COVID-19 SPECIAL PROJECTS

Report on Potential Available State Moneys Identified in Prior Audit Reports

A Report to the Legislature of the State of Hawai‘i

Report No. 20-07
May 2020
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

In 2020, a novel coronavirus that causes COVID-19 forced the State of Hawai‘i to take unprecedented measures to protect public health at a great cost to the Islands’ economy. Efforts to mitigate the impact of the global pandemic shuttered all but essential local businesses and slowed tourism to a trickle. Job loss and wage reductions quickly followed. Tax collections – from general excise taxes, transient accommodation taxes, and income taxes, among others – are projected to tilt sharply downward. Under these extraordinary conditions, the Office of the Auditor is reviewing prior audit reports and other information to identify potential revenue sources. In this report, we highlight portions of our prior audit reports about the Deposit Beverage Container Deposit Fund, Report No. 19-08; the Special Land and Development Fund, Report No. 19-12; and the Land Conservation Fund, Report No. 19-01.

Leslie H. Kondo
State Auditor
In 2020, a novel coronavirus that causes COVID-19 forced the State of Hawai‘i to take unprecedented measures to protect public health, at great cost to the Islands’ economy. Efforts to mitigate the impact of the global pandemic shuttered all but essential local businesses and slowed tourism to a trickle. Job loss and wage reductions quickly followed. Tax collections – from general excise taxes, transient accommodations taxes, and income taxes, among others – are projected to tilt sharply downward. Under these extraordinary conditions, the Office of the Auditor is reviewing prior audit reports and other information to identify potential revenue sources, along with accounts and subaccounts associated with special and revolving funds that have excess state moneys. The Legislature transferred moneys in certain accounts and subaccounts to the General Fund in 2002, during the economic downturn that followed the September 11, 2001 terrorist attacks (Act 178, Session Laws of Hawai‘i (SLH) 2002) and again since FY2018, the most recent year we audited, the redemption rate was below 65 percent.

Annual increases in unclaimed deposit fees swell the fund’s cash balance to $48.82 million

Introduction

Annual increases in unclaimed deposit fees swell the fund’s cash balance to $48.82 million

The Fund
Department of Health’s Deposit Beverage Container Deposit Fund

The Current Balance
$48.82 million

About the Fund
The fund is used to administer the Deposit Beverage Container Program, which requires consumers to pay a $0.05 deposit on certain cans and bottles. When consumers bring the empty containers to redemption centers, their deposits are returned and redemption centers are reimbursed through the fund. The percentage of empty containers being redeemed, i.e., the redemption rate, has been steadily declining, leaving unclaimed deposits to accumulate in the special fund.

*A declining redemption rate = a growing fund balance*

For much of the Deposit Beverage Container Program’s history, the redemption rate has been above 70 percent, hitting a high of 79 percent in FY2009; however, since then, consumers have been redeeming containers at steadily declining rates. In FY2015, the redemption rate

Exhibit 1
Deposit Container Redemption Rates and Ending Cash Balances

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1 Department of Health, Environmental Management Division, Solid and Hazardous Waste Management Branch
Exhibit 2
S-313 Deposit Beverage Container Deposit Special Fund
For the past five years, average revenues have exceeded average expenditures by almost $5.6 million.

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<td>$0</td>
<td>$(4,301)</td>
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fell below 70 percent for the first time since 2007. In FY2018, the most recent year we audited, the redemption rate was below 65 percent. That means, for every 100 cans and bottles that a consumer pays the $0.05 deposit, more than 35 of those containers are not being redeemed and the associated deposits sit dormant in the fund.

During the Great Recession, the Legislature authorized the transfer of excess moneys from the Deposit Beverage Container Deposit Fund to the General Fund – up to $1 million in 2010 and up to $300,000 in 2011.

In our Deposit Beverage Container Deposit Fund audit for FY2012, we noted Act 192, SLH 2010, and Act 124, SLH 2011, transferred a combined $1.3 million in excess moneys from the Deposit Beverage Container Deposit Fund to the General Fund during FY2011.

A self-sustaining fund

In our most recent audit, we reported the program, at June 30, 2018, had revenues of $24.6 million and expenditures of $17.5 million, resulting in a $7.1 million increase in fund balance to $37.7 million. Based on information from the State of Hawai’i’s Financial Accounting and Management System (FAMIS), at the end of FY2019, the fund had grown another $6.6 million to $43.4 million. We retrieved current information from FAMIS on April 15, 2020; according to those unaudited figures, the Deposit Beverage Container Deposit Fund’s FY2020 year-to-date balance was $48.8 million, an increase in fund balance of $5.4 million.

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2 Report No. 19-08, Financial and Program Audit of the Department of Health’s Deposit Beverage Container Deposit Program, [for the fiscal year ended] June 30, 2018

3 FY2019 and FY2020 totals are unaudited.
As shown in Exhibit 2, revenues exceeded expenditures by $2.9 million to $7.1 million each of the past five fiscal years, indicating the program would have sufficient funding to operate if the excess is transferred into the General Fund. In FY2018, the Deposit Beverage Container Program’s operating and administrative costs together totaled $1.2 million, according to audited financial statements.4

More information about the Deposit Beverage Container Deposit Fund can be found in our past reports:

**FY2018, Report No. 19-08:**

**FY2016, Report No. 17-02:**

**FY2014, Report No. 15-02:**

**FY2012, Report No. 13-08:**

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The Office of the Auditor is reviewing prior audit reports and other information to identify potential revenue sources, along with accounts and subaccounts associated with special and revolving funds that have excess state moneys. This report highlights relevant material from Report No. 19-12, *Audit of the Department of Land and Natural Resources’ (DLNR) Special Land and Development Fund (SLDF)*, which this office issued in June 2019. As detailed below, although DLNR met its statutory obligation to remit 20 percent of its ceded lands revenues to the Office of Hawaiian Affairs, the department transferred only a portion of the remainder to the State’s General Fund. For the three fiscal years covered in our audit, DLNR retained more than $27 million in ceded lands revenues in the SLDF.

**Introduction**

*DLNR retained 58 percent ($27.2 million) of its ceded lands revenues for its own programs.*

In FY2015 through FY2017, DLNR retained $27.2 million (58 percent) of the revenues from ceded lands controlled by the Board of Land and Natural Resources for its own programs.
Ceded Land Revenues Retained by the Department of Land and Natural Resources

In our audit of the SLDF, we reported that in FY2015, FY2016, and FY2017, DLNR received a total of $47.1 million in revenues from leases and permits for ceded lands under the control of the Board of Land and Natural Resources. During that three-year period, DLNR remitted 20 percent of those ceded lands revenues ($9.4 million) to the Office of Hawaiian Affairs, as required by statute, but did not transfer the remaining 80 percent to the General Fund. Instead, DLNR transferred only $8.71 million (18 percent) of the ceded lands revenues to the General Fund and retained $27.2 million (58 percent) in the SLDF for its own programs.

We questioned whether DLNR was superseding the Legislature’s authority by deciding to retain the revenues from ceded lands for its own use without specific legislative approval to do so. We suggested that policy decisions about the use of ceded land revenues are the purview of the Legislature – not an individual state department – and suggested that the department seek guidance from the Legislature about its authority to keep and spend the ceded land revenues.

We are reproducing the portion of our Report No. 19-12 that more thoroughly describes our concern about DLNR’s decision to keep and use the revenues from ceded lands.

About the Fund

The SLDF was statutorily created in 1962 and is one of 18 special funds maintained by DLNR. The SLDF receives proceeds from the sale of public lands; mineral and water rights; rents from leases, licenses, and permits; fees, fines, and other administrative charges included in Chapter 171, Hawai‘i Revised Statutes (Management and Disposition of Public Lands); a portion of the highway fuel tax; moneys for the commercial use of the public trails and access; and a portion of transient accommodations tax revenues.

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1 Ceded lands are the approximately 1.8 million acres of land that were transferred, or ceded, to the United States at the time of the annexation of Hawai‘i in 1898. These lands consisted of crown lands once property of the Hawaiian monarchy, and government lands of the Kingdom of Hawai‘i. The Admission Act, which granted statehood to Hawai‘i in 1959, returned the lands to the new State of Hawai‘i and provided that they be held as a public trust. As of May 5, 2020, DLNR’s ceded lands inventory was 1,283,766.543 acres.
The SLDF is the funding source for the entire annual operating budget of the Land Division, the Office of Conservation and Coastal Lands, and the Engineering Division’s Dam Safety and Geothermal programs. The SLDF also funds other positions within DLNR and provides funding support to the Division of State Parks and various resource protection programs administered by the Division of Forestry and Wildlife.

### Special Land and Development Fund – Past Five Fiscal Years FY2015-FY2019 and FY2020 YTD

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<td>$21,724,569</td>
<td>$26,736,526</td>
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<td>$21,192,678</td>
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<td>$12,141,593</td>
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<td><strong>Cash Transfers</strong></td>
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<td>$(1,191,558)</td>
<td>$(1,228,386)</td>
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<tr>
<td><strong>Ending Cash</strong></td>
<td>$19,855,730</td>
<td>$21,075,846</td>
<td>$21,724,569</td>
<td>$26,736,526</td>
<td>$32,720,267</td>
<td>$36,147,972</td>
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Review of the Department of Land and Natural Resources’ Special Land Development Fund

ACCORDING TO the Hawai‘i Admission Act, which made Hawai‘i a U.S. state in 1959, revenue from ceded lands are to be held by the State as a public trust for the following purposes: (1) support of public education; (2) betterment of the conditions of Native Hawaiians; (3) development of farm and home ownership; (4) public improvements; and (5) provision of lands for public use. In 1979, the Legislature enacted Chapter 10, HRS, which created the Office of Hawaiian Affairs. A year later, the Legislature amended Chapter 10, adding section 10-13.5, HRS, which requires that 20 percent of all revenues from ceded lands be expended by OHA for, among other things, the betterment of conditions of Native Hawaiians.

In a December 1, 2010 submittal to the Land Board, the Land Division Administrator reported that, over the years, after paying its 20 percent to OHA, the 80 percent portion of ceded land revenues was used to “supplement” the general fund. However, in the past several years, according to the Land Division Administrator, a portion of these funds had been used to cover the shortfalls of other agencies’ OHA payments. Recently, these agencies had begun to regularly provide their 20 percent to OHA; therefore, he reasoned that the remaining 80

Superseding the Legislature?

Did the Land Board overstep its authority when it designated Land Division properties on ceded lands as “income-producing assets”?

CEDED LANDS are the approximately 1.8 million acres of land that were transferred, or ceded, to the United States at the time of the annexation of Hawai‘i in 1898. These lands consisted of crown lands once property of the Hawaiian monarchy, and government lands of the Kingdom of Hawai‘i. The Admission Act, which granted statehood to Hawai‘i in 1959, returned the lands to the new State of Hawai‘i and provided that they be held as a public trust. The Act stated that management and disposition of such lands should be used as called for by the constitution and laws of Hawai‘i.

What are Ceded Lands?
percent could now be “returned” to the SLDF. He wrote: “Based on the express language of the SLDF as noted above, the remaining 80% of ceded land revenues (after paying OHA its 20% share) is supposed to be deposited directly into the SLDF and expended by the Department in accordance with HRS 171-19.”

The Land Division Administrator recommended that the Land Board designate 88 hotel, resort, commercial, and industrial properties on ceded land as “income-producing assets” and authorize the deposit of the revenues from these properties (minus the 20 percent obligated to OHA) into the SLDF so that they may be “expended for departmental purposes in accordance with HRS 171-19.3.”

Eighty of the properties are located on Hawai‘i Island, with four on O‘ahu and two each on Maui and Kaua‘i. In 2010, the total annual lease rent for the properties was $3.6 million, of which $2.9 million (80 percent) would be deposited into the SLDF. Some of the more recognizable properties on the Land Division Administrator’s proposed list were the Hilton Hawaiian Village Pier and Olomana Golf Links on O‘ahu and the Hilo Hawaiian Hotel on the Big Island.

The Land Board approved the proposal on December 1, 2010. In February 2011, the Land Division proposed amending the board action to add 42 additional properties to the list of income-producing assets. Eight months later, it proposed adding five more properties to the list. The Land Board approved both proposals.

From FY2015 – FY2017, the department deposited approximately $27.2 million (58 percent of total ceded land revenues) into DLNR special fund accounts for use by those DLNR programs and transferred approximately $8.7 million (18 percent) to the general fund.

We question the Land Division Administrator’s interpretation of the statutory provision that created the SLDF, specifically his belief that the revenues from ceded lands administered by the Land Division (after OHA’s 20 percent share) are intended to fund the division and other department programs.

We question the Land Division Administrator’s interpretation of the statutory provision that created the SLDF, specifically his belief that the revenues from ceded lands administered by the Land Division (after OHA’s 20 percent share) are intended to fund the division and other DLNR programs. It is unclear that the uses of the SLDF are consistent with the purposes for which ceded land revenues can be used under the Admissions Act. The ceded lands and the revenues therefrom are held by the State as a public land trust and can only be used for the five specific purposes listed in Section 5(f) of the Admissions Act.

We also question whether DLNR is superseding the Legislature’s power to decide the appropriate use of ceded lands revenues. The Admissions Act returned to the State approximately 1.8 million acres of land that had been transferred, or ceded, to the United States at the time of annexation of Hawai‘i in 1898 and provided the lands be held in a public land trust for one or more of five specific purposes identified in the Act. By keeping the ceded lands revenues (after OHA’s 20 percent share) in the SLDF, DLNR – not the Legislature – is deciding the appropriate use of those moneys; DLNR – not the Legislature – has assumed the State’s fiduciary responsibility to decide how to use the ceded lands revenues, including uses such as the support of public schools that are clearly outside of the purposes of the SLDF.

We believe significant policy decisions about the use of state funds, including the use of ceded land revenues, are the purview of the Legislature – not an individual agency – and suggest that DLNR seek guidance from the Legislature about whether the department is authorized to keep and spend ceded land revenues without specific Legislative approval to do so.
COVID-19 SPECIAL PROJECTS

Review of the Department of Land and Natural Resources’ Land Conservation Fund

In FY2017, the Land Conservation Fund’s cash balance was $27.8 million, of which $16.6 million sat idle, not earmarked for projects or program expenses.

Introduction

The Office of the Auditor is reviewing prior audit reports and other information to identify potential revenue sources, along with accounts and subaccounts associated with special and revolving funds that have excess state moneys. This review highlights relevant material from Report No. 19-01, Audit of the Department of Land and Natural Resources’ Land Conservation Fund, issued in January 2019.

Expenditure Cap Contributes to Growing Cash Balance

Up to $6.8 million\(^1\) is deposited into the Land Conservation Fund (LCF) each fiscal year to support Department of Land and Natural Resources’

\(^1\) The primary source of funding is 10 percent of the State’s conveyance tax revenue or $6.8 million, whichever is less.

Since FY2006, the program has awarded more than $47.3 million to fund 58 projects. By the end of FY2017 awards totaling $11.9 million were still pending.
(DLNR) Legacy Land Conservation Program, but expenditures from the special fund are capped at $5.1 million per fiscal year. This budget constraint limits the amount of moneys available to the program, but it has also caused the fund’s cash balance to nearly double over five fiscal years – from $14.1 million in FY2013 to $27.8 million in FY2017, of which $16.6 million had not been earmarked for projects or program expenses. As of May 6, 2020, the fund balance was $33.2 million, according to recent data we gathered from the Department of Accounting and General Services’ Financial Accounting and Management Information System (FAMIS).

Moneys for Pending Projects Can Languish for Years

State agencies, counties, and nonprofit organizations apply for grants from the Legacy Land Conservation Program to acquire land or conservation easements and for administrative expenses. Since FY2006, the program has awarded more than $47.3 million to fund 58 projects. By the end of FY2017, the Legacy Land Conservation Program had completed 31 of these projects; 8 projects had been discontinued; while 19 others, with awards totaling $11.9 million, were still pending. Of the pending projects, 10 had tied up money for more than 2 years, including 7 grants to state agencies. We found that, whereas the Board of Land and Natural Resources enters into contracts with county and nonprofit grantees that stipulate completion dates, no such contracts are executed for grants awarded to state agencies. With no completion requirements, grant-funded state projects can remain active indefinitely, making earmarked funding unavailable for other uses.

Exhibit 3
Pending Projects by Number of Years Funded
Exhibit 4
Fund Balance for FY2015-FY2019 and 2020 Year-to-Date

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<td>Beginning Cash</td>
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<td>Expenditures</td>
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<td>$35,161,509</td>
<td>$33,174,478</td>
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About the Fund

In 1973, the Legislature laid the foundation for a land conservation program and fund, formalizing the importance of protecting and preserving the natural beauty and historic significance of Hawai‘i’s lands through state-funded acquisition and management. In 2005, the Legislature provided the land conservation program with a dedicated funding source – 10 percent of conveyance tax collected – and repurposed an existing fund, renaming it the Land Conservation Fund, for the express purpose of acquiring land with value as a state resource. The Land Conservation Fund and the associated Legacy Land Conservation Program are administered by the Department of Land and Natural Resources, which delegated that responsibility to its Division of Forestry and Wildlife.