets (both financial and capital), liabilities, revenues, expenses, gains, and losses using the economic resources measurement focus and accrual basis of accounting.”*

In order to report on the accrual basis of accounting, the Department needs to assess all amounts due to and from other State Agencies for services that were provided throughout the year.

In addition, the Department’s management makes the following representation to us before we issue the financial statements:

*We understand that as part of your audit, you prepared the adjusting journal entries necessary to convert our cash basis records to the accrual basis of accounting and acknowledge that we have reviewed and approved those entries and accepted responsibility for them.*

**State of Hawaii  
Department of Health  
Financial Statement Findings  
Schedule of Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Recommendation**

We continue to recommend that the Department develop a policy for preparing contracts and maintaining records of balances due to and from DHS for the programs that are eligible to receive Medicaid reimbursements. A consistent policy will assist in ensuring that the data recorded is appropriate. In addition, if the Department is aware that DHS must reconcile the data at the end of the year, which might result in the Department owing or receiving more Medicaid funds, the Department should ensure that the programs are following up with DHS on the status of the reconciliations. If the Department needs to cut current year costs to repay the prior years' shortfalls, it should ensure that management is aware of these shortfalls and can include them in the approved budget. Conversely, collections from additional receivables could help alleviate the need for other funding sources for required services.

**State of Hawaii  
 Department of Health  
 Drinking Water Treatment Revolving Loan Fund  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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**Section III. Federal Award Findings and Questioned Costs**

		<b>Questioned Cost</b>
<b>Finding No. 09-04:</b>	<b>Allowability (Set-Asides used for Grants)</b>	<b><u>\$ 75,000</u></b>
<b>Federal Agency:</b>	Environmental Protection Agency ("EPA")	
<b>CFDA Number and Title:</b>	66.468 – Capitalization Grants for Drinking Water State Revolving Funds	
<b>Award Number and Award Year:</b>	FS-99986502-1 FS-99986505-1	9/01/2002 – 9/30/2008 10/01/2005 – 6/30/2013

**Finding and Cause and Effect**

During our testing of the federal reporting compliance requirement for the Capitalization Grants for Drinking Water State Revolving Funds ("DWSRF") program (CFDA 66.468) administered by the Drinking Water Treatment Revolving Loan Fund ("DWTRLF"), we noted three grants in the amount of \$75,000 that were disbursed from the program's set-aside funds (2% set-aside for Small Systems Technical Assistance and 15% for Technical or Financial Assistance to PWS's).

In accordance with program guidelines, the State must comply with State statutes. In accordance with State statutes, there is contradictory language in the intent of the law which led us to question whether the DWSRF program is allowed to make grants. Therefore, there is a risk that the program is not in compliance with Federal and State guidelines.

**Criteria**

In accordance with the Drinking Water State Revolving Fund Program Guidelines, "The State must comply with all State statutes and regulations that are applicable to DWSRF funds, including Federal capitalization funds, State match, interest earnings, bond proceeds and repayments, and funds used for set-aside account activities".

§340E-34 of the Hawaii Revised Statutes ("HRS") states:

- (a) *The director may make grants to public water systems from state funds as authorized and appropriated by the legislature for the construction of necessary water treatment works or other related drinking water projects. Grants shall not be made from the drinking water fund.*
- (b) *The director shall coordinate the granting of state funds with available federal funds for the same purpose. Grants involving federal funds shall be consistent with federal law.*

**State of Hawaii**  
**Department of Health**  
**Drinking Water Treatment Revolving Loan Fund**  
**Schedule of Findings and Questioned Costs**  
**Year Ended June 30, 2009**

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*(c) The director may allocate grants to drinking water projects on the basis of existing health concerns. No grant shall be made for any project unless:*

- (1) The project conforms with the state grant plan to provide safe drinking water;*
- (2) The project is certified by the director as being entitled to priority over other eligible projects on the basis of financial as well as drinking water quality needs; and*
- (3) In the case of water treatment works, the applicant for the grant commits to maintain the water treatment plant efficiently and properly after its construction.*

**Recommendation**

We recommend that the program seek an opinion from the Attorney General on whether grants from the program's set aside funds are an allowable activity to ensure that the program is in compliance with State as well as Federal guidelines.

**State of Hawaii  
 Department of Health  
 Substance Abuse and Mental Health Services –  
 Mental Health Transformation State Incentive Grant  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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		<b>Questioned Cost</b>
<b>Finding No. 09-05:</b>	<b>Equipment Management</b>	<b>\$ _____ –</b>
<b>Federal Agency:</b>	Department of Health and Human Services	
<b>CFDA Number and Title:</b>	93.243 – Substance Abuse and Mental Health Services – Projects of Regional and National Significance	
<b>Award Number and Award Year:</b>	5U79SM057457-03	6/30/08 – 6/29/09

**Finding and Cause and Effect**

During our current year audit, we noted that the Mental Health Transformation State Incentive Grant (“MHT SIG”) program did not update its FAIS records to ensure additions, transfers, and disposals were properly reflected in a timely manner. In addition, we noted that the program did not use decals on additions in the current year. This is a violation of the State’s equipment management policies and procedures established in the State Inventory Manual.

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

**Criteria**

40 CFR 31.32 states that a state will use, manage, and dispose of equipment acquired in accordance with the state’s laws and procedures. Per the SPO State Inventory Manual:

- Chapter 3 – “Record keeping of property which includes accounting for all acquired state property by reconciling financial expenditures for property with property recorded in the FAIS; conducting of physical inventory; updating the master inventory listing; maintaining an accurate audit trail; and conducting internal audits.”
- Chapter 3 – “Safekeeping of property which includes affixing of property identification or decal (maintaining a decal number log, assignment of decal numbers to items and ensuring each item is properly tagged or identified); documentation for authorized loan, movement from location, and transfer to another agency; guidelines pertaining to property declared excess, surplus, obsolete, beyond economical repair, lost, or stolen; guidelines for sale of property.”
- Chapter 9 – “At the end of each quarter, but no later than the 15<sup>th</sup> of the following month, the designated property custodian submits AGS Form 17-A (Detail Inventory of Property) to the Inventory Management Office, reporting all property acquisition and changes to their master inventory balances.”
- Chapter 10 – “After the fourth quarter, before September 16 of each year, each designated property custodian must submit to the SPO, Inventory Management Office Form AGS 17-B, Annual Inventory Report.”

**State of Hawaii  
Department of Health  
Substance Abuse and Mental Health Services –  
Mental Health Transformation State Incentive Grant  
Schedule of Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Recommendation**

We recommend that the program follow the State Inventory Manual and monitor its equipment, especially properly recording, safekeeping and reporting all additions and disposals of equipment acquired during the year. We also recommend that the program adhere to the State's established policies and procedures over equipment management in order to comply with Federal and State regulations.

**State of Hawaii  
 Department of Health  
 Substance Abuse Prevention and Treatment Block Grants  
 Substance Abuse and Mental Health Services – Access to Recovery  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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		Questioned Cost
<b>Finding No. 09-06:</b>	<b>Certification for Federally Funded Employees</b>	\$ _____
<b>Federal Agency:</b>	Department of Health and Human Services (“DHHS”)	
<b>CFDA Number and Title:</b>	93. 959 – Substance Abuse Prevention & Treatment Block Grants	
	93.275 – Substance Abuse and Mental Health Services – Access to Recovery	
<b>Award Number and Award Year:</b>	B1HISAPT-08-1	10/1/08 – 9/30/09
	B1HISAPT-07-1	10/1/07 – 9/30/08
	5H79TI019437-02	9/30/08 – 9/29/09
	1H79TI019437-01	9/30/07 – 9/29/08

**Finding and Cause and Effect**

During our testing of the allowability compliance requirement for the Substance Abuse Prevention & Treatment Block Grant and the Substance Abuse and Mental Health Services – Access to Recovery grant, we noted that both programs had employees that spent 100% of their time on the grant but did not obtain semi-annual certifications signed by the employees or (per requirement stated below) their supervisors, confirming that they worked solely on grant-related activities in accordance with OMB Circular A-87 guidelines for payroll.

Although proper controls are in place to ensure that only employees that actually spend time on grant-related activities charge time to the program’s appropriation, there is no documentation maintained to confirm that this control was in place and that the time allocated to the program for these employees were periodically reviewed by the employees or their supervisors.

**Criteria**

In accordance with OMB Circular A-87, compensation for personnel services includes all remuneration, paid currently or accrued, for services rendered during the period of performance under federal awards, including but not necessarily limited to wages, salaries, and fringe benefits. The costs of such compensation are allowable to the extent that they satisfy the specific requirements of this Circular. In accordance with the Circular, where employees are expected to work solely on a single federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications will be prepared at least semi-annually and will be signed by the employee or supervisory official having first hand knowledge of the work performed by the employee.

**Recommendation**

We recommend that the programs implement a procedure to obtain semi-annual certifications from all employees that spend 100% of their time on the grants, confirming that they actually worked solely on grant-related activities. The certification should be signed by either the employee or their supervisor.

**State of Hawaii  
 Department of Health  
 HIV Care Formula Grant  
 Schedule of Findings and Questioned Costs  
 Year Ended June 30, 2009**

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		<b>Questioned Cost</b>
<b>Finding No. 09-07:</b>	<b>Allowable Costs/Cost Principles</b>	<b>\$ _____ -</b>
<b>Federal Agency:</b>	Department of Health and Human Services ("DHHS")	
<b>CFDA Number and Title:</b>	93.917 – HIV Care Formula Grants ("HIV Care")	
<b>Award Number and Award Year:</b>	2 X07HA00050-18-00	4/1/08 – 3/31/09
	2 X07HA00050-19-00	4/1/09 – 3/31/10

**Finding and Cause and Effect**

During our testing of the allowable costs/cost principles compliance requirement for the HIV Care grant, we noted that the program did not maintain adequate supporting documentation for the time charged by an employee to the grant in accordance with OMB Circular A-87 guidelines for payroll.

**Criteria**

In accordance with OMB Circular A-87, compensation for personnel services includes all remuneration, paid currently or accrued, for services rendered during the period of performance under federal awards, including but not necessarily limited to wages, salaries, and fringe benefits. The costs of such compensation are allowable to the extent that they satisfy the specific requirements of this Circular. In accordance with the circular, where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation unless a statistical sampling system or other substitute system has been approved by the cognizant Federal agency. These reports must reflect an after-the-fact distribution of the actual activity of each employee, account for the total activity for which each employee is compensated, be prepared at least monthly and coincide with one or more pay periods, and must be signed by the employee.

**Recommendation**

We recommend that the program implement a procedure to obtain monthly time and effort sheets from all employees who perform work on federal grants, ensuring that expenses charged to federal grants is for actual time spent on the respective grant. The time records should be prepared monthly and signed by the employee.

# **PART V**

## **Prior Year Findings And Questioned Costs**

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

**State of Hawaii  
 Department of Health  
 Financial Statement Findings  
 Status of Prior Year Findings and Questioned Costs  
 Year Ended June 30, 2009**

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**Finding No. 08-01: Restatement of Beginning Fund Balance/Net Assets (Material Weakness)**

During our prior year financial statement audit, we identified an accounting error in the Department's basic financial statements as of and for the year ended June 30, 2007 due to the lack of oversight by fiscal management over the accrual of liabilities. Accordingly, the Department restated its opening net assets attributable to governmental activities and governmental funds' fund balances as of July 1, 2007 to correct these errors which relate to the accounting for appropriations and amounts due to DHS.

The following table reconciles the net assets attributable to governmental activities at June 30, 2007, as previously reported, to the opening net assets attributable to governmental activities at July 1, 2007, as restated:

	<b>Governmental Activities</b>
<b>Net assets at June 30, 2007, as previously reported</b>	\$ 197,032,684
Adjustments attributable to	
Understatement of liabilities	(2,939,660)
<b>Net assets at June 30, 2007, as restated</b>	<u>\$ 194,093,024</u>

The following table reconciles the governmental funds' fund balances at June 30, 2007, as previously reported, to the opening governmental funds fund balances at July 1, 2007, as restated:

	<b>General</b>	<b>Other</b>	<b>Total Governmental</b>
<b>Fund balances at June 30, 2007, as previously reported</b>	\$ 20,758,493	\$ 67,589,250	\$ 134,386,780
Adjustments attributable to			
Understatement of liabilities	-	(2,939,660)	(2,939,660)
Transfer fund balances	(7,025,309)	7,025,309	-
<b>Fund balances at June 30, 2007, as restated</b>	<u>\$ 13,733,184</u>	<u>\$ 71,674,899</u>	<u>\$ 131,447,120</u>

We recommended that the Department restate the beginning balances in its basic financial statements for the year ended June 30, 2008 to correct the error identified. We also recommended that fiscal management of the Department provide greater oversight to ensure that the basic financial statements are prepared and presented in accordance with GAAP. The Department should also ensure that the proper amounts are received from and remitted to DHS.

**Status**

Unresolved. The restated June 30, 2007 balances were properly recorded in the fiscal 2008 financial statements. Therefore, this finding will not carry forward. However, other financial statement errors were noted during our current year audit which resulted in the restatement of \$5,979,815 in net assets attributable governmental activities and governmental funds' fund balances at June 30, 2008. See current year Finding No. 09-01.

**State of Hawaii  
Department of Health  
Financial Statement Findings  
Status of Prior Year Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Finding No. 08-02: Capital Assets (Material Weakness)**

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

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

We also noted that the Department was not reporting assets in accordance with the State Inventory Manual, resulting in other audit adjustments.

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

**Status**

Unresolved. During our current audit, we continued to note numerous instances where capital assets were purchased, but were not reported to FAIS. Since the Department is in the process of implementing our recommendation above in conjunction with its implementation of our recommendation in the current year Finding No. 09-02, this finding will not carry forward.

**State of Hawaii  
Department of Health  
Financial Statement Findings  
Status of Prior Year Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Finding No. 08-03: Department of Human Services Transactions (Material Weakness)**

In prior year audits, it was noted that the Department had difficulty determining the amounts due to and due from DHS related to the Medicaid funds. Certain of the Department's programs are eligible to receive Medicaid funds for the Federal share of the services they provide if the services are provided to Medicaid eligible patients in the State programs.

We noted that there are several different programs within the Department that receive Medicaid funds to pay for the Federal share of the Medicaid eligible patients that are seen by the providers. Each program has a different way of keeping track of the funds that are received from DHS, and each department gets different amounts of Medicaid funds depending on how the programs are set up with DHS.

Because of these issues, the Department continually struggles with DHS to determine amounts they are entitled to receive or need to pay. Also, because DHS did not reconcile its payment data to various data reports, the Department was overpaid which required the Department to return the overpayments to DHS. When the Department becomes aware that it may have received an overpayment, it should ensure that those funds are available to be returned to DHS when requested.

The payable and receivable information is required to be maintained on a full accrual basis for the Department's department-wide statement of net assets.

We recommended that the Department develop a policy for establishing contracts and maintaining records and balances due to and from DHS for the programs that are eligible to receive Medicaid reimbursements. A consistent policy will assist in ensuring that the data that is recorded is appropriate. In addition, if the Department is aware that DHS has to reconcile the data at the end of the year, which might result in the Department owing or receiving more Medicaid funds, the Department should ensure that the programs regularly inquire with DHS on the status of the reconciliations. If the Department needs to cut current year costs to repay the prior years' shortfalls, management must know of these shortfalls and include them in the approved budget. On the other hand, any additional money that the Department could receive would help to alleviate other funding sources that are required to provide the required services.

**Status**

Unresolved. During our current audit, we noted that the Department did not implement a policy to track all balances due to and from DHS and that there was continued difficulty in determining the actual amounts. Since the Department is in the process of implementing our recommendation above in conjunction with its implementation of our recommendation in the current year Finding No. 09-03, this finding will not carry forward.

**State of Hawaii  
Department of Health  
HIV Care Formula Grants  
Status of Prior Year Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Finding No. 08-04: Reporting (Material Weakness)**

During our prior year audit, we also noted the following instances of noncompliance with federal reporting requirements for the HIV Care Formula Grants ("HIV Care") program (CFDA 93.917):

- Maintenance of Effort Report: The amount of State expenditures for FY 2007 was reported as \$4,990,742 compared to \$4,591,930 in actual expenditures.
- The Annual Financial Status Reports, Standard Form ("SF")-269a was submitted approximately three months after the due date, which is submitted by ASO.
- The Final Annual Progress Report was submitted approximately one month after the due date.

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

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

**Status**

Resolved. In the current year audit, we confirmed with the granting agency that reporting on the Maintenance of Effort Report was in line with its requirements. Consequently, this finding will not carry forward.

**State of Hawaii  
Department of Health  
HIV Care Formula Grants  
Status of Prior Year Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Finding No. 08-05: Eligibility (Material Weakness)**

During our prior year audit of the HIV Care program, we tested 40 ADAP patient records and 10 H-COBRA patient records. Due to the Department maintaining insufficient supporting documents, we noted the numerous instances of noncompliance with eligibility requirements for the HIV Care program for both the ADAP and H-COBRA participants.

We recommended that the HIV program conduct initial eligibility certifications and semi-annual eligibility recertifications of all participants as required by federal and State program guidelines. In addition, program personnel should review all case files without exception to ensure that all participant files contain the required documentation.

We also recommended that the HIV program request that the recertification requirement be extended because it is difficult to get patients to recertify when their prescriptions are longer than six months.

**Status**

Resolved. In the current year audit, there were no instances of noncompliance that were noted in the prior years. This was the result of the State waiving the requirement of requiring documentation for the client's estimated value of liquid assets. In addition, there were several patients who were removed from the program because they did not obtain the semi-annual certifications as required. Consequently, this finding will not carry forward.

**State of Hawaii  
Department of Health  
HIV Care Formula Grants  
Status of Prior Year of Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Finding No. 08-06: Earmarking (Material Weakness)**

During our prior year audit of the HIV Care program, we noted the following instance of noncompliance with earmarking requirements for amounts expended on women, infants, children and youth during the grant period. The amount expended was \$303,360, which was \$106,165 less than required by terms of the applicable grant. The shortfall was due primarily to the fact that the need for services for women, infants and children was less than the amount of funds available.

We recommended that program personnel continue to monitor expenditures for specific purposes and ensure compliance with earmarking provisions. Program personnel responsible for monitoring compliance with earmarking provisions should continue to ensure that the providers are aware that the funding is available, should the need arise. The program personnel are aware of the issues and continue to work with service providers to ensure that all individuals in the target population are served.

**Status**

Resolved. In the current year the HIV Care Program was able to meet the earmarking requirements. Consequently, this finding will not carry forward.

**State of Hawaii  
Department of Health  
Centers for Disease Control –  
National Cancer Prevention and Control Branch  
Status of Prior Year Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Finding No. 08-07: Equipment Management**

During our prior year audit, we noted one instance of theft occurred during the prior fiscal year at the Centers for Disease Control and Prevention Investigations and Technical Assistance Program – National Cancer Prevention and Control Branch (“NCPC”) program (CFDA 93.283). We noted that the item that was stolen or misplaced was a laptop computer that may have contained sensitive client information, because of the type of services the program provides to individuals, and the access to information that may have been stored on the computer.

We recommended that the program follow the SPO manual and monitor its equipment, especially theft sensitive equipment, in order to prevent any future thefts from occurring. We also recommended that policies and procedures for monitoring data access are identified, especially for those individuals who deal with sensitive information.

**Status**

Resolved. As the asset was properly disposed of in the prior year, it appears that the program has the proper procedures in place. Consequently, this finding will not carry forward.

**State of Hawaii  
Department of Health  
Public Health Emergency Preparedness  
HIV Care Formula Grants  
Status of Prior Year Findings and Questioned Costs  
Year Ended June 30, 2008**

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**Finding No. 08-08: Certification for Federally Funded Employees**

During our testing of the allowability compliance requirement for the Public Health Preparedness and Response for Bioterrorism program (CFDA 93.069) and the HIV Care program, we noted that both programs had employees that spent 100% of their time on the grant but did not obtain semi-annual certifications signed by the employees or their supervisors, confirming that they worked solely on grant-related activities in accordance with OMB Circular A-87 guidelines for payroll.

We recommended that the programs implement a procedure to obtain semi-annual certifications from all employees that spend 100% of their time on the grants, confirming that they actually worked solely on grant-related activities. The certification should be signed by either the employee or their supervisor.

**Status**

Resolved. In the current year, we noted that both programs had certifications for their federally funded employees that were properly signed. As such, it appears that the finding is resolved and will not carry forward.

**State of Hawaii  
Department of Health  
Centers for Disease Control and Prevention  
Special Supplemental Nutrition Program for Women, Infants, and Children  
Status of Prior Year Findings and Questioned Costs  
Year Ended June 30, 2009**

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**Finding No. 06-08: Cash Management**

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

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

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

**Status**

Unresolved. We continued to find that neither the Special Supplemental Nutrition Program for Women, Infants, and Children ("WIC") program (CFDA 10.557) nor Centers for Disease Control ("CDC") programs (CFDA 93.283) are calculating interest on the funds drawn down in advance.

We were also still unable to verify whether the Department and DAGS complied with the Cash Management Improvement Act's requirement to minimize the time between the transfer of funds from the U.S. Treasury and disbursement by the Department.

**State of Hawaii  
Department of Health  
HIV Care Formula Grants  
Status of Prior Year Findings and Questioned Costs  
Year Ended June 30, 2008**

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

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

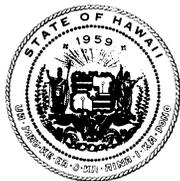
We recommended that the Department finalize and implement its Quality Assurance Plan to ensure compliance with PHS guidelines and enable the Department to effectively monitor its HIV Care programs.

**Status**

Resolved. The Quality Assurance Plan was created and was in place in fiscal year 2009. The program continues to ensure that the plan is implemented as required. Consequently, this finding will not carry forward.

## **Corrective Action Plan**

LINDA LINGLE  
GOVERNOR OF HAWAII



CHIYOME LEINAALA FUKINO, M.D.  
DIRECTOR OF HEALTH

**STATE OF HAWAII**  
**DEPARTMENT OF HEALTH**  
P.O. BOX 3378  
HONOLULU, HAWAII 96801-3378

In reply, please refer to  
File:

ASO-F/10-5881

March 23, 2010

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

Dear State Auditor:

Attached are the Department of Health's Corrective Action Plan for the findings on the audit report for fiscal year 2009 and comments regarding prior year findings.

We appreciate the opportunity to comment on the audit report.

Sincerely,

Chiyome Leinaala Fukino, M.D.  
Director of Health

Attachment

## **II. Financial Statement Findings**

### **Finding Nos. 09-01 and 08-01: Restatement of Beginning Fund Balance/Net Assets (Material Weakness)**

#### **Finding and Cause and Effect**

During our current year financial statement audit of the Department's deposit beverage container fund, we identified an accounting error that resulted in the understatement of liabilities as of June 30, 2008 and overstatement of revenues for the year ended June 30, 2008. The error resulted from the lack of oversight by fiscal management over the accrual of liabilities and reconciliation of differences between the deposit beverage container fund's accounting system ("Quickbooks") and the State's Financial Accounting Management and Information System ("FAMIS"). FAMIS is maintained on the cash basis of accounting and Quickbooks is maintained on the accrual basis. Therefore, the differences were not properly reflected in the Department's financial statements.

#### **Corrective Action Plan**

The Department has already restated the beginning balances in the financial statements for the year ended June 30, 2008 to correct the error identified. The new Departmental Fiscal Officer will assist the program in reviewing the reporting process and implementing recommendations for improvement to ensure that basic financial statements are prepared and presented in accordance with generally accepted accounting principles ("GAAP").

#### **Person Responsible**

ASO Fiscal Officer

#### **Anticipated Date of Completion**

June 30, 2010

### **Finding No. 09-02 and 08-02: Capital Assets (Material Weakness)**

#### **Finding and Cause and Effect**

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

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

### **Corrective Action Plan**

The Department continues to transmit the quarterly listing of fixed assets and the FAIS inventory reports to the programs. After finishing the reconciliations and resolving any discrepancies, the programs send the completed reports to ASO and ASO, in turn, transmits these reports to SPO. The ASO monitors the programs and continues to assist the programs to ensure fixed assets are properly recorded in accordance with the policies and procedures in the DAGS-SPO-Inventory Management Branch Training Manual.

### **Person Responsible**

ASO Procurement and Supply Specialist and the Public Health Administration Officer for each program

### **Anticipated Date of Completion**

July 1, 2010

## **Finding No. 09-03 and 08-03: Department of Human Services Transactions (Material Weakness)**

### **Finding and Cause and Effect**

In prior audits, it was noted that the Department had difficulty determining the amounts due to and due from the Department of Human Services ("DHS") related to the Medicaid funds. Certain of the Department's programs are eligible to receive Medicaid funds for the federal share of the services they provide if the services are provided to Medicaid eligible patients in State programs.

We noted that there are several different programs within the Department that receive Medicaid funds to pay for the federal share of the Medicaid eligible patients that are seen by the providers. Each program has a different way of tracking the funds that are received from DHS, and each program receives different amounts of Medicaid funds depending on the agreements established with DHS.

Because of these issues, the Department continually struggles with DHS to determine amounts they are entitled to receive or need to pay. Also, because DHS did not reconcile its payment data to various data reports, the Department was overpaid which required the Department to return the overpayments to DHS. When the Department becomes aware that it may have received an overpayment, it should ensure that those funds are available to be returned to DHS when requested.

### **Corrective Action Plan**

To ensure standardized reporting, the Fiscal Staff of the Administrative Services Office (ASO) developed a reporting format to be used by the DOH programs that receive Medicaid reimbursements and distributed the format to the programs on January 25, 2010. This report will be submitted to the ASO on a monthly basis.

### **Person Responsible for Corrective Action**

ASO Accountant V and Public Health Administrative Officers of programs receiving Medicaid reimbursements

### **Anticipated Date of Completion**

January 25, 2010

## **Section III. Federal Award Findings and Questioned Costs**

### **Finding Nos. 09-04: Allowability (Set-Asides used for Grants)**

#### **Finding and Cause and Effect**

During our testing of the federal reporting compliance requirements for the Capitalization Grants for Drinking Water State Revolving Funds ("DWSRF") program (CFDA 66.468) administered by the Drinking Water Treatment Revolving Loan Fund ("DWTRLF"), we noted three grants in the amount of \$75,000 that were disbursed from the program's set-aside funds (2% set-aside for Small Systems Technical Assistance and 15% for Technical or Financial Assistance to PWS's).

In accordance with program guidelines, the State must comply with State statutes. In accordance with State statutes, there is contradictory language in the intent of the law which led us to question whether or not grants are allowed to be made from the DWTRLF program. Therefore, there is risk that the program is not in compliance with Federal and State guidelines.

#### **Corrective Action Plan**

The Safe Drinking Water Branch will be seeking advice from the Department of the Attorney General to clarify this issue.

#### **Person Responsible for Corrective Action**

Safe Drinking Water Branch Chief

**Anticipated Completion Date**

December 1, 2010

**Finding Nos. 09-05: Equipment Management**

**Finding and Cause and Effect**

During our current year audit, we noted that the Mental Health Transformation State Incentive Grant ("MHT SIG") program did not update its FAIS records to ensure additions, transfers, and disposals were properly reflected in a timely manner. In addition, we noted that the program did not use decals on additions in the current year. This is a violation of the State's equipment management policies and procedures established in the State Inventory Manual.

**Corrective Action Plan**

MHT SIG is in the process of implementing the inventory procedures set forth in the State Procurement Office Inventory Management Manual. The completion of AGS Form 17-A will be added as a required step to procurement of items that fall under non-expendable state property and theft sensitive property to update its FAIS records. For inventory additions in the current year and prior years, AGS Form 17-A will be completed and, upon receipt of the decals, the respective items will be affixed with the decals in a timely manner. MHT SIG will follow the State's established policies and procedures for equipment management to ensure compliance with Federal and State regulations.

**Person Responsible**

MHT SIG Chief Operations Officer

**Anticipated Date of Completion**

May 28, 2010

**Finding Nos. 09-06: Certification for Federally Funded Employees**

**Finding and Cause and Effect**

During our testing of the allowability compliance requirement for the Substance Abuse Prevention & Treatment Block Grant and the Substance Abuse and Mental Health Services - Access to Recovery grant, we noted that both programs had employees that spent 100 percent of their time on the grant but did not obtain semi-annual certifications signed by the employees or (per requirement state below) their supervisors, confirming that they worked solely on grant related activities in accordance with OMB Circular A-87 guidelines for payroll.

Although proper controls are in place to ensure that only employees that actually spend time on grant-related activities charge time to the program's appropriation, there is no documentation

maintained to confirm that this control was in place and that the time allocated to the program for these employees were periodically reviewed by the employees or their supervisors

**Corrective Action Plan**

The ADAD has implemented an internal procedure to require supervisors of all federally funded employees to be responsible for completion of the semi-annual certifications. Certifications are to be completed and signed by the supervisors then submitted to the Division PHAO for review and record keeping.

**Person Responsible**

Division PHAO

**Anticipated Date of Completion**

April 1, 2010

**Finding No. 09-07: Allowable Costs/cost Principles (Control Deficiency)**

**Finding and Cause and Effect**

During our testing of the allowable costs/cost principles compliance requirement for the HIV Care grant, we noted that the program did not maintain adequate supporting documentation for the time charged by an employee to the grant in accordance with OMB Circular A-87 guidelines for payroll.

**Corrective Action Plan**

SAPB has implemented a procedure to obtain semi-annual certifications from all employees that spend 100 percent of their time on the grant, confirming that they actually worked solely on grant related activities.

For those employees who are funded by different federal grants and their total time equals 100 percent, SAPB will implement procedures to obtain monthly time and effort sheets from these employees to ensure that expenses charged to each of the federal grants involved represents the employee's actual time spent on the respective grant.

**Person Responsible for Corrective Action**

Public Health Administrative Services Officer

**Anticipated Date of Completion**

July 1, 2010

## **Finding No. 06-08: Cash Management**

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

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

### **Corrective Action Plan**

The Department of Health is part of the Executive Branch of the State of Hawaii. As such, the Department must follow the accounting guidelines and procedures provided by the State Department of Accounting and General Services (DAGS). DAGS requires that all cash receipts and disbursements must be recorded in the State's Financial Accounting Management and Information System. Because there are two accounting systems (State and Federal) involved in the cash management for federal grants, the Department is unable to meet the requirements of the federal 3-day drawdown rule which results in payment delays.

### **Person Responsible for Corrective Action**

Administrative Services Officer and Fiscal Officer

### **Anticipated Date of Completion**

Not applicable.