EXECUTIVE SUMMARY

Performance Audit of Akaku: Maui Community Television (Akaku)

In April 2011, the Governor signed into law Act 19 (SLH 2011) which, among other things, requires the Department of Commerce and Consumer Affairs (DCCA), through its Cable Television Division (CATV), to conduct an annual performance audit, also known as a management audit, of each of the state's four public, educational, and governmental ("PEG") access organizations for the three years from July 1, 2011 through June 30, 2014. In response to the Act's requirement, CATV contracted with the Certified Public Accounting firm of Merina & Company, LLP (MCO) to conduct the performance audits.

MCO has organized their audit and reporting into five sections

- Introduction
- Management and Oversight
- Operations
- Financial
- Compliance

The performance audit was conducted in accordance with auditing standards generally accepted in the United States of America and the standards for performance audits contained in *Government Auditing Standards* (Yellow Book), issued by the Comptroller General of the United States.

The most significant comments and recommendations for improvement resulting from our audit are presented below.

Management and oversight significant comments and one recommendation include:

- For the period from January 1, 2006 through June 30, 2011:
  - Akaku maintained detailed meeting minutes that show the Board of Directors due diligence and governance of the organization.
  - Akaku's management team appears to have the appropriate experience and knowledge for the size of the PEG.
  - Akaku should develop a strategic plan, for a period not less than 3 years, which includes a detailed plan, measurable goals and triggers to implement the plan. The strategic plan should address Akaku's deficit spending, discussed below.

Operations significant comments and recommendations include:

Operating Facilities

- Building community involvement and awareness is what Akaku views as fulfilling the organization's core purpose.
- Akaku has adapted well to changing user needs and the opportunities for service brought about by the Internet.
- Akaku's success in building community awareness to meet the needs in Maui County which are informational and also social, is one of the positive marks of its particular character, and is arguably well in line with its mission and what Akaku sees as the organization's core purpose.
- Akaku should develop a marketing strategy to focus on drawing new residents in to use Akaku services and equipment.

Transition from Analog to Digital and High Definition (HD)

- Akaku is in the process of making the transition from analog to digital and HD. Akaku has and will continue to purchase digital equipment that has the capability to convert digital to HD in the future. Although there's no timeline for the conversion to HD in Maui County, this places Akaku in a position to provide these services in the future, when necessary.

Metrics: The Measurement of Results

- Akaku has been successful in keeping and reporting statistics useful for both regulators and management in the past.

Financial significant comments and recommendations include:

Financial Ratios

- Akaku's financial metrics show a consistent pattern of use of available funds with improvement in 2011. The use of resources for services has exceeded the operating funds available for 2006 though 2010. This cannot continue for much longer and in 2011 Akaku shows some improvement. Going forward either its spending has to be brought in line with its available resources or the funding for the organization has to be increased. Akaku ratios show improvement in 2011 but the historical trends are concerning. In order to continue to improve these ratios Akaku needs to create and follow a strategic plan that includes ensuring expenses are in line with revenues and/or increase current revenues.

- Deficit spending is when the organizations revenues do not cover the expenses; therefore the excess spending is covered by cash and investments (i.e. Operating Reserve) or by borrowing. Short-term deficits can, but not always, represent an investment for future benefits, provided that there is an underlying plan or strategy. This does not appear the case for Akaku. Organizations cannot operate at a deficit for the long-term; they will eventually run out of Cash, Cash Equivalents and Investments. For 2006 through 2010 Akaku operated at a deficit. The only year included in this performance audit that did not have deficit spending was 2011.

- In order for Akaku to not fully deplete its Operating Reserve Akaku has to stop operating at a deficit. In 2011, Akaku did not operate at a deficit, but the historical trend of operating at a deficit from 2006 through 2010 are concerning. Akaku needs to ensure expenses are in line with revenues and/or increase current revenues or find new revenue sources (i.e. grants, fundraising, and fees). If Akaku does not continue to address this excessive spending, the organization is in danger of depleting its reserves, and will be unable to sustain operations at the current levels.

Items Identified By Akaku's Independent External Auditors

- The audits for the fiscal years ended June 30, 2006 through June 30, 2011 did not identify any deficiencies in internal control or management advisory comments.

Compliance significant comments and recommendations include:

- It appears that Akaku is making a conscious effort to meet its reporting deadlines outlined in its June 17, 1999 agreement with DCCA and April 13, 2006 letter from DCCA. However Akaku should implement a tickler system on their calendars to notify them of reporting deadlines to ensure reports are timely submitted to DCCA.

- Akaku should implement controls to ensure the operations and capital accounts are properly maintained and are not commingled without prior written approval from DCCA. Not properly maintaining separate accounts could jeopardize Akaku's contract with DCCA.

Response form Akaku

COMMENTS OF AKAKU: MAUI COMMUNITY TELEVISION
RE: PERFORMANCE AUDIT OF AKAKU: MAUI COMMUNITY TELEVISION
CONDUCTED BY: MERINA & COMPANY, LLP

RESPECTFULLY SUBMITTED BY

Jay April
President and Chief Executive Officer
Maui County Community Television Inc.
Dba, Akaku: Maui Community Television

November 14, 2012,

Akaku management has reviewed the draft performance audit report by Merina & Company (MCO) released in August 2012 and its revised report released in October 2012 and would like to provide the following formal response to the significant comments and recommendations in the applicable sections of the report:

In the Management and Oversight section of the report, Merina & Company (MCO) stated the following:

Akaku should develop a strategic plan, for a period not less than 3 years, which includes a detailed plan, measurable goals and triggers to implement the plan. The strategic plan should address Akaku's deficit spending discussed below

RESPONSE: Akaku has a strategic plan in place that has been in operation since 2010 and this plan is frequently updated with ongoing scenario planning. As noted in the report, these included a strategic planning board retreat that took place in the spring of 2012 with an outside professional facilitator and a series of detailed Strategic Planning Committee meetings, which took place in May, June, July and October of 2012. Akaku will submit detailed business plans to DCCA in its PEG Designation Proposal in order to address financial issues as recommended by MCO. With reference to deficit spending, please see comments in Financial section below.

In the Operating Facilities section, MCO stated:

Akaku should develop a marketing strategy to focus on drawing new residents in to use Akaku services and equipment

RESPONSE: Akaku currently uses a variety of methods to market services to all residents including new residents. These include on air promotions in a market where there is 90% cable penetration, social networks, email blasts, presence at community events, radio cross promotion and a variety of websites. As we move forward with PEG designation and franchise renewal we will be employing even more tools, including survey instruments to improve marketing efforts for Akaku's classes and services. It needs to be noted however, that unstable and arbitrary PEG channel placement by Oceanic Time Warner as a result of the analog to digital transition will continue to challenge these efforts.

In the Operating Facilities section on Metrics: The Measurement of Results - on page 11 under the heading, **Findings** there is a table that indicates students trained in Akaku classes for the years 2006 - 2011. This table is meant to *identify operating trends useful for Akaku management to know as well as for regulators and other stakeholders.*

Upon review, we noticed that under the years 2008 and 2011, there appeared to be a calculation by MCO that appeared to be a significant deviation from other years in the category of "Students trained in Akaku classes": (see 2008 and 2011 figures in bold below)

Number of Students Trained in Akaku Classes by Fiscal Year

2006	2007	2008	2009	2010	2011
637	858	**305**	551	605	**2,717**

Because the figures in 2008 and 2011 appeared to us as anomalies, we checked our DCCA Annual Reports submitted for FY2008 and FY 2011 and discovered the following information for clarification:

1. FY 2008 - Akaku education programs consist of a number of categories which include formal classes, special workshops, special trainings, youth camps, group trainings, media salons and producer nights on Maui and Molokai. There are also a number of students who take more than one class. Based on the report, we believe a more accurate total for 2008 is 661 people served by education on Maui and 59 on Molokai for a total of 720.

2. FY 2011 - Upon reviewing the education statistics for the FY2011 DCCA Annual Report it was discovered that attendees at all gubernatorial, primary and general election events were incorrectly recorded in the education total. It was also discovered that we had an exceptionally active Molokai educational component in 2011.We believe a more accurate and conservative total for people served by education on Maui and Molokai for FY2011 is 643, not 2,717.

In summary the corrected estimates are as follows:

2006	2007	2008	2009	2010	2011
637	858	**720**	551	605	**643**

In the Financial section of the report *MCO expressed a number of concerns about deficit spending from 2006 - 2010 but recognized a turnaround in 2011.*

RESPONSE: Akaku is currently not operating at a deficit. We fully expect that our audited financial statements for FY2012 will show positive cash flow and are confident that careful attention to expenses, identified income from our subsidiary and projected revenue from social enterprise consistent with our mission, will engender cautious optimism about our our bottom line in FY2013.

In retrospect, Akaku was subject to a "perfect storm" of operational and financial difficulties in 2005 and 2006 whereby special interests from the Maui land development community (who did not agree with federally protected content submitted to Akaku for air by unaffiliated, independent residents) funded an expensive, sophisticated campaign to significantly diminish the resource by influencing state agencies and others hostile to

PEG. Their goal was to orchestrate a raid on PEG funds and resources. This bitter political struggle resulted in a significant loss of revenue including a 33% reduction in franchise fee operating funds to Akaku for a three-year period and a 25% reduction after that. In 2007, the organization began to rebuild which required it to spend down its reserves due in part to high legal costs associated with protecting itself from a politically motivated, ongoing state procurement process. This undertaking lasted for five years and culminated in April 2011, when the Governor signed a bill to exempt PEG organizations from the requirement. In 2009-2010, Maui experienced the worst economic downturn since the Great Depression that materially affected revenues and the non-profit community has had to make adjustments to reflect this reality.

The good news is by cutting expenses and by practicing sound fiscal management, Akaku has reversed the trend of deficit spending and now enjoys positive cash flow for 2011 and 2012. We expect that upward trend to continue as we adjust to new revenue opportunities in what many experts project will be an improving economy.

Thank you for your interest in helping Akaku better serve all of our Maui Nui residents.

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MERINA
& COMPANY, LLP
Certified Public Accountants and Consultants

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

PARTNERS
KAMALA K. AUSTIN, CPA • TONYA M. MOFFITT, CPA

INDEPENDENT AUDITOR'S REPORT

We have completed the performance audit, also referred to as a management audit, of Akaku: Maui Community Television (Akaku) for the period January 1, 2006 through June 30, 2011. The purpose of the performance audit was to examine and report on the sufficiency of Akaku's organizational, planning, budget and operating documents, Akaku's compliance with applicable laws, regulations, and its contract with DCCA, and to analyze selected operational and financial parameters.

We conducted our performance audit as required pursuant to Act 19 (SLH 2011) which was passed by the Hawaii State Legislature in April 2011 and in accordance with auditing standards generally accepted in the United States of America and the standards applicable to performance 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 sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Merina & Company

Merina & Company, LLP
November 14, 2012

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Chapter 1

INTRODUCTION

Section 1(h) of Act 19 (SLH 2011)[1] sets out audit requirements for each Public, Educational, and Governmental (PEG) access organization as follows:

> "The department [meaning DCCA] shall conduct an annual management and financial audit of the access organization designated under this section."

The performance audit, also known as a management audit, for Akaku: Maui Community Television (Akaku) has been completed. This performance audit does not include the financial audit called for in the HRS.

We performed the performance audit for the period January 1, 2006 through June 30, 2011. This time frame was selected because if only one year is audited it would most likely give an inaccurate picture of the organization. At a minimum, three years of data should be analyzed but five or more years of data provides a more accurate picture when analyzing trends.

The performance audit objectives, scope, and methodology are detailed below:

Audit Objectives

The objectives of the performance audit were to:

- Assess the sufficiency of Akaku's organizational, planning, budget and operating documents

- Assess Akaku's compliance with applicable laws, regulations, and its contract with DCCA

- Document and report on selected operational and financial parameters

- Make recommendations as appropriate

[1] Hawaii Revised Statutes (HRS), codified as Chapter 440G §440G-8.3

Audit Scope

The scope of the performance audit covered:

- Organizational and governing documents currently in place
- Laws, regulations, and Decisions and Orders currently in force
- Operational and financial data for the last five years

Audit Methodology

Our audit was conducted between January and February 2012. We conducted interviews with Akaku personnel and representatives from the DCCA. We performed the majority of our procedures at Akaku's headquarters at its Kahului facility.

We obtained support to substantiate interviewees' statements. Audit procedures also included examination of pertinent policies and procedures, strategic and operating plans, reports, agreements, and other documents to assess adherence to those policies and procedures as well as adherence to various governing authorities. We also obtained and read the Board of Directors' minutes.

This audit was conducted in accordance with auditing standards generally accepted in the United States of America and the standards for performance 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 sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objects. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Auditor's Access to Information

At the onset of our audit we submitted an information request detailing the documents and other pertinent information we would require. We timely received that information in hard copy as well as by e-mail. Our performance audit was conducted with the full cooperation of all parties involved. We had unfettered access to all information we deemed necessary to conduct the performance audit.

Chapter 2

MANAGEMENT AND OVERSIGHT

Board of Directors, Management Team, and Oversight

Background

Since 1992, Akaku has provided PEG access for the County of Maui. Akaku's mission statement is:

- "Empowering the community's voice through access to media."

Findings

Board of Directors

In December 2006, Akaku amended its By-Laws to eliminate (1) the requirement that the Director of DCCA appoint six board of director members and (2) the authority of the Director of DCCA removal at any time, with cause, any member of the Board.

In May 2008, Akaku amended its By-Laws for committee changes and to add changes that are subject to technical errors that are not substantive in nature.

In June 2009, Akaku amended its By-Laws for clarifying vacancy appointments of directors and officers. The change allows a director or the President to fill a vacant staff officer position with the advice and counsel of the Executive Committee.

In March 2010, Akaku amended its By-Laws to change section 7.2 to allow the appointed President/CEO to be a voting member on the Executive Committee and add section 12.7 regarding guidelines for the handling of corporate records and outlining a retention and destruction policy of the organization.

Akaku's Board of Director Committees, have changed over the years. Since 2006, the standing committees included:

- Finance Committee;
- Development Committee;
- Program Committee; and the
- Personnel Committee.

In 2008, the standing committees changed to include the:

- Executive Committee;
- Audit Committee;
- Finance Committee; and the
- Planning and Policy Committee.

In 2010, the standing committees changed again to only include the:

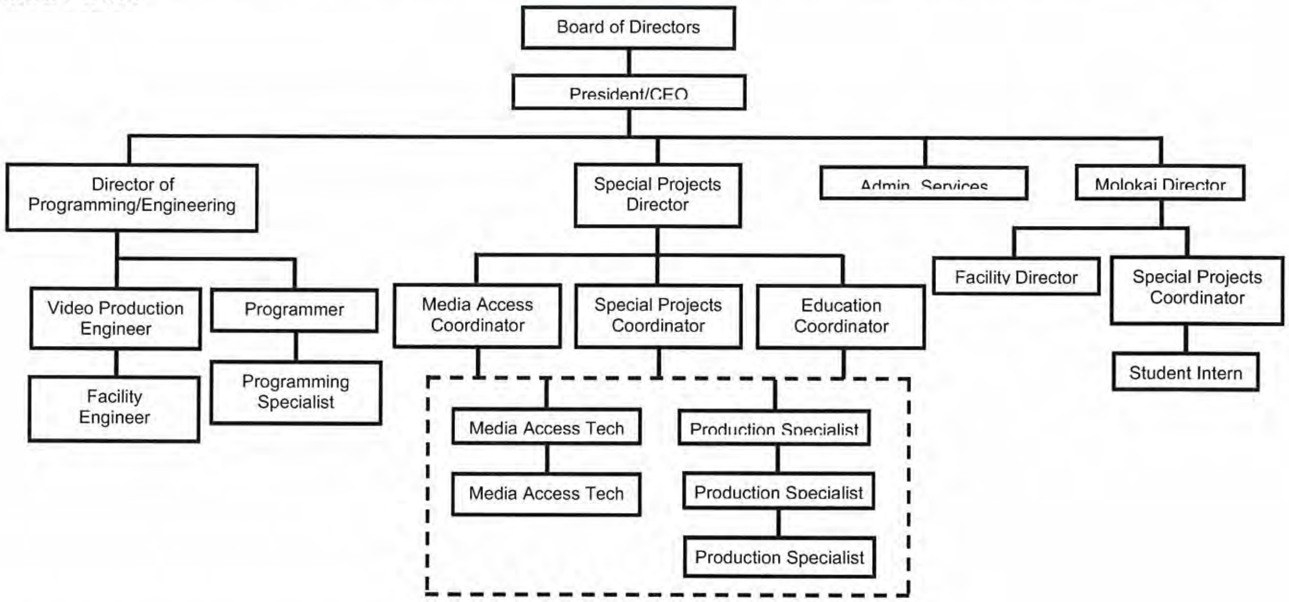
- Executive Committee;
- Audit Committee; and the
- Finance Committee.

The Executive Committee consists of the elected officers of the corporation and the appointed President/CEO who is a voting member of the Executive Committee. The Executive Committee is vested with administrative powers of the corporation and the Board of Directors during the interim between Board meetings. The Audit Committee is responsible for recommending an independent auditor and review of independent audits. The Finance Committee is responsible for all capital assets and other existing financial resources of the corporation and executive fiscal matters, including without limitation, procurement of facilities and equipment, care and maintenance of capital assets, allocation of assets, fiscal policy, preparation of the annual budget, investment management and financial oversight and reporting.

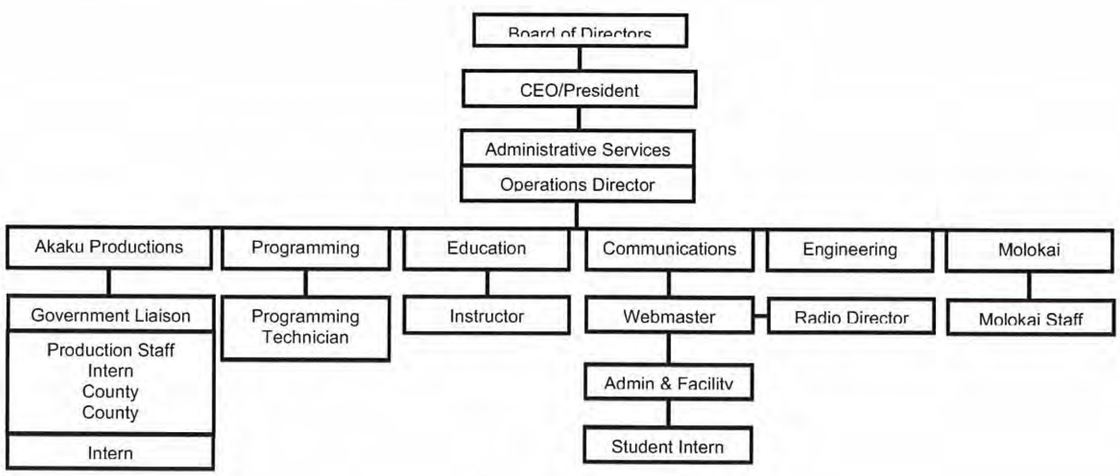
Akaku's Board of Directors meets at least six times a year and the Board Committees meet on a regular basis and/or as needed.

Management Team

In 2007, Akaku changed its organizational structure. Akaku's former organizational chart was:



The new organization chart is:



The changes to the organizational structure were the result of restructuring with a new President/CEO.

The personnel within Akaku have been relatively consistent during the period January 1, 2006 through June 30, 2011, although the titles and responsibilities may have changed.

One significant change during that time period occurred when the former President/CEO left Akaku in fiscal year 2007. The current President/CEO took over in January 2007.

Oversight

Akaku developed a "Strategic Plan 2002-2007", a "Strategic Plan" in May 2009, and held a Strategic Planning Retreat in February 2010 in which another "Strategic Plan" was developed that they are currently following.

Akaku also prepares an "Annual Report", as required by DCCA, that includes a quarterly analysis of programming hours for public, government and educational access channels, a summary of complaints, outreach and marketing efforts, and a summary of revenues for the fiscal year.

Subsequent Events

In March 2012, Akaku's Board of Directors convened a special meeting to engage in scenario planning with a trained facilitator and that the Board has constituted a Strategic Planning Committee, which is meeting to review the current strategic plan and consider revisions.

Comments/Recommendations

For the period from January 1, 2006 through June 30, 2011:

- Akaku maintained detailed meeting minutes that show the Board of Directors due diligence and governance of the organization.

- Akaku's management team appears to have the appropriate experience and knowledge for the size of the PEG.

- Akaku should develop a strategic plan, for a period not less than 3 years, which includes a detailed plan, measurable goals and triggers to implement the plan. The strategic plan should address the deficit spending discussed in Chapter 4 below.

Chapter 3

OPERATIONS

Operating Facilities

Background

Since its incorporation in 1992, Akaku has maintained as part of its stated core purpose the "preservation, development and enhancement of the diversity of thought, culture and heritage within Hawaii," and with that, the facilitation of "lifelong learning and the community's participation in the democratic process." From a planning point of view, the strategy of how to achieve this purpose for the future years should be contained in Akaku's strategic planning process, described in Chapter 2 of this report.

Findings

Operationally, Akaku has sought to achieve its purposes, and carry out its mission, through establishing a central operating facility in Kahului, a media center on Moloka'i, opening a new media center on Lana'i and getting involved in communities around the islands of Maui, Moloka'i and Lana'i. The President/CEO and staff of Akaku attend various community events throughout the year to build awareness about the organization, build relationships with residents, and provide coverage as requested.

Both the Kahului and Moloka'i facilities provide training for residents to become certified producers for access to Akaku facilities, equipment and assistance in producing. Akaku attempts to provide its services according to the specific character and needs of particular local communities on the island, considering its diversity of social cultures, political traditions, economic situations, and ethnic makeup.

Any member of the public or the representative of any social service agency may become trained in the use of production and editing equipment, and produce television programs intended for cable casting on local cable television channels. Government agencies may arrange for the use of Akaku staff and equipment to record legislative or other meetings for cable casting on cable channels.

Subsequent Events

In August 2011, Akaku opened a new media center location on Lana'i. This location offers camera and editing certification classes, computers for editing and equipment for rent to producers on the island.

Comments/Recommendations

- Building community involvement and awareness is what Akaku views as fulfilling the organization's core purpose.
- Akaku has adapted well to changing user needs and the opportunities for service brought about by the Internet.
- Akaku's success in building community awareness to meet the needs in Maui County which are informational and also social, is one of the positive marks of its particular character, and is arguably well in line with its mission and what Akaku sees as the organization's core purpose.
- Akaku should develop a marketing strategy to focus on drawing new residents in to use Akaku services and equipment.

Transition from Analog to Digital and High Definition

Background

Akaku has been working on the transition from analog to digital over the past four years. They began with the migration of replacing analog cameras to digital tape based cameras and have continually moved towards all digital tapeless production. Next Akaku plans to transition all post production to digital file formats, then fully transition studio production to all digital HD recording format, followed by all digital HD playback on the cable system and digital feeds for streaming, video-on-demand and social media. Akaku's distribution system is currently a standard definition digital encoder and playback for all three channels and they use a Grass Valley Indigo digital video switcher that records standard definition because Oceanic Time Warner only provides standard definition (analog) for Akaku channels.

Findings

The transition to digital has been a gradual migration. Within the last year Akaku has acquired three new fully digital, HD camera packages that record digital files to internal drives and/or flash memory. Akaku intends to completely replace all the camera packages with HD cameras that record digital files to drives or flash memory by the end of 2014. Akaku's Michael Clark Studio is equipped with three HD digital cameras and uses a Grass Valley Indigo digital video switcher which is capable of a high resolution output. The studio also has the capability for tapeless production; however Akaku plans to upgrade the switcher at the end of the year to a full HD/SDI switcher. As discussed above, Akaku's distribution system is currently a standard definition digital encoder and playback for all three channels, but Akaku plans to upgrade the playback and encode system to handle HD playback within the coming year.

Akaku is in the process of purchasing the equipment and positioning itself with the capability of transmitting video programming in digital and HD. However, it should be noted that in order for the transition to HD programming to become fully effective, it needs to be complemented by Oceanic Time Warner system upgrades to permit transporting HD signals between Akaku and the Oceanic headend. Per Akaku's staff, Oceanic has not indicated any time schedule for converting to HD.

Comment/Recommendations

- Akaku is in the process of making the transition from analog to digital and HD. Akaku has and will continue to purchase digital equipment that has the capability to convert digital to HD in the future. Although there is no timeline for the conversion to HD in Maui County, this places Akaku in a position to provide these services in the future, when necessary.

Metrics: The Measurement of Results

Background

Akaku has kept records of its activities since its inception. Measurement and reporting of results is an integral part of the management and operation of any organization. However, this process was sharpened when DCCA required Akaku, as part of its contract, to provide a specific set of reports (i.e. an Annual Activity Report, a Year-End Activity Report, and a monthly general ledger of professional expenditures). In accordance with this requirement, Akaku, among other efforts of accounting for its activities, has been keeping and annually reporting to DCCA detailed statistics on the following key elements of its operations:

- Total Hours of Programming: First Run, Repeat, and Submitted but Not Aired
- Programming by Origin: Locally Produced, Non-Locally Produced, and Bulletin Board
- Programming By Source: First Run Hours from PEG Sectors in the Categories of Dropped off for Play, PEG Trained and Certified Producers, and Hours Created by Akaku (Open Mic and Created by PEG)
- Video Production Training: All Locations
- Number of Students Trained and Certified as Producers: All Locations

Findings

As a result, it is possible to identify operating trends useful for Akaku management to know as well as for regulators and other stakeholders. For example, the following information on trends was constructed for analysis from some of the available statistics:

	2006	2007	2008	2009	2010	2011
Total Hours of Programming	41,538	39,516	39,982	40,576	40,210	40,897
Hours of Locally Produced Programming	16,917	14,898	18,600	18,820	17,668	18,718
Students trained in Akaku classes	637	858	305	551	605	2,717*

* In 2011 Akaku provided youth outreach training to students; therefore the number of students trained is significantly higher than previous years.

The reports provided to DCCA are based on the performance of Akaku as a whole. However, Akaku also provides selected separate reports on the Moloka'i location. Given that Akaku just opened a new location on Lana'i, it's a matter of interest how the new location performs individually as well.

We found Akaku's focus on metrics lies primarily on the reporting requirements to DCCA. The President/CEO has consistently tracked and monitored the quantitative data and presents it to the Board in a way that is aligned with Akaku's mission. However, Akaku should emphasize on setting goals and identifying measurable outcomes.

Comment/Recommendations

- Akaku has been successful in keeping and reporting statistics useful for both regulators and management in the past.
- As noted in Chapter 2, Akaku should develop a strategic plan, for a period not less than 3 years, which includes a detailed plan, measurable goals and triggers to implement the plan.

Chapter 4

FINANCIAL

This performance audit does not include a financial audit. A financial audit is the verification of the financial statements of an organization, with an expression of an audit opinion. This performance audit includes an analysis of Akaku's financial ratios and items identified by Akaku's independent external auditors and is not a verification of Akaku's financial statements.

Akaku's Financial Ratios

Background

Financial ratios are useful indicators of an organization's performance and financial health. Financial ratios can be used to analyze and to compare an organization's financials to those of similar organizations.

To be truly comparable, however, the organizations should be of similar size, age, located in the same area or locale, and have similar missions and programs. In the case of Akaku, there is a lack of organizations in the same locale of similar size and with similar programs. All four Hawaii PEGs differ in size and offer different programs. In addition, due to the widely varying situations of PEG organizations with respect to local needs, franchise requirements, levels of volunteer activity and other factors, there exists no set of standards for comparison of PEGs which is commonly accepted in the national PEG arena. Accordingly, the analysis conducted for this report will be limited to tracking Akaku's performance and financial position over time relative to itself. Accordingly, the ratios developed for Akaku include:

- Current Ratio

  The current ratio, also referred to as the working capital ratio, is current assets divided by current liabilities.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

  A high current ratio is of particular interest to creditors since it tends to reduce their risk. On the other hand, a high current ratio may indicate that an organization is either overfunded or that it is accumulating assets for future expansion.

- Quick Ratio

One drawback of the current ratio is that it includes inventory that may contain items that are used over several years or that are difficult to liquidate quickly or have uncertain liquidation values. The quick ratio is an alternative measure of liquidity that excludes inventory and prepaid expenses.

$$\text{Quick Ratio} = \frac{\text{Current Assets} - \text{Inventory} - \text{Prepaid Expenses}}{\text{Current Liabilities}}$$

Accordingly, the current assets used in the quick ratio are cash, investments, current accounts receivable, and current notes receivable. The quick ratio is also referred to as the acid test.

- Cash Ratio

The cash ratio is the most conservative of the liquidity ratios. It excludes all the current assets except the most liquid i.e. cash and cash equivalents, and investments (securities).

$$\text{Cash Ratio} = \frac{\text{Cash and Cash Equivalents} + \text{Investments}}{\text{Current Liabilities}}$$

The cash ratio is an indication of the organization's ability to pay off its current liabilities if for some reason immediate payment were demanded.

- Liquid Funds Indicator

The liquid funds indicator measures an organization's operating liquidity and is computed as follows:

$$\text{Liquid Funds Indicator} = \frac{(\text{Net Assets} - \text{Net Property and Equipment}) \times 12}{\text{Total Expenses}}$$

A high liquid funds indicator could point to lower cash funding urgency and excessive savings. A lowering of the liquid funds indicator over time is likely a sign of a planned capital equipment improvement program.

- Program Ratio

  The program ratio measures the relationship between direct program expenses and the organization's total expenses. Total expenses account for direct program expenses and management and general expenses (overhead).

  $$\text{Program Ratio} = \frac{\text{Program Services Expenses}}{\text{Total Expenses}}$$

  Younger organizations will likely have lower program ratios than more mature organizations as they set up the infrastructure to deliver their services. Over time, organizations should see increasingly higher program services ratios. If not, their overhead may need to be examined.

- Savings Ratio

  The savings ratio revels the rate of a nonprofit's cash and investments accumulation by measuring the relationship between savings (cash and cash equivalents, and investments balances) and total expenses.

  $$\text{Savings Ratio} = \frac{\text{Total Revenue} - \text{Total Expenses}}{\text{Total Expenses}}$$

  The savings ratio is an important factor in an organization's long term viability; high ratios may indicate excess funding. The savings ratio should be considered in conjunction with the liquid funds indicator. If the organization has low liquid funds indicator, a higher savings ratio would be desirable.

Most ratios by themselves are not particularly meaningful. They should be viewed as indicators, with several of them combined to paint a picture of an organization's situation. Ratios of non-profit organizations are, by their nature, typically limited to measures of liquidity, program expenditures, and overhead.

Findings

We have computed the ratios described above for Akaku's fiscal years ended June 30, 2006 through 2011. The results are presented in the table below.

	2006	2007	2008	2009	2010	2011
Current Ratio	2.8	3.0	1.8	0.9	0.4	0.8
Quick Ratio	2.8	3.0	1.7	0.8	0.4	0.7
Cash Ratio	1.7	1.8	1.2	0.5	0.4	0.7

Liquid Funds Indicator	8.1	5.3	1.8	-0.1	-1.7	-0.9
Program Ratio	0.8	0.8	0.8	0.8	0.8	0.8
Savings Ratio	-0.1	-0.1	-0.2	-0.1	-0.1	0.1

The first three ratios, the Current Ratio, Quick Ratio, and Cash Ratio, are known as liquidity ratios. Akaku's three liquidity ratios demonstrate a uniform pattern of decline from 2006 through 2010. The decline in the liquidity ratios is primarily due to the continual decrease in cash and cash equivalents. This reflects the organization's increase in use of funds on property and equipment and/or operating expenses. In 2011 these ratios increased, the increase shows some improvement.

The last three ratios, the Liquid Funds Indicator, Program Ratio, and Savings Ratio, are measures of Akaku's operating efficiency in terms of utilization of available resources to meet its perceived needs of the community as set out in its Mission Statement.

The liquid funds indicator shows continual decrease from 2006 through 2010 and a slight improvement in 2011. This is consistent with the pattern exhibited by the three liquidity ratios.
The program ratio has been relatively constant over the years. This indicates that Akaku has been able to hold general and administrative expenses from increasing in relation to total expenses.

The savings ratio presents some troubling trends from 2006 through 2010. In short, the organization is spending money at a faster rate than it is earning it. In 2011 the savings ratio increased, the increase shows some improvement.

<u>Comments/Recommendations</u>

- Akaku's financial metrics show a consistent pattern of use of available funds with improvement in 2011. The use of resources for services has exceeded the operating funds available for 2006 though 2010. This cannot continue for much longer and in 2011 Akaku shows some improvement. Going forward either its spending has to be brought in line with its available resources or the funding for the organization has to be increased. Akaku ratios show improvement in 2011 but the historical trends are concerning. In order to continue to improve these ratios Akaku needs to create and follow a strategic plan that includes ensuring expenses are in line with revenues and/or increase current revenues.

- Deficit spending is when the organizations revenues do not cover the expenses; therefore the excess spending is covered by cash and investments (i.e. Operating Reserve) or by borrowing. Short-term deficits can, but not always, represent an investment for future benefits, provided that there is an underlying plan or strategy. This does not appear the case for Akaku. Organizations cannot operate at a deficit for the long-term; they will eventually run out of Cash, Cash Equivalents and Investments. For 2006 through 2010 Akaku operated at a deficit. The only year included in this performance audit that did not have deficit spending was 2011.

- In order for Akaku to not fully deplete its Operating Reserve Akaku has to stop operating at a deficit. In 2011, Akaku did not operate at a deficit, but the historical trend of operating at a deficit from 2006 through 2010 are concerning. Akaku needs to ensure expenses are in line with revenues and/or increase current revenues or find new revenue sources (i.e. grants, fundraising, and fees). If Akaku does not continue to address this excessive spending the organization is in danger of depleting its reserves, and will be unable to sustain its operations at current levels.

- As noted in Chapter 2, Akaku should develop a strategic plan, for a period not less than 3 years, which includes a detailed plan on how use of funds will contribute to achieving those future goals.

Items Identified By Akaku's Independent External Auditors

Background

Independent external auditors who complete a financial statement audit consider the organization's internal control over financial reporting (internal control) as a basis for designing auditing procedures for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the organizations internal controls. These financial statement audits are not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore there can be no assurance that all such deficiencies have been identified.

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. The two reportable deficiencies include:

- A material weakness is a deficiency or 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.

External auditors of an entity's financial statements are required to document, in writing, if they identify internal control deficiencies that are considered material weaknesses or significant deficiencies. These reports are required by Statement on Auditing Standards 112 or Statement on Auditing Standards 115 (SAS 112/115).

If an independent external auditor identifies any internal control deficiencies that do not rise to the level of a material weakness or a significant deficiency, they may issue management advisory comments. These comments are typically made in writing to those charged with governance (i.e. Board of Directors). They generally include comments, suggestions and/or recommendations that strengthen internal controls and foster operating efficiencies.

Findings

For the period from January 1, 2006 through June 30, 2011 Akaku did not receive a SAS 112/115 report or management advisory comments.

Comments/Recommendations

- The audits for the fiscal years ended June 30, 2006 through June 30, 2011 did not identify any deficiencies in internal control or management advisory comments.

Chapter 5

COMPLIANCE

Analysis of Akaku's Compliance with Applicable Laws, Regulations, and its Contract with DCCA

Background

On June 17, 1999 Akaku entered into an agreement with the State of Hawaii through its DCCA. As part of the agreement, Akaku is responsible for the management and operations of the Maui County PEG access facilities and equipment including channels, facilities and equipment, training, marketing, support services, and insurance. On June 24, 2004, DCCA requested that the schedule of reporting be revised to provide for the annual activity and annual year end activity reports to be due at the same time within 60 days of the close of the reporting year. On April 13, 2006 DCCA required Akaku to submit monthly general ledger information on professional services expenditures.

In addition, Akaku is required to file reports with DCCA in order for DCCA to monitor Akaku's compliance with the provisions of the agreement. The reporting requirements for the period January 1, 2006 through June 30, 2011 are as follows:

1. Amendments to the articles of incorporation and by-laws no later than 30 days after approval by the board of directors.

2. A roster of the board of directors and officers and their respective term of office no later than 30 days after Akaku's annual meeting or no later than 30 days after a change in board membership when the change occurs other than at the annual meeting.

3. Annual financial statements no later than 90 days following the close of each calendar year.

4. Annual audited financial statements no later than 30 days after acceptance by the board of directors.

5. An annual operational plan and budget on or before June 1.

6. Akaku shall also develop and periodically update a strategic or long-range planning document for a period of not less than three years, and shall submit a copy of such document no later than 30 days after acceptance by the board of directors.

7. Complete equipment inventory upon execution of the Agreement, and thereafter an annual update on or before June 1 of each year.

8. An annual activity report, due no later than 60 days following the close of the reporting year, which shall include, but not limited to, the following information:

    a. Public Access Programming

    b. Governmental Programming

    c. Educational programming

    d. Summary of all channel outages from maintenance records including total hours and reasons therefore.

    e. Facility Use

    f. Training

    g. Summary of complaints including the nature of the complaints and the actions taken.

    h. Summary of outreach and marketing efforts.

    i. Summary of revenues from sources other than TWE Maui and TWE Hawaiian including the amounts, sources, and purpose of funds.

9. An annual year end activity report due no later than 60 days following the close of the reporting year.

10. A monthly general ledger report for professional services expenditures due by the fifteenth of the subsequent month.

Akaku is also required to designate one bank account for operations and another account for capital acquisitions (facilities and equipment). Akaku shall be responsible for administering the accounts, and shall not commingle operating funds with capital funds without prior written approval of the Director (DCCA).

Findings

As described in Chapter 1, Akaku's Board of Directors and their current and past management teams have taken their responsibility for the management and operations of the PEG access facilities and equipment including channels, facilities and equipment, training, marketing, support services, and insurance seriously.

Akaku's compliance with its reporting requirements for the period January 1, 2006 through June 30, 2011 is summarized in the below:

1. No amendments to the articles of incorporation were noted. Amendments to the by-laws appear to have been made in December 2006, May 2008, June 2009 and March 2010; however these were not submitted within 30 days after approval by the board of directors. The May 2008 amendment was submitted to DCCA 42 days after approval by the board of directors. MCO did not note approval of the changes to the By-Laws from May 2008 to June 2009; however a revised By-Laws was submitted to DCCA in June 2009. The March 2010 amendment was submitted to DCCA 47 days after approval by the board of directors.

2. Annual meetings appear to be held in October; however board rosters do not appear to be consistently submitted to DCCA within 30 days of the annual meetings. MCO also noted several instances where changes in board membership were made, during the period January 1, 2006 through June 30, 2011, and an updated roster of the Board of Directors and officers was not submitted to DCCA.

3. All the annual financial statements were submitted no later than 90 days following the close of each calendar year with the following exception:

    a. The 2010 annual financial statements were not submitted to DCCA.

4. All of the annual audited financial statements were submitted no later than 30 days after acceptance by the board of directors with the following exceptions:

    a. The 2009 annual audited financial statements were approved on November 13, 2009 but were submitted late on January 28, 2010.
    b. The 2010 annual audited financial statements were approved on October 15, 2010 but were submitted late on October 25, 2011.

5. All of the annual operational plans and budgets were submitted on or before June 1 with the following exceptions:

    a. The 2006, 2007 and 2011 annual operational plans and budgets were submitted late on August 31, 2006, June 29, 2007, and June 2, 2011, respectively.

6. The board of directors approved and submitted period strategic or long-range planning documents during the period. However, strategic plans submitted for 2010 and 2009 did not cover a period of three years or more.

7. All of the equipment inventories were submitted on or before June 1 with the following exception:

   a. The 2006, 2007 and 2011 annual equipment inventories were submitted late on August 31, 2006, July 5, 2007, and June 2, 2011, respectively.

8. All of the annual activity reports were submitted within 60 days following the close of the reporting year with the following exception:
   a. The 2008 annual activity report was submitted was submitted 2 days late.

9. All of the annual year end activity reports were within 60 days following the close of the reporting year.
   a. The 2008 annual activity report was submitted was submitted 2 days late.

10. MCO noted several instances where the monthly general ledger report for professional services expenditures was not submitted to DCCA by the fifteenth of each month.

Akaku maintained separate bank accounts for the operating funds and the capital funds for the period January 1, 2006 through June 30, 2011. However, until July 2009 Akaku had not been properly using their capital account to make payments for capital purchases. Prior to July 2009 capital purchases appear to have been paid for out of the operating account and funds were being transferred out of the capital account to the operating account. After July 2009, capital purchases appear to be appropriately paid out of the capital account. It appears that Akaku jeopardized the contract with DCCA by not properly maintaining the separate bank accounts.

During the performance audit nothing came to our attention to suggest that there were any other instances of non-compliance with laws or regulations.

Subsequent Events

Per the August 24, 2011 letter from DCCA, Akaku is no longer required to submit a monthly general ledger report for professional services expenditures.

Comments/Recommendations

- It appears that Akaku is making a conscious effort to meet its reporting deadlines outlined in its June 17, 1999 agreement with DCCA and the June 24, 2004 and April 13, 2006 letters from DCCA. However Akaku should implement a tickler system on their calendars to notify them of reporting deadlines to ensure reports are timely submitted to DCCA.

- Akaku should implement controls to ensure the operations and capital accounts are properly maintained and are not commingled without prior written approval from DCCA. Not properly maintaining separate accounts could jeopardize Akaku's contract with DCCA.

- As noted in Chapter 2, Akaku should develop a strategic plan, for a period not less than 3 years, which includes a detailed plan, measurable goals and triggers to implement the plan.