

Department of Transportation Airports Division

State of Hawaii

(An Enterprise Fund of the State of Hawaii)

Single Audit Reports

June 30, 2017

**Department of Transportation Airports Division
State of Hawaii**

(An Enterprise Fund of the State of Hawaii)

June 30, 2017

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**Department of Transportation Airports Division
State of Hawaii**

(An Enterprise Fund of the State of Hawaii)

**Schedule of Expenditures of Federal Awards
Year Ended June 30, 2017**

Federal Grantor/Program Title	Federal CFDA Number	Total Federal Expenditures
U.S. Department of Transportation		
Federal Aviation Administration - Airport Improvement Program	20.106	\$ 20,368,305
U.S. Department of Agriculture		
Animal and Plant Health Inspection Service (APHIS)	10.025	<u>380,192</u>
Total federal expenditures		<u>\$ 20,748,497</u>

Department of Transportation Airports Division State of Hawaii

(An Enterprise Fund of the State of Hawaii)

Notes to Schedule of Expenditures of Federal Awards Year Ended June 30, 2017

Notes to Schedule

(1) General

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal award activity of the Airports Division, Department of Transportation, State of Hawaii (the Airports Division) under programs of the federal government for the year ended June 30, 2017. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the Airports Division, it is not intended to and does not present the financial position, changes in net assets or cash flows of the Airports Division.

(2) Basis of Accounting

Expenditures reported on the Schedule are reported on the accrual basis of accounting basis of accounting. Such expenditures are recognized following, as applicable, either the cost principles in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments* or the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Negative amounts shown on the Schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years. The Airports Division has elected not to use the 10 percent de minimis indirect cost rate allowed under the Uniform Guidance.

(3) Federal Loans

The Airports Division had no federal loans that they were administering as of June 30, 2017.

**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***

The Auditor
State of Hawaii
Oahu, 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 Airports Division, Department of Transportation, State of Hawaii (an enterprise fund of the State of Hawaii) (the Airports Division), which comprise the statement of net position as of June 30, 2017, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 8, 2017, which contained an “Emphasis of Matters” paragraph for the identification of the financial statements as individual fund statements not representing the State of Hawaii as a whole.

Internal Control Over Financial Reporting

Management of the Airports Division is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the financial statements, we considered the Airports Division’s internal control to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Airports Division’s internal control. Accordingly, we do not express an opinion on the effectiveness of the Airports Division’s internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses.

The Auditor
State of Hawaii

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 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. 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 Airports Division's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs as item 2017-001 to be a material weakness.

Compliance and Other Matters

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

Airports Division's Response to Findings

The Airports Division's response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The Airports Division's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

We also noted certain matters that we reported to the Airports Division's management in a separate letter dated December 8, 2017.

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 Airports Division'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 Airports Division's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

BKD, LLP

Denver, Colorado
December 8, 2017

Independent Auditor's Report on Compliance for the Major Federal Program; Report on Internal Control Over Compliance; and Report on Schedule of Expenditures of Federal Awards as Required by the Uniform Guidance

The Auditor
State of Hawaii
Oahu, Hawaii

Report on Compliance for Each Major Federal Program

We have audited the Airports Division's, Department of Transportation, State of Hawaii (an enterprise fund of the State of Hawaii) (the Airports Division) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on the Airports Division's major federal program for the year ended June 30, 2017. The Airports Division's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, contracts and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the Airports Division's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Airports Division's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

The Auditor
State of Hawaii

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the Airports Division's compliance.

Opinion on the Major Federal Program

In our opinion, the Airports Division complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2017.

Report on Internal Control Over Compliance

Management of the Airports Division is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Airports Division's internal control over compliance with the types of requirements that could have a direct and material effect on its major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Airports Division's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

The Auditor
State of Hawaii

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the financial statements of the Airports Division as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Airports Division's basic financial statements. We issued our report thereon dated December 8, 2017, which contained an unmodified opinion on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

BKD, LLP

Denver, Colorado
February 23, 2018

**Department of Transportation Airports Division
State of Hawaii**

(An Enterprise Fund of the State of Hawaii)

Schedule of Findings and Questioned Costs (continued)

Year Ended June 30, 2017

7. Identification of major programs:

<u>Cluster/Program</u>	<u>CFDA Number</u>
U.S. Department of Transportation – Federal Aviation Administration – Airport Improvement Program	20.106

8. Other threshold used to distinguish between Type A and Type B programs: \$750,000.

9. Auditee qualified as low-risk auditee?

Yes

No

Department of Transportation Airports Division State of Hawaii

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Schedule of Findings and Questioned Costs (continued) Year Ended June 30, 2017

Section II – Financial Statement Findings

Reference Number	Summary of Finding	Status
2017-001	<p>Criteria or Specific Requirement: Management is responsible for establishing and maintaining effective internal controls over financial reporting to support the preparation of financial statements and related footnote disclosures in accordance with generally accepted accounting principles. Timely accounting tasks such as cross-checks and reviews play a key role in proving the accuracy of accounting data and financial information that comprise year-end financial statements.</p> <p>Condition: During the 2017 audit, a number of variances between account balances and supporting documentation provided were identified. In the aggregate, the variances identified below could be indicative of a larger internal control issue. The following conditions were noted:</p> <p>Recorded audit adjustments:</p> <ol style="list-style-type: none"> (1) To decrease revenue erroneously recognized in fiscal year 2017 (\$8.5 million) (2) To record principal payments on lease revenue certificates of participation as an offset to the liability rather than as an expense (\$6.3 million) (3) To decrease the principal on the lease revenue certificates of participation balance for amounts erroneously recorded twice (\$4.7 million) (4) To increase expense for costs inappropriately capitalized as construction in progress (\$4.5 million) <p>Proposed audit adjustments not recorded:</p> <ol style="list-style-type: none"> (1) To increase depreciation for construction in progress projects completed in the period (\$4.0 million) (2) To decrease construction in progress for excess interest capitalized (\$3.0 million) (3) To increase federal grant revenue (\$0.9 million) <p>Context: The Airports Division’s Finance Department is primarily responsible for the financial reporting process. Financial records are maintained on a cash basis throughout the year, and the year-end close process requires financial information to be captured that is only compiled and analyzed annually. During the year-end close process, the Finance Department converts the cash basis financial records to the accrual basis of accounting for reporting requirements in the audited financial statements.</p> <p>The Airports Division experienced significant turnover in the Finance Department over the past few years. There was a loss of employees who had institutional knowledge of the Airports Division and, more specifically,</p>	

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Schedule of Findings and Questioned Costs Year Ended June 30, 2017

Reference Number	Summary of Finding	Status
	<p>primary responsibility for the preparation of reconciliations. These issues were exacerbated by an overall lack of personnel resources. In an attempt to address the lack of resources, the Airports Division hired contract accountants to assist with the preparation of account reconciliations.</p> <p>Effect: If left uncorrected, these errors would have materially misstated the financial statements.</p> <p>Cause: As mentioned above, the Airports Division has experienced significant turnover in the finance department, including several individuals who had been employed for many years. The Airports Division has also experienced difficulty in replacing these positions and has been forced to operate with reduced staffing for the majority of the fiscal year. This has placed considerable pressure on the Airports Division Finance Department. To help alleviate this situation the Airports Division hired contract accountants to assist with preparation for the audit; however, the contract was executed very late in the fiscal year and not long before the audit started. Therefore, Finance Department personnel and contract accountants, who were not previously responsible for the year-end close process or preparation of the financial statements, were assigned account reconciliations and financial analyses to complete. These analyses were not subject to a timely secondary review, given personnel constraints and the timing of year-end deadlines. As a result, errors were made in compiling information for financial reporting purposes.</p> <p>Recommendation: We recommend the Airports Division continue to cross-train Finance Department employees on the roles and responsibilities within the accounting and financial reporting cycles. We also recommend the Airports Division continue to develop and complete written policies and procedures documenting all accounting employees' roles and responsibilities in relation to accounting procedures, as well as audit workpaper preparation. This would include a formal, documented review where all reconciliations and analyses are reviewed by a secondary employee with knowledge of the subject matter. These combined recommendations will aid in transition of primary responsibilities to new personnel should turnover in Finance Department positions occur again in the future and assist in proving the accuracy of financial data supporting the annual financial statements.</p> <p>Views of Responsible Officials and Planned Corrective Action: We agree with the finding. See separate report for corrective action plan.</p>	

**Department of Transportation Airports Division
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**Schedule of Findings and Questioned Costs (continued)
Year Ended June 30, 2017**

Section III – Federal Award Findings and Questioned Costs

Reference Number	Summary of Finding	Questioned Costs
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No matters are reportable.

**Department of Transportation Airports Division
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Status of Prior Audit Findings

Year Ended June 30, 2017

Reference Number	Summary of Finding	Questioned Costs
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No matters are reportable.