FINANCIAL AUDIT OF
OFFICE OF THE AUDITOR
STATE OF HAWAII

FOR THE
FISCAL YEAR ENDED JUNE 30, 2015
(With Independent Auditor's Reports)

OFFICE OF THE AUDITOR
STATE OF HAWAII

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CHOO, OSADA & LEE, CPAs, INC.
CERTIFIED PUBLIC ACCOUNTANTS

1136 12TH AVENUE
SUITE 240
HONOLULU, HAWAII 96816

TELEPHONE (808) 734-1921

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

To the State Auditor
Office of the Auditor
State of Hawaii

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and the general fund of the Office of the Auditor of the State of Hawaii (Agency) as of and for the year ended June 30, 2015, and the related notes to the financial statements, which comprise the Agency's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. 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. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the general fund of the Agency as of June 30, 2015 and the respective changes in financial position thereof and the respective budgetary comparison for the general fund for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements of the Agency are intended to present the financial position and the changes in financial position of only that portion of the governmental activities and general fund of the State of Hawaii that is attributable to the transactions of the Agency. They do not purport to, and do not, present fairly the financial position of the State of Hawaii as of June 30, 2015 and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standard Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 22, 2016, on our consideration of the Agency's internal control over financial reporting and 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 the 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* in considering the Agency's internal control over financial reporting and compliance.

Choo, Osada & Lee, CPAs, Inc.

Honolulu, Hawaii
March 22, 2016

OFFICE OF THE AUDITOR
STATE OF HAWAII
MANAGEMENT'S DISCUSSION AND ANALYSIS
FISCAL YEAR ENDED JUNE 30, 2015

This Management's Discussion and Analysis provides an overview of the financial activities of the Office of the Auditor of the State of Hawaii ("Agency") for the fiscal year ended June 30, 2015. Readers should consider the information presented here in conjunction with the basic financial statements as a whole.

Overview of the Basic Financial Statements

This discussion and analysis is intended to serve as an introduction to the Agency's basic financial statements. The Agency's basic financial statements are comprised of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the basic financial statements.

Government-Wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the Agency's finances in a manner similar to private-sector companies.

The Statement of Net Position presents information on all of the Agency's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Agency is improving or deteriorating.

The Statement of Activities presents information showing how the Agency's net position changed during the fiscal year. This statement shows the extent to which the Agency's activities depend on state appropriations for support.

The Statement of Net Position, and the Statement of Activities can be found in the Statement of Net Position and Governmental Fund Balance Sheet, and in the Statement of Activities and Governmental Fund Revenues, Expenditures and Changes in Fund Balance, respectively, which immediately follow this discussion and analysis.

Fund Financial Statements

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 Agency's funds are comprised solely of governmental funds.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on the balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the Agency's near-term financing requirements.

Because the focus of governmental funds is narrower than that of government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities of the government-wide financial statements. By doing so, readers may better understand the long-term impact of the Agency's near-term financing decisions. Both the Statement of Net Position and Governmental Fund Balance Sheet, and the Statement of Activities and Governmental Fund Revenues, Expenditures and Changes in Fund Balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The Agency maintains a single governmental fund, its General Fund.

The basic governmental fund financial statements can be found in the Statement of Net Position and Governmental Fund Balance Sheet, and in the Statement of Activities and Governmental Fund Revenues, Expenditures and Changes in Fund Balance, respectively, which immediately follow this discussion and analysis.

Notes to the Basic Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the governmental-wide and fund financial statements. The notes can be found immediately following the basic financial statements.

Condensed Financial Information

The following are summaries from the Agency's government-wide financial statements as of and for the fiscal years ended June 30, 2015 and 2014.

Table 1
Condensed Summary of Net Position

	2015	2014
Assets:		
Current assets	$ 7,701,318	$ 7,393,945
Capital assets	69,030	68,347
Total assets	$ 7,770,348	$ 7,462,292
Liabilities:		
Current liabilities and other liabilities	$ 439,073	$ 313,572
Long-term liabilities	215,240	212,655
Total liabilities	$ 654,313	$ 526,227
Net position:		
Invested in capital assets	$ 69,030	$ 68,348
Unrestricted	7,047,005	6,867,717
Total net position	$ 7,116,035	$ 6,936,065

Table 2
Condensed Summary of Revenues, Expenses, and Changes in Net Position

	Governmental Activities	
	2015	2014
General revenues		
State appropriations, net of lapsed amounts	$ 5,188,630	$ 5,022,182
State-provided payroll fringe benefits	873,531	898,671
Interest	21,909	21,205
Reimbursements	2,956,242	2,678,165
Total general revenues	9,040,312	8,620,223
Expenses		
Current		
Personal services	2,926,289	3,127,865
Contractual services	5,737,304	5,110,722
Depreciation	15,858	14,255
Dues and subscriptions	58,166	29,205
Equipment rental and maintenance	17,784	16,543
Office supplies and postage	9,521	7,422
Printing	4,883	3,313
Telephone	16,244	16,443
Training	22,022	7,003
Travel and subsistence, in-state	6,380	4,402
Travel and subsistence, out-of-state	30,825	25,493
Other	1,009	2,309
Capital outlays		
Equipment and furniture	14,057	11,816
Total expenses	8,860,342	8,376,791
Change in net position	179,970	243,432
Beginning net position	6,936,065	6,692,633
Ending net position	$ 7,116,035	$ 6,936,065

Analysis of Overall Financial Position and Results of Operations

Overall Financial Position

Assets of the Agency exceeded its liabilities by $7,116,035 as of June 30, 2015.

The surplus in total government-wide net position increased by $179,970, or 2.59 percent over the prior fiscal year.

Results of Operations

State appropriations, net of lapsed amounts, totaled $5,188,630, an increase of $166,448 or 3.31 percent over the prior fiscal year. The increase was due to the decrease in amounts lapsed.

State-provided payroll fringe benefits, totaled $873,531, a decrease of $25,140 or 2.80 percent over the prior fiscal year. The decrease was due to a decrease in personal services over the prior fiscal year.

Total expenses amounted to $8,860,342, an increase of $483,551 or 5.77 percent over the prior fiscal year. Items contributing to the increase included an increase in contractual services, training and travel.

Analysis of Agency's Individual Funds

Governmental Funds

The focus of the Agency's governmental fund is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in evaluating the Agency's financing requirements. In particular, unreserved fund balances may serve as a useful measure of the Agency's net resources available for spending next year.

At the end of the fiscal year, the Agency's governmental fund (general fund) reported an ending fund balance of $7,369,161, an increase of $167,016 or 2.32 percent from the prior fiscal year. The entire fund balance was unassigned or assigned.

General Fund Budget

The fiscal year budget for the Agency's General Fund remained the same from the original to the final budget.

Actual personal services on a budgetary basis were less than the budgeted amount by $335,780 or 13.86 percent. The difference was primarily attributable to vacant staff positions.

Contractual services on a budgetary basis were less than the budgeted amount by $1,014,837 or 15.27 percent. The difference was primarily attributable to decreases in cost of consultant contracts.

Capital Assets and Long-Term Debt

At June 30, 2015, the Agency had capital assets, net of accumulated depreciation, of $69,030. There was an increase in capital assets (additions, deductions, and depreciation) of $683 or 1.00 percent from the prior fiscal year. Further details can be found in Note 7 to the basic financial statements.

At June 30, 2015, the Agency had long-term liabilities of $215,240, consisting of the liabilities for employees' compensated absences due after one year. There was an increase of $2,585 or 1.22 percent from the prior fiscal year. Further details can be found in Note 8 to the basic financial statements.

Currently Known Facts and Conditions

The 2014 State Legislature provided the Agency a flat budget for fiscal year 2014-2015. No other events or factors that may impact future periods are anticipated at this time.

OFFICE OF THE AUDITOR
STATE OF HAWAII
STATEMENT OF NET POSITION AND GOVERNMENTAL FUND BALANCE SHEET
JUNE 30, 2015

	General Fund	Adjustments (Note 3)	Statement of Net Position
ASSETS			
Cash and cash equivalents	$ 7,633,063	$ -	$ 7,633,063
Reimbursements receivable from State of Hawaii departments and agencies	68,255	-	68,255
Capital assets			
Depreciable, net of accumulated depreciation of $79,397	-	69,030	69,030
Total assets	$ 7,701,318	$ 69,030	$ 7,770,348
LIABILITIES			
Vouchers and contracts payable	$ 177,497	$ -	$ 177,497
Accrued wages and employee benefits payable	152,660	-	152,660
Due to State of Hawaii	2,000	-	2,000
Compensated absences			
Due within one year	-	106,916	106,916
Due after one year	-	215,240	215,240
Total liabilities	332,157	322,156	654,313
FUND BALANCE/NET POSITION			
Fund balance			
Assigned	4,999,166	(4,999,166)	-
Unassigned	2,369,995	(2,369,995)	-
Total fund balance	7,369,161	(7,369,161)	-
Total liabilities and fund balance	$ 7,701,318		
Net position			
Invested in capital assets		69,030	69,030
Unrestricted		7,047,005	7,047,005
Total net position		$ 7,116,035	$ 7,116,035

See accompanying notes.

OFFICE OF THE AUDITOR
STATE OF HAWAII
STATEMENT OF ACTIVITIES AND GOVERNMENTAL FUND REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
FISCAL YEAR ENDED JUNE 30, 2015

	General Fund	Adjustments (Note 4)	Statement of Activities
General revenues			
State appropriations, net of lapsed amount of $558,719	$ 5,188,630	$ -	$ 5,188,630
State-provided payroll fringe benefits	873,531	-	873,531
Interest	21,909	-	21,909
Reimbursements	2,956,242	-	2,956,242
Total general revenues	9,040,312	-	9,040,312
Expenditures/expenses			
Audit services			
Current			
Personal services	2,938,560	(12,271)	2,926,289
Contractual services	5,737,304	-	5,737,304
Depreciation	-	15,858	15,858
Dues and subscriptions	58,166	-	58,166
Equipment rental and maintenance	17,784	-	17,784
Office supplies and postage	9,521	-	9,521
Printing	4,883	-	4,883
Telephone	16,244	-	16,244
Training	22,022	-	22,022
Travel and subsistence, in-state	6,380	-	6,380
Travel and subsistence, out-of-state	30,825	-	30,825
Other	1,009	-	1,009
Capital outlays			
Equipment and furniture	30,598	(16,541)	14,057
Total expenditures/expenses	8,873,296	(12,954)	8,860,342
Excess of revenues over expenditures	167,016	12,954	179,970
Net change in fund balance	167,016	(167,016)	-
Change in net position	-	179,970	179,970
Fund balances/net position			
Beginning of the fiscal year	7,202,145	(266,080)	6,936,065
End of the fiscal year	$ 7,369,161	$ (253,126)	$ 7,116,035

See accompanying notes.

OFFICE OF THE AUDITOR
STATE OF HAWAII
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FISCAL YEAR ENDED JUNE 30, 2015

	Final	Actual on Budgetary Basis	Variance
Budgetary Balance at July 1, 2014	$ 3,016,264	$ 3,016,264	$ -
Resources (inflows)			
State appropriations	5,747,349	5,747,349	-
Interest	-	21,909	(21,909)
Reimbursements	483,736	2,887,987	(2,404,251)
Amounts available	9,247,349	11,673,509	(2,426,160)
Charges to appropriations (outflows)			
Current			
Personal services	2,422,349	2,086,569	335,780
Contractual services	6,644,916	5,630,079	1,014,837
Equipment rental and maintenance	20,000	18,980	1,020
Office supplies and postage	45,500	77,095	(31,595)
Printing	7,000	4,883	2,117
Training	12,000	22,022	(10,022)
Travel and subsistence, in-state	4,800	6,380	(1,580)
Travel and subsistence, out-of-state	42,000	39,348	2,652
Other	2,000	1,759	241
Capital outlays			
Equipment, furniture and books	46,784	32,094	14,690
	9,247,349	7,919,209	1,328,140
Lapsed appropriations	-	558,719	(558,719)
Budgetary Balance at June 30, 2015	$ -	$ 3,195,581	$ (3,195,581)

See accompanying notes.

OFFICE OF THE AUDITOR
STATE OF HAWAII
BUDGETARY RECONCILIATION - GENERAL FUND
FISCAL YEAR ENDED JUNE 30, 2015

Sources/inflows of resources	
Actual amounts (budgetary basis) available	$ 11,673,509
Differences between budgetary basis and GAAP basis	
Lapsed appropriations	(558,719)
On-behalf fringe benefits	873,531
Reimbursements receivable from State of Hawaii departments and agencies	68,255
Revolving fund beginning balance	(3,016,264)
Total revenues per governmental fund financial statement	$ 9,040,312
Uses/outflows of resources	
Actual amounts (budgetary basis) charged to appropriations	$ 7,919,209
Differences between budgetary basis and GAAP basis	
Reserved for encumbrances	(4,816,244)
Expenditures for liquidation of prior fiscal year encumbrances	4,743,669
Expenditures of future appropriations	153,131
On-behalf fringe benefits	873,531
Total expenditures per governmental fund financial statement	$ 8,873,296

See accompanying notes.

NOTE 1 - FINANCIAL REPORTING ENTITY

The Office of the Auditor (Agency) is a governmental unit of the State of Hawaii (State) Legislative Branch and conducts post-audits of the transactions, accounts, programs and performance of all departments, offices, and agencies of the State and its political subdivisions.

These basic financial statements reflect only the Agency's portion of financial transactions and activities. The State Comptroller maintains the central accounts for all state funds and publishes financial statements for the State annually which includes the Agency's financial activities. The Agency utilizes office space in a State building and, accordingly, no expenditure is recorded for such space.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

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

The government-wide financial statements report all assets, liabilities, and activities of the Agency as a whole. They include all funds of the reporting entity except for fiduciary funds.

Net position is restricted when constraints placed on it are either externally imposed or imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net position. When both restricted and unrestricted resources are available for use, it is generally the Agency's policy to use restricted resources first, then unrestricted resources as they are needed.

Fund financial statements are organized on the basis of funds, each of which is considered to be a separate accounting entity. The operations of each accounting fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund balances, revenues and expenditures. The Agency uses fund accounting to report on its financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

Governmental Funds Types

The Agency has only one governmental fund, which is the general fund, and no proprietary fund operations.

The general fund is used to account for all of the Agency's financial resources. The annual operating budget as authorized by the State Legislature provides the basic framework within which the resources and obligations of the general fund are accounted for.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - continued

Measurement Focus and Basis of Accounting

Government-wide financial statements - Government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when they are earned and expenses are recorded at the time liabilities are incurred or economic assets used. Revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place.

In addition, amounts paid to acquire capital assets are capitalized as assets in the government-wide financial statements rather than reported as an expenditure. Amounts paid to reduce long-term indebtedness of the reporting government are reported as a reduction of the related liability, rather than as an expenditure.

Governmental fund financial statements - Governmental fund financial statements are reported using the current financial resources management focus and on the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recorded when susceptible to accrual, i.e., both measurable and available, usually when the appropriations are allotted. Expenditures are generally recognized when the related liability is incurred, except for accumulated unpaid vacation, which are recognized as expenditures when payable from expendable available resources.

Amounts expended to acquire capital assets are recorded as expenditures in the fiscal year that resources were expended, rather than as fund assets. Expenditures related to compensated absences are recorded only when payment is due.

Encumbrances are recorded obligations in the form of purchase orders or contracts. The State records encumbrances at the time purchase orders or contracts are awarded and executed. Encumbrances outstanding at fiscal year-end do not constitute expenditures or liabilities.

Governmental entities with a single governmental program are allowed to present combined government-wide and fund financial statements. Thus, the basic financial statements of the Agency are composed of the following:

- Statement of Net Position and Governmental Fund Balance Sheet
- Statement of Activities and Governmental Fund Revenues, Expenditures and Changes in Fund Balance
- Budgetary Comparison Schedule – General Fund
- Budgetary Reconciliation – General Fund
- Notes to the Basic Financial Statements

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - continued

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the basic financial statements and accompanying notes. Actual results could differ from those estimates.

Appropriations

Appropriations represent the authorizations granted by the State Legislature that permit a state agency, within established fiscal and budgetary controls, to incur obligations and to make expenditures. The allotted appropriations lapse if not expended by or encumbered at the end of the fiscal year, with the exception of the State appropriations made to the Audit Revolving Fund, which do not lapse.

Reimbursement Receivables

The Agency pays for the audit fees incurred by departments, offices, agencies and political subdivisions of the State of Hawaii and are reimbursed by them based on a predetermined percentage of the audit fee. All receivables are reported net of estimated uncollectible amounts.

Capital Assets

The accounting treatment over capital assets depends on whether the assets are used in the governmental fund and whether they are reported in the government-wide or fund financial statements.

Government-wide Financial Statements

The Agency records the acquisition of capital assets, costing $5,000 or more, which only includes furniture and equipment, net of accumulated depreciation. Depreciation of furniture and equipment is computed using the straight-line method over 7 years.

Maintenance and repairs are charged to operations when incurred. Betterments and major improvements which significantly increase values, change capacities, or extend useful lives are capitalized. Upon sale or retirement of capital assets, the cost and the related accumulated depreciation, as applicable, are removed from the respective accounts, and any resulting gain or loss is recognized in the statement of activities.

Fund Financial Statements

Capital assets used in governmental fund operations are accounted for as capital expenditures of the governmental fund upon acquisition.

Compensated Absences

Employees are permitted to accumulate earned but unused vacation and sick leave benefits. There is no liability for unpaid accumulated sick leave since sick leave is not convertible to pay upon termination of employment. All vacation pay is accrued when incurred and is reported in the statement of net position.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - continued

Fund Balance

In the governmental fund financial statements, fund balances are classified using a hierarchy based on the extent to which the Agency is bound to follow constraints on the specific purposes for which amounts in the funds may be spent.

Fund balances are classified as follows:

Nonspendable - Nonspendable fund balance includes amounts that cannot be spent because they are either not in spendable form or they are legally or contractually required to be maintained intact.

Restricted - Restricted fund balances are restricted to specific purposes which are usually imposed by external parties such as grantors, contributors, or laws or regulations of other governments.

Committed - Committed fund balances are amounts that can only be used for specific purposes pursuant to formal action of the State Legislature.

Assigned - Assigned fund balance includes amounts that are constrained by the State's intent to be used for specific purposes, but are neither restricted nor committed. The State Legislature authorizes the amounts to specific purposes through the budgetary process. Assigned amounts within the general fund include non-liquidated encumbrances at year end that are carried forward to the next fiscal year.

Unassigned - Unassigned fund balance is the residual classification for the general fund. This classification represents fund balance that has not been assigned to other funds, and that has not been restricted or assigned to specific purposes within the general fund.

The Agency has only assigned and unassigned fund balances.

Risk Management

The Agency is exposed to various risks for losses related to torts; theft of, damage to, or destruction of assets; errors or omissions; natural disasters; and injuries to employees. A liability for a claim for a risk of loss is established if information indicates that it is probable that a liability has been incurred at the date of the basic financial statements and the amount of the loss is reasonably estimable.

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 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 does have the duty of due care that would be required of an ordinary prudent investor. Accordingly, the assets and liabilities of the State's deferred compensation plan are not reported in the State's or Agency's basic financial statements.

NOTE 3 - EXPLANATION OF DIFFERENCES BETWEEN THE GOVERNMENTAL FUND BALANCE SHEET AND STATEMENT OF NET POSITION

"Total fund balance" of the Agency's general fund of $7,369,161 differs from the "net position" of governmental activities of $7,116,035 reported in the statement of net position. This difference primarily results from the long-term economic focus of the statement of net position and the current financial resources focus of the governmental fund balance sheet.

Capital-Related Items

When furniture and equipment that are to be used in governmental activities are purchased, the costs of those activities are reported as expenditures in governmental funds. However, the statement of net position includes those capital assets among the assets of the Agency as a whole.

Long-Term Liabilities

Long-term liabilities applicable to the Agency's governmental activities are not due and payable in the current period and accordingly are not reported as fund liabilities. All liabilities (both current and long-term) are reported in the statement of net position. The balance of compensated absences payable at June 30, 2015, was $322,156.

NOTE 4 - EXPLANATION OF DIFFERENCES BETWEEN THE GOVERNMENTAL FUND OPERATING STATEMENT AND THE STATEMENT OF ACTIVITIES

The "net change in fund balance" for the governmental fund of $167,016 differs from the "change in net position" for governmental activities of $179,970 reported in the statement of activities. The differences arise primarily from the long-term economic focus of the statement of activities and the current financial resources focus of the governmental funds.

Capital-Related Items

When capital assets that are to be used in governmental activities are purchased, the resources expended for those assets are reported as expenditures in the governmental fund. However, in the statement of activities, the costs of those assets are allocated over their estimated useful lives and reported as depreciation expense. As a result, fund balance decreases by the amount of financial resources expended, whereas, net position decreased by the amount of depreciation expense charged for the fiscal year. As of June 30, 2015, the Agency had $69,030 invested in capital assets. There was a net increase of $683 from the end of the prior fiscal year in capital assets.

Long-Term Liability Transactions

Some expenses 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 fund. For the Agency, this difference is due to a net adjustment resulting from a net change in compensated absences of $2,585.

NOTE 5 - BUDGETING AND BUDGETARY CONTROL

Revenue estimates are provided to the State Legislature at the time of budget consideration and are revised and updated periodically during the fiscal year. Amounts reflected as budgeted revenues and budgeted expenditures in the Budgetary Comparison Schedule General Fund are derived primarily from acts of the State Legislature and from other authorizations contained in other specific appropriation acts in various Session Laws of Hawaii.

To the extent not expended or encumbered, general fund appropriations generally lapse at the end of the fiscal year for which the appropriations were made. The State Legislature specifies the lapse date and any other particular conditions relating to terminating the authorization for other appropriations. The Audit Revolving Fund is allowed to carry over unused funds to the subsequent fiscal year.

For purposes of budgeting, the Agency's budgetary fund structure and accounting principles differ from those utilized to present the general fund financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP). The Agency's annual budget is prepared on the modified accrual basis of accounting with several differences, principally related to the encumbrance of purchase orders and contract obligations. These differences represent departures from GAAP. The differences between the budgetary amounts and the amounts presented in accordance with GAAP for the fiscal year ended June 30, 2015, are further explained in the Budgetary Reconciliation - General Fund.

NOTE 6 - CASH AND CASH EQUIVALENTS

Substantially all of the Agency's cash is held in the State Treasury. The State Director of Finance is responsible for safekeeping of all monies paid into the State Treasury. The State Director of Finance pools and invests any monies, which in the State Director of Finance's judgment, are in excess of the amounts necessary for meeting specific requirements of the State. The Hawaii Revised Statutes authorize the State Director of Finance to invest in obligations of, or guaranteed by, the U.S. Government, obligations of the State, federally-insured savings and checking accounts, time certificates of deposit, and repurchase agreements with federally-insured financial institutions.

Information relating to interest rate risk, credit risk, custodial credit risk, and concentration of credit risk is available on a statewide basis and not for individual departments or agencies. Cash and deposits with financial institutions are collateralized in accordance with State statutes.

Interest Rate Risk

As a means of limiting its exposure to fair value losses arising from rising interest rates, the State's investment policy generally limits maturities on investments to not more than five years from the date of investment.

Credit Risk

The State's investment policy limits investments in state and U.S. Treasury securities, time certificates of deposit, U.S. government or agency obligations, repurchase agreements, commercial paper, bankers' acceptances, and money market funds and student loan resource securities maintaining a Triple-A rating.

NOTE 6 - CASH AND CASH EQUIVALENTS - continued

Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the State will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The State's investments are held at broker/dealer firms which are protected by the Securities Investor Protection Corporation (SIPC) up to a maximum amount. In addition, excess-SIPC coverage is provided by the firms' insurance policies. The State also requires the institutions to set aside in safekeeping, certain types of securities to collateralize repurchase agreements. The State monitors the market value of these securities and obtains additional collateral when appropriate.

Concentration of Credit Risk

The State's policy provides guidelines for portfolio diversification by placing limits on the amount the State may invest in any one issuer, types of investment instruments, and position limits per issue of an investment instrument.

Cash in Bank

The Agency also maintains cash in banks which are held separately from cash in the State Treasury. As of June 30, 2015, the carrying amount of total bank balance was approximately $2,000, which is insured by the Federal Deposit Insurance Corporation.

NOTE 7 - CAPITAL ASSETS

The changes in capital assets were as follows:

	Balance July 1, 2014	Increases	Decreases	Balance June 30, 2015
Governmental activities				
Equipment and furniture, at cost	$ 150,654	$ 16,541	$ (18,768)	$ 148,427
Less accumulated depreciation	82,307	15,858	(18,768)	79,397
Governmental activities capital assets, net	$ 68,347	$ 683	$ -	$ 69,030

NOTE 8 - LONG-TERM LIABILITIES

The only long-term liability for governmental activities is for compensated absences. Long-term liability activity during the fiscal year ended June 30, 2015, was as follows:

Balance at June 30, 2014	$ 334,427
Additions	125,811
Reductions	(138,082)
Balance at June 30, 2015	$ 322,156
Due within one year	$ 106,916

The compensated absences liability has been paid primarily by the general fund in the past.

NOTE 9 - NON-IMPOSED EMPLOYEE FRINGE BENEFITS

Payroll fringe benefit costs of the Agency's employees funded by state appropriations (general fund) are assumed by the State and are not charged to the Agency's operating funds. These costs, totaling approximately $874,000 for the fiscal year ended June 30, 2015, have been reported as revenues and expenditures of the Agency's general fund.

NOTE 10 - RETIREMENT BENEFITS

Employees' Retirement System

Plan Description

All eligible employees of the Agency are provided pensions through a cost-sharing multiple-employer defined benefit pension plan administered by the Employees' Retirement System of the State of Hawaii (ERS). Benefit terms, eligibility, and contribution requirements are established by HRS Chapter 88 and can be amended through legislation. The ERS issues a publicly available financial report that can be obtained at ERS' website: http://www.ers.ehawaii.gov.

Benefits Provided

The ERS provides retirement, disability and death benefits that are covered by the provisions of the noncontributory, contributory and hybrid retirement plans. The three plans provide a monthly retirement allowance equal to the benefit multiplier (generally 1.25% or 2%) multiplied by the average final compensation multiplied by years of credited service. The benefit multiplier decreased by 0.25% for new hybrid and contributory class members hired after June 30, 2012. Average final compensation is an average of the highest salaries during any three years of credited service, excluding any salary paid in lieu of vacation for employees hired January 1, 1971 or later and the average of the highest salaries during any five years of credited service including any salary paid in lieu of vacation for employees hired prior to January 1, 1971.

NOTE 10 - RETIREMENT BENEFITS – continued

For members hired before July 1, 2012, the original retirement allowance is increased by 2.5% each July 1 following the calendar year of retirement. This cumulative benefit is not compounded and increases each year by 2.5% of the original retirement allowance without a ceiling (2.5% of the original retirement allowance the first year, 5% the second year, 7.5% the third year, etc.). For members hired after June 30, 2012, the post-retirement annuity increase was decreased to 1.5% per year.

Retirement benefits for certain groups, such as police officers, firefighters, some investigators, sewer workers, judges, and elected officials, vary from general employees.

Noncontributory Class

- Retirement Benefits - General employees' retirement benefits are determined as 1.25% of average final compensation multiplied by the years of credited service. Employees with ten years of credited service are eligible to retire at age 62. Employees with 30 years of credited service are eligible to retire at age 55.

- Disability Benefits - Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 35% of their average final compensation. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined in the same manner as retirement benefits but are payable immediately, without an actuarial reduction, and at a minimum of 12.5% of average final compensation.

- Death Benefits - For service-connected deaths, the surviving spouse/reciprocal beneficiary receives a monthly benefit of 30% of the average final compensation until remarriage or re-entry into a new reciprocal beneficiary relationship. Additional benefits are payable to surviving dependent children up to age 18. If there is no spouse/reciprocal beneficiary or dependent children, no benefit is payable.

  Ten years of credited service is required for ordinary death benefits. For ordinary death benefits, the surviving spouse/reciprocal beneficiary (until remarriage/reentry into a new reciprocal beneficiary relationship) and dependent children (up to age 18) receive a benefit equal to a percentage of the member's accrued maximum allowance unreduced for age or, if the member was eligible for retirement at the time of death, the surviving spouse/reciprocal beneficiary receives 100% joint and survivor lifetime pension.

Contributory Class for Employees Hired Prior to July 1, 2012

- Retirement Benefits - General employees' retirement benefits are determined as 2% of average final compensation multiplied by the years of credited service. General employees with five years of credited service are eligible to retire at age 55.

  Police officers and firefighters' retirement benefits are determined as 2.5% of average final compensation for each year of service up to a maximum of 80%. Police officers and firefighters with five years of credited service are eligible to retire at age 55.

NOTE 10 - RETIREMENT BENEFITS – continued

- Disability Benefits - Members are eligible for service-related disability benefits regardless of length of service and receive a one-time payment of the member's contributions and accrued interest plus a lifetime pension of 50% of their average final compensation. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined as 1.75% of average final compensation multiplied by the years of credited service but are payable immediately, without an actuarial reduction, and at a minimum of 30% of average final compensation.

- Death Benefits - For service-connected deaths, the designated beneficiary receives a lump sum payment of the member's contributions and accrued interest plus a monthly benefit of 50% of the average final compensation to the surviving spouse/reciprocal beneficiary until remarriage or re-entry into a new reciprocal beneficiary relationship. If there is no surviving spouse/reciprocal beneficiary, surviving children (up to age 18) or dependent parents are eligible for the monthly benefit. If there is no spouse/reciprocal beneficiary or dependent children/parents, the ordinary death benefit is payable to the designated beneficiary.

  Ordinary death benefits are available to employees who were active at time of death with at least one year of service. Ordinary death benefits consist of a lump-sum payment of the member's contributions and accrued interest plus a percentage of the salary earned in the 12 months preceding death, or 50% Joint and Survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% Joint and Survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary.

Contributory Class for Employees Hired After June 30, 2012

- Retirement Benefits - General employees' retirement benefits are determined as 1.75% of average final compensation multiplied by the years of credited service. General employees with ten years of credited service are eligible to retire at age 60.

  Judges and elected officers' retirement benefits are determined as 3.0% of average final compensation multiplied by the years of credited service up to a maximum of 75%. Judges and elected officers with ten years of credited service are eligible to retire at age 60.

  Police officers and firefighters' retirement benefits are determined as 2.25% of average final compensation for each year of service up to a maximum of 80%. Police officers and firefighters with ten years of credited service are eligible to retire at age 60.

- Disability and Death Benefits - Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 50% of their average final compensation plus refund of contributions and accrued interest. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are 3% of average final compensation for each year of service for judges and elected officers and 1.75% of average final compensation for each year of services for police officers and firefighters and are payable immediately, without an actuarial reduction, at a minimum of 30% of average final compensation.

  Death benefits for contributory class members hired after June 30, 2012 are generally the same as those for contributory class members hired June 30, 2012 and prior.

NOTE 10 - RETIREMENT BENEFITS – continued

Hybrid Class for Employees Hired Prior to July 1, 2012

- Retirement Benefits - General employees' retirement benefits are determined as 2% of average final compensation multiplied by the years of credited service. General employees with five years of credited service are eligible to retire at age 62. General employees with 30 years of credited service are eligible to retire at age 55.

- Disability Benefits - Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 35% of their average final compensation plus refund of their contributions and accrued interest. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined in the same manner as retirement benefits but are payable immediately, without an actuarial reduction, and at a minimum of 25% of average final compensation.

- Death Benefits - For service-connected deaths, the designated surviving spouse/reciprocal beneficiary receives a lump sum payment of the member's contributions and accrued interest plus a monthly benefit of 50% of the average final compensation to the surviving spouse/reciprocal until remarriage or re-entry into a new reciprocal beneficiary relationship. If there is no surviving spouse/reciprocal beneficiary, surviving children (up to age 18) or dependent, parents are eligible for the monthly benefit. If there is no spouse/reciprocal beneficiary or dependent children/parents, the ordinary death benefit is payable to the designated beneficiary.

  Ordinary death benefits are available to employees who were active at time of death with at least five years of service. Ordinary death benefits consist of a lump sum payment of the member's contributions and accrued interest plus a percentage multiplied by 150%, or 50% Joint and Survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% Joint and Survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary.

Hybrid Class for Employees Hired After June 30, 2012

- Retirement Benefits - General employees' retirement benefits are determined as 1.75% of average final compensation multiplied by the years of credited service. General employees with ten years of credited service are eligible to retire at age 65. Employees with 30 years of credited service are eligible to retire at age 60. Sewer workers, water safety officers, and emergency medical technicians may retire with 25 years of credited service at age 55.

- Disability and Death Benefits - Provisions for disability and death benefits generally remain the same except for ordinary death benefits. Ordinary death benefits are available to employees who were active at time of death with at least ten years of service. Ordinary death benefits consist of a lump sum payment of the member's contributions and accrued interest plus a percentage multiplied by 120%, or 50% Joint and Survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% Joint and Survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary or if less than ten years of service, return of the member's contributions and accrued interest.

NOTE 10 - RETIREMENT BENEFITS – continued

Contributions

Contributions are established by HRS Chapter 88 and may be amended through legislation. The employer rate is set by statute based on the recommendations of the ERS actuary resulting from an experience study conducted every five years. Effective July 1, 2005, employer contribution rates are a fixed percentage of compensation, including the normal cost plus amounts required to pay for the unfunded actuarial accrued liabilities. Pension benefit contributions paid by the State on behalf of the Agency for the fiscal years ended June 30, 2015, 2014, and 2013, were approximately $344,000, $355,000, and $286,000, respectively, at the rate of 16.50%, 16.50%, and 15.50% of compensation, respectively.

The employer is required to make all contributions for noncontributory members. For contributory class employees hired prior to July 1, 2012, general employees are required to contribute 7.8% of their salary and police officers and firefighters are required to contribute 12.2% of their salary. For contributory class employees hired after June 30, 2012, judges and elected officials are required to contribute 9.8% of their salary and police officers and firefighters are required to contribute 14.2% of their salary. Hybrid members hired prior to July 1, 2012 are required to contribute 6.0% of their salary. Hybrid members hired after June 30, 2012 are required to contribute 8.0% of their salary.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

Measurement of the net pension liability, pension expense, deferred inflows related to pension, and deferred outflows related to pension are made for the State as a whole and are not separately computed for the individual state departments and agencies. The State has only computed the proportion share of these items for proprietary funds and component units that are reported separately in the State's Comprehensive Annual Financial Report (CAFR). Therefore, the proportionate share of the pension liability, pension expense, deferred inflows related to pension, and deferred outflows related to pension for the Agency were not available and are not included in the financial statements. The State's CAFR includes the required footnote disclosures and required supplementary information on the State's pension plan.

Post-Retirement Health Care and Life Insurance Benefits

Plan Descriptions

The State provides certain health care and life insurance benefits to all qualified employees. Pursuant to Act 88, SLH of 2001, the State contributes to the Hawaii Employer-Union Health Benefits Trust Fund (EUTF), an agent multiple-employer defined benefit plan that replaced the Hawaii Public Employees Health Fund effective July 1, 2003. The EUTF was established to provide a single delivery system of health benefits for state and county workers, retirees and their dependents. The EUTF issues an annual financial report that is available to the public. That report may be obtained by writing to the EUTF at P.O. Box 2121, Honolulu, Hawaii 96805-2121.

For employees hired before July 1, 1996, the State pays the entire base monthly contribution for employees retiring with 10 years or more of credited service, and 50% of the base monthly contribution for employees retiring with fewer than 10 years of credited service. Retirees in this category can elect a family plan to cover dependents.

NOTE 10 - RETIREMENT BENEFITS – continued

For employees hired after June 30, 1996 but before July 1, 2001, and who retire with less than 10 years of service, the State makes no contributions. For those retiring with at least 10 years but fewer than 15 years of service, the State pays 50% of the base monthly contribution. For those retiring with at least 15 years but fewer than 25 years of service, the State pays 75% of the base monthly contribution. For those employees retiring with at least 25 years of service, the State pays 100% of the base monthly contribution. Retirees in this category can elect a family plan to cover dependents.

For employees hired on or after July 1, 2001, and who retire with less than 10 years of service, the State makes no contributions. For those retiring with at least 10 years but fewer than 15 years of service, the State pays 50% of the base monthly contribution. For those retiring with at least 15 years but fewer than 25 years of service, the State pays 75% of the base monthly contribution. For those employees retiring with at least 25 years of service, the State pays 100% of the base monthly contribution. Only single plan coverage is provided for retirees in this category. Retirees can elect family coverage but must pay the difference.

Cost

The State's base contribution levels to the EUTF are established by statutes and the retiree is responsible to pay the difference if the base contribution is less than the cost of the monthly premium. Post-retirement health care and life insurance benefits paid by the State on behalf of the Agency for the fiscal years ended June 30, 2015, 2014 and 2013 were approximately $212,000, $223,000, and $191,000, respectively.

The State's annual OPEB cost for each plan was calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

Measurement of the actuarial valuation and the ARC are made for the State as a whole and are not separately computed for the individual state departments and agencies. The State has only computed the allocation of the other postemployment benefit (OPEB) costs to proprietary funds and component units that are reported separately in the State's CAFR. Therefore, the OPEB costs for the Agency were not available and are not included in the financial statements. The State's CAFR includes the required footnote disclosures and required supplementary information on the State's OPEB plans.

NOTE 11 - RISK MANAGEMENT

The Agency is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; and workers' compensation. The State records a liability for risk financing and insurance-related losses 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. The excess layers insured with commercial insurance companies are consistent with the prior fiscal year. Settled claims have not exceeded the coverage provided by commercial insurance companies in any of the past three fiscal years. A summary of the State's underwriting risks is as follows:

NOTE 11 - RISK MANAGEMENT - continued

Property Insurance

The State has an insurance policy with a variety of insurers in a variety of layers for property coverage. The deductible for coverage is 3% of loss subject to a $1 million per occurrence minimum. This policy includes windstorm, earthquake, flood damage, terrorism and boiler and machinery coverage. The limit of loss per occurrence is $200 million, except for terrorism, which is $50 million per occurrence and a $10,000 deductible.

Crime Insurance

The State also has a crime insurance policy for various types of coverages with a limit of loss of $10 million per occurrence with a $500,000 deductible per occurrence, except for claims expense coverage, which has a $100,000 per occurrence and a $1,000 deductible. Losses under the deductible amount are paid by the Risk Management Office of the Department of Accounting and General Services and losses not covered by insurance are paid from legislative appropriations of the State's General Fund.

General Liability (Including Torts)

Liability claims under $10,000 and automobile claims under $15,000 are handled by the Risk Management Office of the Department of Accounting and General Services. All other claims are handled by the Department of the Attorney General. The State has personal injury and property damage liability, including automobile and public errors and omissions, insurance policy in force with a $4 million self-insured retention per occurrence. The annual aggregate limit per occurrence is $15 million, and for crime loss, $10 million with no aggregate limit.

Losses under the deductible amount or over the aggregate limit are paid from legislative appropriations of the State's General Fund.

Self-Insured Risks

The State generally self-insures its automobile no-fault and workers' compensation losses. Automobile losses below $15,000 are administered by the Risk Management Office of the Department of Accounting and General Services. The State administers its workers' compensation losses.

Reserve for Losses

At June 30, 2015, the State recorded an estimated loss for workers' compensation and general liability claims as long-term debt 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 Agency's portion of the State's workers' compensation expense for the fiscal year ended June 30, 2015, was approximately $23,000.

NOTE 12 - COMMITMENTS AND CONTINGENCIES

Encumbrances
Encumbrances totaled approximately $4,999,000 as of June 30, 2015.

Accumulated Sick Leave
Employees earn sick leave credits at the rate of one and three-quarters working days for each month of service without limit. Sick leave can be taken only in the event of illness and is not convertible to pay upon termination of employment. However, an employee who retires or leaves government service in good standing with sixty days or more of unused sick leave is entitled to additional service credit in the ERS. Accumulated sick leave as of June 30, 2015, amounted to approximately $955,000.

Litigation
From time to time, the Agency is named as a defendant in various legal proceedings. It has been the State's historical practice that certain types of judgments and settlements against an agency of the State are paid from the State's General Fund through an appropriation bill which is submitted annually by the Department of the Attorney General to the State Legislature.

Lease Commitments
The Agency leases office equipment under noncancelable operating leases expiring in March 2017. Total equipment rental expenditures for the fiscal year ended June 30, 2015 amounted to approximately $17,000. Future lease commitments for the operating leases are approximated as follows:

Fiscal Year Ending June 30,	
2016	$ 12,600
2017	9,400
	$ 22,000

CHOO, OSADA & LEE, CPAs, INC.
CERTIFIED PUBLIC ACCOUNTANTS

1136 12TH AVENUE
SUITE 240
HONOLULU, HAWAII 96816

TELEPHONE (808) 734-1921

INDEPENDENT AUDITOR'S REPORT 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*

To the State Auditor
Office of the Auditor
State of Hawaii

We have audited, 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, the financial statements of the governmental activities and general fund of the Office of the Auditor of the State of Hawaii (Agency), as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the Agency's basic financial statements, and have issued our report thereon dated March 22, 2016.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Agency's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Agency's internal control. Accordingly, we do not express an opinion on the effectiveness of the Agency's internal control.

A *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, including applicable provisions of the Hawaii Procurement Code (Chapter 103D of the Hawaii Revised Statutes), 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Choo, Osada & Lee, CPAs, Inc.

Honolulu, Hawaii
March 22, 2016