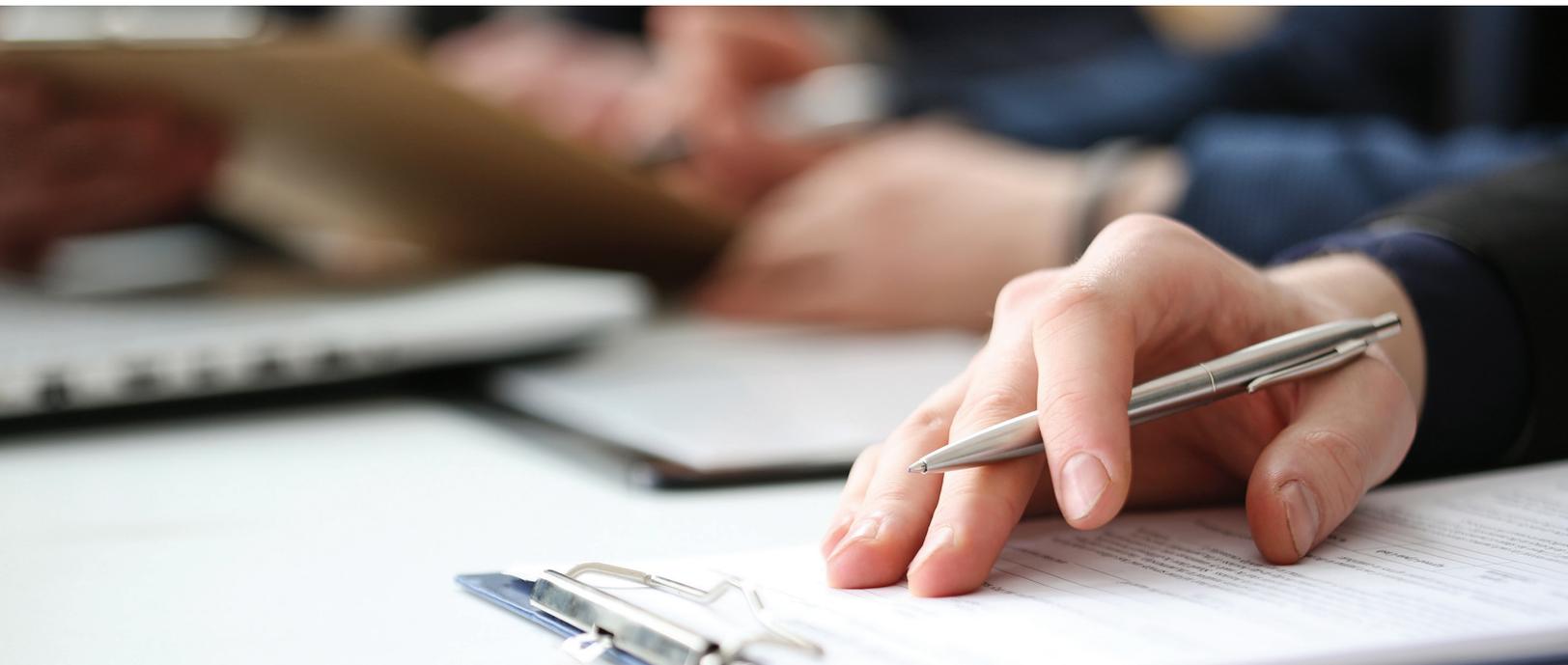


Review of Special Funds, Revolving Funds, Trust Funds, and Trust Accounts of the Department of Taxation

A Report to the Governor
and the Legislature of
the State of Hawai'i

Report No. 17-10
November 2017



OFFICE OF THE AUDITOR
STATE OF HAWAII



OFFICE OF THE AUDITOR STATE OF HAWAII

Constitutional Mandate

Pursuant to Article VII, Section 10 of the Hawai'i State Constitution, the Office of the Auditor shall conduct post-audits of the transactions, accounts, programs and performance of all departments, offices and agencies of the State and its political subdivisions.

The Auditor's position was established to help eliminate waste and inefficiency in government, provide the Legislature with a check against the powers of the executive branch, and ensure that public funds are expended according to legislative intent.

Hawai'i Revised Statutes, Chapter 23, gives the Auditor broad powers to examine all books, records, files, papers and documents, and financial affairs of every agency. The Auditor also has the authority to summon people to produce records and answer questions under oath.

Our Mission

To improve government through independent and objective analyses.

We provide independent, objective, and meaningful answers to questions about government performance. Our aim is to hold agencies accountable for their policy implementation, program management and expenditure of public funds.

Our Work

We conduct performance audits (also called management or operations audits), which examine the efficiency and effectiveness of government programs or agencies, as well as financial audits, which attest to the fairness of financial statements of the State and its agencies.

Additionally, we perform procurement audits, sunrise analyses and sunset evaluations of proposed regulatory programs, analyses of proposals to mandate health insurance benefits, analyses of proposed special and revolving funds, analyses of existing special, revolving and trust funds, and special studies requested by the Legislature.

We report our findings and make recommendations to the Governor and the Legislature to help them make informed decisions.

For more information on the Office of the Auditor, visit our website:
<http://auditor.hawaii.gov>

Foreword

This is a report of our review of the special funds, trust funds, and trust accounts of the Department of Taxation.

Section 23-12, Hawai‘i Revised Statutes (HRS), requires the Auditor to review all existing special, revolving, and trust funds once every five years. Although not mandated by statute, we included trust accounts as part of our review. This is our fifth review of the revolving funds, trust funds, and trust accounts of the Department of Taxation. It is our first review of its special funds since Section 23-12, HRS, was amended by Act 130, Session Laws of Hawai‘i 2013, to include reviews of special funds. The Department of Taxation did not have any revolving funds during our review period.

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

Leslie H. Kondo
State Auditor

Table of Contents

Auditor’s Summary	1
Chapter 1 Introduction	3
Description of Special Funds, Revolving Funds, Trust Funds, and Trust Accounts.....	4
Criteria for Reviewing Special Funds, Revolving Funds, Trust Funds, and Trust Accounts	5
Objectives of the Review	6
Scope and Methodology	6
Chapter 2 Department of Taxation	9
Chapter 3 The Department of Taxation Did Not Report Non-General Funds As Required by Law	21
Office of the Auditor’s Comments on the Affected Agency Response	25
Attachment 1 Department of Taxation Response	27

List of Exhibits

Exhibit 2.1	Cash Balances for DoTAX Non-General Funds, FY2013–FY2017 (in millions).....	9
Exhibit 2.2	DoTAX Fund Totals by Type, FY2017	10
Exhibit 2.3	DoTAX Funds Not Meeting Criteria.....	11
Exhibit 3.1	DoTAX Funds and Trust Accounts Not Reported to the Legislature	22
Exhibit 3.2	DoTAX Administratively Created Funds and Trust Accounts Not Reported to the Legislature	23



Auditor's Summary

Review of Special Funds, Revolving Funds, Trust Funds, and Trust Accounts of the Department of Taxation

Report No. 17-10

Two special funds and three trust accounts did not meet criteria

OUR REVIEW OF FOUR SPECIAL FUNDS, two trust funds, and seven trust accounts of the Department of Taxation (DoTAX) found two special funds and three trust accounts did not meet criteria and should be closed or reclassified.

Section 23-12, Hawai'i Revised Statutes (HRS), requires the Auditor to review all existing special, revolving, and trust funds every five years. Reviews are scheduled so that each department's funds are reviewed once every five years. Although not mandated by statute, we included trust accounts as part of our review. DoTAX did not have any revolving funds during our review period. This is our fifth review of DoTAX's revolving funds, trust funds, and trust accounts. It is our first review of DoTAX's special funds.

We used criteria developed by the Legislature and by our office based on public finance and accounting literature. For each fund, we present a five-year financial summary, the purpose of the fund, and conclusions about its use. We did not audit the financial data which is provided for informational purposes. We do not present conclusions about the effectiveness of programs or their management, or whether the programs should be continued.

Reporting shortfall

WE ALSO NOTED that DoTAX did not file statutorily required reports for non-general funds and for administratively created funds. Accurate and complete reporting will greatly improve the Legislature's oversight and control of these funds and provide increased budgetary flexibility.

Agency response

DOTAX GENERALLY AGREED WITH OUR FINDINGS and will take appropriate action to close one special fund and three trust accounts that did not meet criteria and inform the Department of Budget and Finance of our recommendation to reclassify one special fund to a trust account. DoTAX will also comply with reporting requirements.



FUND TYPES

SPECIAL FUNDS

are used to account for revenues earmarked for particular purposes and from which expenditures are made for those purposes.

REVOLVING FUNDS

such as loan funds, are often established with an appropriation of seed money from the general fund and must demonstrate the capacity to be self-sustaining.

TRUST FUNDS

such as a pension fund, invoke the State's fiduciary responsibility to care for and use the assets held to benefit those with a vested interest in the assets.

TRUST ACCOUNTS

are typically separate holding or clearing accounts and are often used as accounting devices for crediting or charging state agencies or projects for payroll and other costs.



Chapter 1

Introduction

This review encompasses the special funds, trust funds, and trust accounts administered by the Department of Taxation (DoTAX). Section 23-12, Hawai'i Revised Statutes (HRS), requires the Auditor to review each state department's special, revolving, and trust funds every five years. Specifically, the Auditor's review must include:

1. An evaluation of the original intent and purpose of each fund, both as expressed by the Legislature and as understood by the expending agency;
2. The degree to which each fund achieves its stated and claimed purposes;
3. An evaluation of the fund's performance standards as established by the agency; and
4. A summary statement reflecting total fund transactions in the preceding five fiscal years, including the fund balance at the beginning of each fiscal year, total deposits and withdrawals, amount of interest earned, total expenditures made from the fund, and the ending balance for each fiscal year.

Although not mandated by Section 23-12, HRS, we have included trust accounts as part of our review. Trust accounts, like special, revolving, and trust funds, are subject to minimal legislative scrutiny.

This is our fifth review of DoTAX's trust funds and trust accounts, and our first review of special funds held by DoTAX.¹ We last examined DoTAX's trust funds and trust accounts in 2012.

In this report, we reviewed 13 funds administered by DoTAX — specifically, four special funds, two trust funds, and seven trust accounts.

¹ Prior to 2013, Section 23-12, HRS, did not require reviews of departments' special funds.

Description of Special Funds, Revolving Funds, Trust Funds, and Trust Accounts

Special funds

Section 37-62, HRS, defines a special fund as one that is “dedicated or set aside by law for a specified object or purpose, but excluding revolving funds and trust funds.” According to the State’s *Accounting Manual*, special funds are funds used to account for revenues earmarked for particular purposes and from which expenditures are made for those purposes. Examples of special funds include the Captive Insurance Administrative Fund, which is funded by fees paid by insurers that support the State’s Captive Insurance Program, and the Wireless Enhanced 911 Fund. The Wireless Enhanced 911 Fund receives surcharges from wireless phone users for the upgrade of the 911 emergency system.

Revolving funds

Section 37-62, HRS, defines a revolving fund as one “from which is paid the cost of goods and services rendered or furnished to or by a state agency and which is replenished through charges made for the goods or services or through transfers from other accounts or funds.” Activities commonly financed through revolving funds include loan programs, which are initially established by general fund seed moneys and are then replenished through the repayment of loans. An example of a revolving fund is the State Motor Pool Revolving Fund, which is used to purchase and maintain the State’s fleet of motor vehicles and is replenished by charges to state agencies for the use of the vehicles.

Trust funds

Section 37-62, HRS, defines a trust fund as one in which “designated persons or classes of persons have a vested beneficial interest or equitable ownership, or which was created or established by a gift, grant, contribution, devise or bequest that limits the use of the fund to designated objects or purposes.” Trust funds invoke a fiduciary responsibility of state government to care for and use only for those designated to benefit from the funds. A pension fund is an example of a trust fund. Contributions and payments are to be held for the beneficiaries of the pension fund. Another example is tenants’ security deposits, which are held in trust for the future benefit of tenants and landlords. Until forfeited or returned, deposits are the property of the tenants and should be accounted for accordingly.

Trust accounts

The Department of Accounting and General Services (DAGS) defines a trust account as a separate holding or clearing account for State agencies. Trust accounts also serve as accounting devices to credit or charge agencies or projects for payroll or other costs.

Criteria for Reviewing Special Funds, Revolving Funds, Trust Funds, and Trust Accounts

Special and revolving fund criteria

In 2002, the Legislature set the requirements for establishing and continuing special and revolving funds. Sections 37-52.3 and 37-52.4, HRS, state that special and revolving funds may only be established by statute. The criteria used to review special and revolving funds are the extent to which each fund:

- Serves a need, as demonstrated by: (1) the purpose of the program to be supported by the fund; (2) the scope of the program, including financial information on fees to be charged, sources of projected revenue, and costs; and (3) an explanation of why the program cannot be implemented successfully under the general fund appropriation process;
- Reflects a clear nexus between the benefits sought and charges made upon the program users or beneficiaries, or a clear link between the program and the sources of revenue — as opposed to serving primarily as a means to provide the program or users with an automatic means of support, removed from the normal budget and appropriation process;
- Provides an appropriate means of financing for the program or activity that is used only when essential to the successful operation of the program or activity; and
- Demonstrates the capacity to be financially self-sustaining.

Trust fund and trust account criteria

Unlike the requirements for special and revolving funds, the law is silent on whether a trust fund or trust account must be established by statute. The criteria used to review trust funds and trust accounts are the extent to which each fund and account:

- Continues to serve the purpose and intent for which it was originally created; and
- Meets the definition of a trust fund or trust account, respectively.

The first criterion is derived from the objectives of Section 23-12, HRS, which requires the Auditor to evaluate the original intent of each fund and account and the degree to which each fund and account achieves its stated purpose. The second criterion assesses whether a fund is held by the State only for the benefit of those with a vested interest in the assets or an account is held as a separate or clearing account.

Objectives of the Review

1. Identify and review all special funds, revolving funds, trust funds, and trust accounts of DoTAX.
2. For each special fund, revolving fund, trust fund, and trust account, determine whether the fund or account meets the respective criteria.
3. Provide a five-year (FY2013–FY2017) unaudited financial summary for each fund and account reviewed.

Scope and Methodology

We reviewed all special funds, trust funds, and trust accounts directly administered by DoTAX during the five-year period under review (FY2013–FY2017). Funds and accounts included those established by statute as well as by administrative authority. DoTAX did not have any revolving funds during our review period.

To identify funds subject to this review, we used a variety of sources, including our prior reviews, accounting reports from DAGS, non-general fund reports, legislative budget briefing documents, and other records. To gain an understanding of fund operations, we reviewed applicable agency administrative rules and interviewed key fiscal and program personnel, as necessary.

We obtained a summary statement for each fund that reflects total fund transactions in the preceding five fiscal years (July 1, 2012 to June 30, 2017), including beginning fund balances, total revenues,

amount of interest earned, total expenditures, transfers, and ending fund balances for each fiscal year. We requested explanations for discrepancies between ending balances for FY2012 reported in our last review, Report No. 12-10, and opening balances reported for FY2013. We did not audit DoTAX's financial data, which are provided for informational purposes only.

Procedures were performed on each fund using relevant criteria as stated above. We reviewed fund information for consistency with the intent of each fund's use and to ascertain the relationship between charges on users and expenditures. We reviewed and compared fund balances to financial activity and projected program needs and standards. We reviewed information on performance standards established for the funds or accounts and performed other procedures as necessary.

Where appropriate, we relied on our prior reports, including Report Nos. 97-20, *Review of Revolving and Trust Funds of the Department of Human Resources Development, Department of Labor and Industrial Relations, Department of Public Safety, and Department of Taxation*; 02-15, *Report on the Revolving Funds, Trust Funds, and Trust Accounts of the Department of Human Resources Development, Department of Labor and Industrial Relations, Department of Public Safety, and Department of Taxation*; 07-07, *Review of Revolving Funds, Trust Funds, and Trust Accounts of the Departments of Human Resources Development, Labor and Industrial Relations, Public Safety, and Taxation*; 12-10, *Review of Revolving Funds, Trust Funds, and Trust Accounts of the Departments of Human Resources Development, Labor and Industrial Relations, Public Safety, and Taxation*; and 12-04, *Study of the Transfer of Non-general Funds to the General Fund*.

Our review was conducted from July to October 2017. Recommendations were made where applicable.

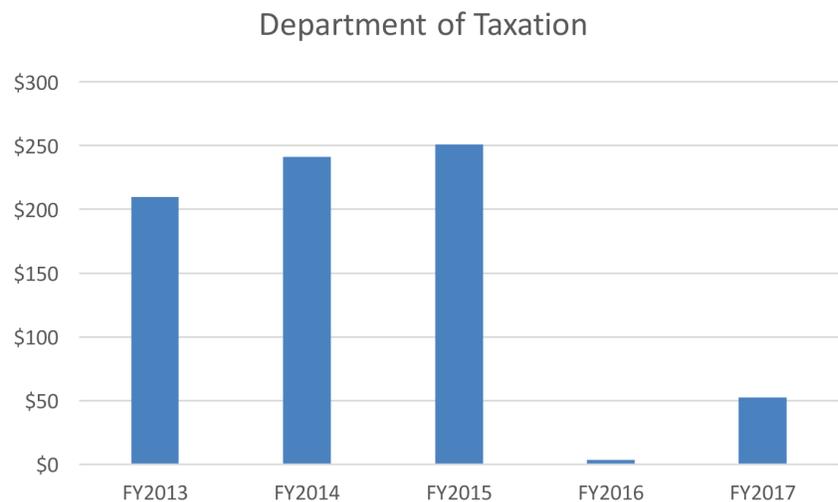
Chapter 2

Department of Taxation

This chapter presents the results of our review of four special funds, two trust funds, and seven trust accounts. Fund fiscal year-end balances amounted to at least \$3 million per year during the period reviewed.

Exhibit 2.1 displays the totals for these fund balances at the end of each fiscal year.

Exhibit 2.1
Cash Balances for DoTAX Non-General Funds, FY2013–FY2017 (in millions)



Source: Office of the Auditor

Substantial amounts were also collected and expended by the funds annually. In FY2017, the special funds, trust funds, and trust accounts collected more than \$8.2 billion and spent or transferred more than \$8.2 billion.

Exhibit 2.2 presents totals for the combined revenue and interest, expenses and transfers, and ending fund balances for the different fund types for FY2017.

Exhibit 2.2
DoTAX Fund Totals by Type, FY2017

Fund Type	Revenue and Interest	Expenses and Transfers	Year-End Cash Balance
Special Funds	\$5,867,000	\$2,667,000	\$7,087,000
Trust Funds and Trust Accounts	8,253,045,000	8,207,600,000	45,179,000
Total	\$8,258,912,000	\$8,210,267,000	\$52,266,000

Source: Office of the Auditor

For each fund, we present a five-year financial summary, the purpose of the fund, and conclusions about its use and whether it meets the criteria for continuance of a special or revolving fund or the definition of a trust fund or account. We do not assess the effectiveness of programs and their management. The funds are presented in alphabetical order.

Exhibit 2.3 presents DoTAX funds that do not meet criteria for continuance and should be repealed, closed, or reclassified.

**Exhibit 2.3
DoTAX Funds Not Meeting Criteria**

Fund Name	Fund Type	FY2017 Ending Balance (rounded)	No longer serves original purpose and/or does not serve a need	No clear nexus between benefits sought and user charges or a clear link between the program and revenue sources	Inappropriate financing mechanism	Not financially self-sustaining	Does not meet special fund, trust fund, or trust account definition
Est/Adm License and Permit Tobacco and Cigarette	Special	\$43,000	✓	✓	✓	✓	✓
IRS Refund Intercept Account	Trust Account	\$1,000	✓				✓
Special Enforcement Section Collections Trust Account	Trust Account	\$500,000	✓				✓
Taxes Payable to Counties – Fuel Accounts	Trust Account	\$1,546,000	✓				✓
Unemployment Tax Clearance Accounts	Special	\$485,000			✓		✓

**Cigarette Tax Stamp
Administrative Special
Fund
(special fund)**

Section 245-41.5, HRS

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$444	\$536	\$547	\$620	\$717
Revenues	256	219	234	225	206
Interest	0	0	0	0	0
Expenditures	(164)	(208)	(161)	(128)	(108)
Transfers (net)	0	0	0	0	0
Ending Balance	\$536	\$547	\$620	\$717	\$815
Encumbrances	\$44	\$39	\$47	\$72	\$87

This fund continues to serve the purpose for which it was created and meets the criteria for a special fund. Created in 2001, the fund is used to

deposit the portion of the cigarette tax stamp fee designated to reimburse the State for providing the cigarette tax stamps. Revenues come from a portion of the stamp fee collected from every cigarette and tobacco wholesaler or dealer who purchases cigarette tax stamps. Expenditures consist of costs to provide the stamps and administer the cigarette tax stamp provisions, including vendor expenses to produce stamps, costs to maintain and distribute stamps, and administrative expenses to maintain the fund.

Est/Adm License and Permit Tobacco and Cigarette (special fund)

Administratively established

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$43	\$43	\$43	\$43	\$43
Revenues	0	0	0	0	0
Interest	0	0	0	0	0
Expenditures	0	0	0	0	0
Transfers (net)	0	0	0	0	0
Ending Balance	\$43	\$43	\$43	\$43	\$43
Encumbrances	\$0	\$0	\$0	\$0	\$0

This fund should be closed and the remaining balance transferred to the general fund. The fund does not serve the purpose for which it was created and has had no financial activity since FY2009.

IRS Refund Intercept Account (trust account)

Administratively established

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$1	\$1	\$1	\$1	\$1
Revenues	0	0	0	0	0
Interest	0	0	0	0	0
Expenditures	0	0	0	0	0
Transfers (net)	0	0	0	0	0
Ending Balance	\$1	\$1	\$1	\$1	\$1
Encumbrances	\$0	\$0	\$0	\$0	\$0

This account does not meet the criteria for a trust account and should be closed. This account was established as a clearing account for delinquent tax collections owed to the Internal Revenue Service (IRS). In accordance with a federal/state agreement, the department intercepts state tax refunds owed to Hawai'i taxpayers to cover delinquent federal taxes owed by those taxpayers. Delinquent taxes owed to the IRS are disbursed from the Undistributed Tax Collections Accounts to this account and subsequently disbursed to the IRS. However, the account has been inactive since FY2000 as IRS fund intercepts are now taken directly from Undistributed Tax Collections Accounts as the requests are processed by DAGS.

***Litigated Claims Fund
(trust fund)***

***Administratively
established***

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$18,789	\$225,573	\$252,019	\$251,794	\$10,307
Revenues	206,784	46,163	911	39,125	48,010
Interest	0	0	0	0	0
Expenditures	0	(19,717)	(1,136)	(280,612)	(9,938)
Transfers (net)	0	0	0	0	0
Ending Balance	\$225,573	\$252,019	\$251,794	\$10,307	\$48,379
Encumbrances	\$0	\$0	\$0	\$0	\$0

This fund continues to serve the purpose for which it was created and meets the criteria for a trust fund. The fund is used as a holding account for amounts in dispute when tax appeal cases are litigated. The disputed amount is disbursed to either the State's general fund or the taxpayer after the case is resolved.

**Sales of Assets for
Delinquent Taxes—
O‘ahu
(trust account)**

**Administratively
established**

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$3	\$3	\$3	\$3	\$3
Revenues	0	0	0	0	0
Interest	0	0	0	0	0
Expenditures	0	0	0	0	0
Transfers (net)	0	0	0	0	0
Ending Balance	\$3	\$3	\$3	\$3	\$3
Encumbrances	\$0	\$0	\$0	\$0	\$0

This account continues to meet the criteria for a trust account. This trust account was established to hold surplus funds from the sale of property seized and foreclosed upon to pay unpaid taxes, penalties, interest, costs, and expenses. Section 231-25(b)(7)(D), HRS, requires that, once payment for unpaid taxes has been made, any surplus received following the sale of the seized property be deposited with the department until returned to the owner. Though the account is inactive, the department reported that the account is needed to meet the statutory requirements regarding collection efforts pertaining to the sale of property to pay taxes, penalties, interest, costs, and expenses.

**Special Enforcement
Section Collections
Trust Account
(trust account)**

**Administratively
established**

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$500	\$500	\$500	\$500	\$500
Revenues	0	0	0	0	0
Interest	0	0	0	0	0
Expenditures	0	0	0	0	0
Transfers (net)	0	0	0	0	0
Ending Balance	\$500	\$500	\$500	\$500	\$500
Encumbrances	\$0	\$0	\$0	\$0	\$0

This account does not meet the criteria for a trust account and should be closed. Act 134, Session Laws of Hawai‘i 2009, established the Special Enforcement Section (SES), which is responsible for carrying

out complex civil-enforcement efforts of Hawaii’s tax laws. Act 134 also allowed for the tax collections by the SES to be deposited into the Tax Administration Special Fund and then expended for the operations of the SES. This account was established to facilitate the distribution of the SES collections. The department reported that it has discontinued use of this account because SES collections are now transferred directly to the Tax Administration Special Fund.

**Tax Administration
Special Fund
(special fund)**

Section 235-20.5, HRS

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$1,172	\$972	\$612	\$1,953	\$2,642
Revenues	24	20	1,663	2,675	5,661
Interest	0	0	0	0	0
Expenditures	(224)	(380)	(322)	(1,986)	(2,559)
Transfers (net)	0	0	0	0	0
Ending Balance	\$972	\$612	\$1,953	\$2,642	\$5,744
Encumbrances	\$41	\$40	\$1	\$0	\$0

This fund continues to serve the purpose for which it was created and meets the criteria for a special fund. Created in 2004, the fund is used to facilitate the operations of the SES and to offset costs incurred by the department. Revenues come from fees collected for the issuance of comfort letters and certificates of tax credit claims, revenues collected by the special enforcement section, and fines assessed for violations of registration requirements under the transient accommodations tax. Moneys from the fund are used to issue comfort letters, letter rulings, written opinions, and certificates of tax credit claims; administer the operations of the department’s special enforcement section; and develop, implement, and provide taxpayer education programs.

**Tax Reserve Fund
(trust fund)****Section 231-23, HRS****Financial Data for FY2013–2017 (in thousands)**

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$0	\$0	\$0	\$46	\$0
Revenues	539,643	635,552	560,950	607,537	653,131
Interest	0	0	0	0	0
Expenditures	(539,643)	(632,669)	(550,137)	(605,261)	(650,134)
Transfers (net)*	0	(2,883)	(10,767)	(2,322)	(2,997)
Ending Balance	\$0	\$0	\$46	\$0	\$0
Encumbrances	\$0	\$0	\$0	\$0	\$0

* Transfers were made to the Undistributed Tax Collections Account after refunds were rejected or cancelled.

This fund continues to serve the purpose for which it was created and meets the criteria for a trust fund. This fund was established in 1939 as a clearing account to enable the department to refund taxes collected. The fund collects amounts from the Undistributed Tax Collections Accounts and disburses them to taxpayers as refunds on overpaid taxes. Taxpayers who are owed tax refunds benefit from the fund and have a vested interest in the fund. Revenues come from overpaid taxes collected from taxpayers, and expenditures consist of tax refunds.

**Taxes-Paid-Under-
Protest Accounts
(trust account)****Administratively
established****Financial Data for FY2013–2017 (in thousands)**

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$6,470	\$6,130	\$6,130	\$6,130	\$20
Revenues	0	0	0	1,515	274
Interest	0	0	0	0	0
Expenditures	(340)	0	0	(7,625)	(273)
Transfers (net)	0	0	0	0	0
Ending Balance	\$6,130	\$6,130	\$6,130	\$20	\$21
Encumbrances	\$0	\$0	\$0	\$0	\$0

These accounts continue to meet the criteria for a trust account. These trust accounts were established to collect amounts related to taxes paid under protest. Moneys are disbursed from the Undistributed Tax

Collections Accounts to the Taxes-Paid-Under-Protest Account. When a tax appeal case is litigated, the amounts in dispute are disbursed to the Litigated Claims Fund.

Taxes Payable to Counties – Fuel Accounts (trust account)

Administratively established

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$1,546	\$1,546	\$1,546	\$1,546	\$1,546
Revenues	0	0	0	0	0
Interest	0	0	0	0	0
Expenditures	0	0	0	0	0
Transfers (net)	0	0	0	0	0
Ending Balance	\$1,546	\$1,546	\$1,546	\$1,546	\$1,546
Encumbrances	\$0	\$0	\$0	\$0	\$0

These accounts do not meet the criteria for trust accounts and should be closed. These accounts were established as clearing accounts for fuel tax collections payable to the counties. Separate accounts were established for the Honolulu, Maui, and Kaua‘i districts. According to the department, the accounts have been inactive since FY2007, and the moneys now go directly to the counties.

Temporary Deposits—Payroll Overpayment Trust Account (trust account)

Administratively established

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$1	\$1	\$1	\$1	\$1
Revenues	0	0	0	0	1
Interest	0	0	0	0	0
Expenditures	0	0	0	0	0
Transfers (net)	0	0	0	0	0
Ending Balance	\$1	\$1	\$1	\$1	\$2
Encumbrances	\$0	\$0	\$0	\$0	\$0

This account continues to meet the criteria for a trust account. This account was established in 2008 as a temporary deposit account for employees who received a payroll overpayment. When the total

overpayment amount has been recovered in full from the employee, moneys are taken from this account and deposited into the payroll clearance fund.

Undistributed Tax Collections Accounts (trust account)

Administratively established

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	(\$48,218)	(\$25,910)	(\$20,702)	(\$12,403)	(\$12,644)
Revenues	6,529,244	6,621,566	6,957,566	7,383,048	7,551,629
Interest					
Expenditures	(6,506,936)	(6,619,241)	(6,960,034)	(7,385,611)	(7,547,255)
Transfers (net)*	0	2,883	10,767	2,322	2,997
Ending Balance	(\$25,910)	(\$20,702)	(\$12,403)	(\$12,644)	(\$5,273)
Encumbrances	\$0	\$0	\$0	\$0	\$0

*Transfers were made from the Tax Reserve Fund for refunds that were rejected or cancelled.

This account continues to meet the criteria for a trust account. These accounts were established as clearing accounts for taxes collected on behalf of the various counties. Separate accounts were established for the Honolulu, Maui, Hawai‘i, and Kaua‘i districts. All taxes collected by the department are deposited into these accounts and then disbursed to other trust accounts. Funds and accounts receiving disbursements from these accounts may include the Tax Reserve Fund (to provide taxpayers refunds for overpayments) and the Taxes-Paid-Under-Protest Accounts.

Unemployment Tax Clearance Accounts (special fund)

Administratively established

Financial Data for FY2013–2017 (in thousands)

	FY2013	FY2014	FY2015	FY2016	FY2017
Beginning Balance	\$485	\$485	\$485	\$485	\$485
Revenues	0	0	0	0	0
Interest	0	0	0	0	0
Expenditures	0	0	0	0	0
Transfers (net)	0	0	0	0	0
Ending Balance	\$485	\$485	\$485	\$485	\$485
Encumbrances	\$0	\$0	\$0	\$0	\$0

This fund does not meet the criteria for a special fund and should be reclassified as a trust account. These accounts are used as clearing accounts for the deposit of unemployment taxes owed to the Unemployment Compensation Trust Fund.

Chapter 3

The Department of Taxation Did Not Report Non-General Funds As Required by Law

As we reported in our *Study of the Transfer of Non-general Funds to the General Fund*, Report No. 12-04, special, revolving, and other types of non-general funds collectively represent about half of the State's operating budget — moneys that are not subject to the same level of legislative scrutiny as the general fund. Accurate and complete reporting of all funds as required by law would greatly improve the Legislature's oversight and control of these funds and provide increased budgetary flexibility. Fund reports are one of the primary means through which the Legislature tracks non-general funds. The reports are used to monitor fund balances and identify excess moneys for possible transfer to the general fund.

Section 37-47, HRS, requires departments to submit to the Legislature an annual report of each non-general fund account including information such as the intended purpose of the fund, current program activities supported by the fund, and financial data. The Director of Finance annually issues a memorandum requesting all departments to complete and submit Form 37-47, *Report on Non-General Fund Information*, to the Department of Budget and Finance for each of their non-general funds. The Department of Budget and Finance compiles a report of all non-general fund accounts and submits it to the Legislature prior to the start of each legislative session.

Section 37-52.5, HRS, requires the Judiciary and any department that administratively establishes a new fund or account to submit a report to the Legislature. The report must be filed within 30 working days of a fund or account's creation and should include a justification for the fund or account and identification of its sources of revenue. In addition, prior to the start of each legislative session, the law also requires each department to submit to the Legislature a listing of all administratively established funds or accounts along with a statement of their revenues, expenditures, encumbrances, and ending balances for each fund or account.

During our review of DoTAX’s non-general funds, we noted non-compliance with statutory requirements to report financial activity and balances, as required by Section 37-47, HRS, as well as fund information for administratively established funds and accounts under Section 37-52.5, HRS. DoTAX did not report to the 2017 Legislature all non-general funds with balances totaling \$262,000 at the end of FY2016, as shown in Exhibit 3.1. As shown in Exhibit 3.2, DoTAX had administratively created non-general funds with balances totaling \$262,000 that were not reported to the Legislature, as required by Section 37-52.5, HRS.

**Exhibit 3.1
DoTAX Funds and Trust Accounts Not Reported to the Legislature**

Fund Name	Fund Type	FY2016 Ending Balance (rounded)
Est/Adm License and Permit Tobacco and Cigarette	Special	\$43,000
IRS Refund Intercept Account	Trust Account	1,000
Litigated Claims Fund	Trust	10,307,000
Sales of Assets for Delinquent Taxes – O’ahu	Trust Account	3,000
Special Enforcement Section Collections Trust Account	Trust Account	500,000
Tax Reserve Fund	Trust	-
Taxes-Paid-Under-Protest Accounts	Trust Account	20,000
Taxes Payable to Counties – Fuel Accounts	Trust Account	1,546,000
Temporary Deposits – Payroll Overpayment Trust Account	Trust Account	1,000
Undistributed Tax Collections Accounts	Trust Account	(12,644,000)
Unemployment Tax Clearance	Special	485,000
DoTAX Total		\$262,000

Source: Office of the Auditor

Exhibit 3.2**DoTAX Administratively Created Funds and Trust Accounts Not Reported to the Legislature**

Fund Name	Fund Type	FY2016 Ending Balance (rounded)
Est/Adm License and Permit Tobacco and Cigarette	Special	\$43,000
IRS Refund Intercept Account	Trust Account	1,000
Litigated Claims Fund	Trust	10,307,000
Sales of Assets for Delinquent Taxes – O’ahu	Trust Account	3,000
Special Enforcement Section Collections Trust Account	Trust Account	500,000
Taxes-Paid-Under-Protest Accounts	Trust Account	20,000
Taxes Payable to Counties – Fuel Accounts	Trust Account	1,546,000
Temporary Deposits – Payroll Overpayment Trust Account	Trust Account	1,000
Undistributed Tax Collections Accounts	Trust Account	(12,644,000)
Unemployment Tax Clearance	Special	485,000
DoTAX Total		\$262,000

Source: Office of the Auditor

Office of the Auditor's Comments on the Affected Agency Response

Comments on Agency Response

We transmitted a draft of this review to DoTAX on October 25, 2017. DoTAX provided its written response to the draft report dated October 31, 2017 (Attachment 1).

DoTAX generally agreed with our findings and will take appropriate action to close one special fund and three trust accounts that did not meet criteria and inform the Department of Budget and Finance of our recommendation to reclassify one special fund to a trust account. DoTAX will also comply with reporting requirements.



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LT. GOVERNOR



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October 31, 2017

TO: Leslie H. Kondo
State Auditor

FROM: Maria E. Zielinski
Director of Taxation

A handwritten signature in blue ink, appearing to read "mz", is written over the printed name of Maria E. Zielinski.

SUBJECT: Response to the Review of Special, Revolving, Trust Funds, and Trust Accounts

Due to updated processes, we agree with the findings of the State Auditor that the following funds should be closed and are no longer used by the department:

- Est/Adm License and Permit Tobacco and Cigarette
- IRS Refund Intercept Account
- Special Enforcement Section Collections Trust Account
- Taxes Payable to Counties – Fuel Accounts

The State Auditor recommends reclassifying the Unemployment Tax Clearance Accounts (special fund) as a trust account. Because Budget and Finance also uses this account, we will inform them of the recommendation.

Going forward, the Department will report all non-general funds per Section 37-47, HRS.

Please let me know if you have any questions.

