OVERVIEW

Audit of the Office of Hawaiian Affairs

Report No. 01-06, March 2001

Summary

The Office of Hawaiian Affairs (OHA) is a state agency responsible for improving the conditions of all persons of Hawaiian ancestry. During FY1998-99 OHA received nearly $5 million in general and federal funding to be used for this purpose. Its share of ceded land revenues paid in that year totaled $15 million. It also earned $11 million in dividends and interest. In addition, OHA's investment portfolio was valued at approximately $350 million at the close of that fiscal year. This audit assesses the adequacy of OHA's management of these resources, its efforts to improve the conditions of all Hawaiians, and the efficiency of the agency's organizational structure.

We found the Board of Trustees has not adequately planned to improve the conditions of Hawaiians. The board has allowed OHA's master and functional plans to remain outdated and has inefficiently planned for program expenditures. For example, during FY1998-99 the trustees spent approximately $13 million on unplanned expenses—exceeding OHA's budget by 100 percent. Although the board recently adopted a spending policy to balance spending for current beneficiaries while reserving assets for future generations, it failed to coordinate this policy with other plans that are intricately related to spending.

The board also failed to uphold its fiduciary duties and inefficiently managed OHA's public land trust funds. We found certain trustees misused funds for personal needs. Two trustees used over $8,000 in personal expense allowances to make interest-free loans to themselves and family members, while another trustee spent over $1,000 on beauty salon services over a three-year period. The board did not invest in international equities for many years although required to do so by OHA's investment policy. In fact, Morgan Stanley Dean Witter, OHA's former investment consultant, estimated that OHA could have earned approximately $2 million if the former board chair and the agency's administrator had not delayed hiring two international money managers selected by the board. Moreover, the board failed to terminate under-performing fund managers in a timely manner which further decreased the overall value of OHA's investment portfolio by approximately $1 million.

OHA did not ensure that funds disbursed from its grant and Native Hawaiian Revolving Loan Fund programs were well spent. OHA awarded over $900,000 in grants during FY1998-99 without ensuring that the recipient agencies indeed provided services to Hawaiians. We also found that loan funds were disbursed to beneficiaries without assessing whether these individuals would be able to repay. Moreover, funds were disbursed prior to receipt of loan-closing documents, and staff failed to implement collection controls for accounts in arrears. Consequently,

the solvency of this fund was jeopardized. As of June 30, 2000, 158 loans with a combined balance of $4.6 million were outstanding. Approximately half of this amount was past 90 days due.

We reviewed OHA's organizational effectiveness and concluded that OHA's on-going reorganization has led to a state of crisis. Staff are unsure of their duties and responsibilities because the administrator hastily reassigned staff to new positions for which approved position descriptions were lacking. In fact, some of these staff do not appear to be qualified for their positions. An exodus of knowledgeable staff has also hurt OHA. The reorganization has led other staff to resign who were not afforded the opportunity to grieve the administrator's actions.

Recommendations and Response

We recommended that the board direct its attention to identifying OHA's role in improving the conditions of all Hawaiians, and fulfill its fiduciary duties and improve its management of OHA's investments. We recommended that OHA improve its management of its grant and Native Hawaiian Revolving Loan Fund programs. We also recommended that the board develop clear policies and procedures for effecting organizational change that requires careful planning prior to implementation.

The board did not dispute any of our audit recommendations and responded that it has much to accomplish. The board described steps it has already taken as well as timeframes for implementing changes to address our audit findings and recommendations. The board disagreed with some of our findings and agreed with others. Specifically, the board agreed that it needs to update key planning documents; however, the board disagrees that it lacks the leadership and direction needed to improve the conditions of Hawaiians. The board agrees that improvements are needed in trustee expense accounts and that it failed to comply with the guidelines established in its investment policy. Although these guidelines were developed to ensure superior return rates, the board responded that its non-compliance did not result in any *overall* losses during 1999. This response does not sufficiently address the long-term effect of non-compliance. In fact, the board's own written response indicates that it did not meet the policy benchmark in three of the past four years.

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