



# **OFFICE OF THE CITY AUDITOR**

City and County of Honolulu  
State of Hawai'i

## **Financial Audit of the City and County of Honolulu, State of Hawai'i**

For the Fiscal Year Ended  
June 30, 2014

Management Letter





A Hawaii Limited Liability Partnership

February 27, 2015

The Chair and Members of the City Council  
City and County of Honolulu:

Under auditing standards generally accepted in the United States, auditors are encouraged to report various matters concerning internal control noted during an audit, and are required to report certain of those matters. Matters that are required to be reported are “significant deficiencies in the design or operation of internal control, which could adversely affect the organization’s ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements.”

As part of our audit of the basic financial statements of the City and County of Honolulu (the City), for the year ended June 30, 2014, we considered the City’s internal control, but only to the extent we felt necessary for the purpose of providing a basis for reliance thereon in determining the nature, timing and extent of the audit tests applied in connection with our audit.

Our consideration of internal control did not entail a detailed study and evaluation of any of its elements and was not made for the purpose of making detailed recommendations or evaluating the adequacy of internal control to prevent or detect errors and fraud. In this regard, it should be recognized that, because of inherent limitations in any internal control, errors or fraud may occur and not be detected. Furthermore, projection of any evaluation of internal control to future periods is subject to the risk it may become inadequate because of changes in conditions or deterioration in its operating effectiveness.

While the purpose of our consideration of internal control was not to provide assurances thereon, certain matters came to our attention that we want to report to you. These matters, which were considered by us during our audit and do not modify the opinions expressed in our auditor’s report dated December 23, 2014, and along with our recommendations, are described in the accompanying memorandum.

We wish to express our appreciation for the courtesies and cooperation extended to our staff. We would be pleased to discuss these recommendations in greater detail or otherwise assist in their implementation.

*KMH LLP*

KMH LLP

Honolulu, Hawaii

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# City and County of Honolulu State of Hawaii

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## Current Year Comments

### Financial Statements:

#### **2014-01 Deferred Inflows or Outflows of Resources Related to Advance Refunding of Bonds**

In fiscal year 2013, the City issued General Obligation Bond series 2012. Certain proceeds from General Obligation Bond series 2012 were used to advance refund a portion of previously issued General Obligation Bond series. During the audit, we noted the calculation of the deferred outflow of resources related to the advance refunding was not calculated in accordance with GASB No. 7. The erroneous calculation resulted in a current year misclassification between deferred outflows and long-term liabilities of approximately \$15.7 million. Further, due to the errant calculation of the deferred outflow of resources, current year interest expense related to deferred outflows was misstated by approximately \$3.2 million.

**Recommendation:** We recommend that the City be more diligent in its calculation of any deferred inflows or outflows of resources related to advance refunding in accordance with GASB No. 7.

#### **2014-02 Sewer Fund Inventory**

The City's Sewer Fund inventory records are maintained by the City's Department of Environmental Services (ENV). Based on certain parameters requested by ENV, the IT department runs a query from the inventory system detailing the inventory existing at year end. This inventory report is utilized by the City's accounting department to record the inventory held by the Sewer Fund at year end.

During the audit, we noted that the query used by the ENV department did not properly exclude transactions related to the subsequent fiscal year.

**Recommendation:** Although the resulting difference of approximately \$146,000 was not significant, management should review the parameters of its inventory reports to avoid future errors.

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**2014-03 Public Transportation System – Deferred Revenue**

During the audit, we noted that Public Transportation System (PTS) management did not perform a reconciliation or analysis on the outstanding deferred revenue balances.

We informed PTS management of this deficiency and after management’s further analysis of the outstanding deferred revenue balance; management provided a post-closing adjustment of approximately \$580,000 to properly state the deferred revenue balance.

**Recommendation:** We recommend that PTS establish procedures to reconcile and analyze the deferred revenue balances periodically.

Federal Grant Programs:

*Housing Voucher Cluster*

**2014-04 Eligibility**

During our testing of the eligibility requirements of the Housing Voucher Cluster program, we noted the following:

- 1) In accordance with 24 CFR Section 5.508(b), “Each family member, regardless of age, must submit the following evidence to the responsible entity: For U.S. citizens or U.S. nationals, the evidence consists of a signed declaration of U.S. citizenship or U.S. nationality.”
  - For 2 out of 60 tenant files tested, we noted that a declaration of citizenship form was missing.
- 2) In accordance with the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement for the Housing Voucher Cluster (CFDA No. 14.871, 14.879), the City must obtain and document in the family file third-party verification of: (1) reported family annual income; (2) the value of assets; (3) expenses related to deductions from annual income; and (4) other factors that affect the determination of adjusted income or income-based rent for both family income examinations and reexaminations.
  - For 1 out of 60 tenant files tested, we noted that the annual income was inadequately documented as there was a lack of documentation of termination of employment.
  - For 2 out of 60 tenant files tested, we noted that the asset verification was incorrectly reported on the HUD-50058 form.

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- 3) In accordance with the OMB Circular A-133 Compliance Supplement for the Housing Voucher Cluster (CFDA No. 14.871, 14.879), the City must determine income eligibility and calculate the tenant's rent payment using the documentation from third-party verification in accordance with 24 CFR part 5 subpart F.
  - For 5 out of 60 tenant files tested, we noted that HAP was incorrectly calculated.

**Recommendation:** We recommend that the City be more diligent in performing such procedures and continue to enforce the quality control review of tenant files. Such a quality control review could identify areas requiring more attention by management and ultimately reduce the number of errors.

## 2014-05 Reporting - Special Reporting

During our testing of the reporting (special reporting) requirements of the Housing Voucher Cluster program, we noted the following:

- 1) In accordance with the OMB Circular A-133 Compliance Supplement for the Housing Voucher Cluster (CFDA No. 14.871, 14.879), the City is required to submit the HUD-50058, *Family Report*, electronically to the United States Department of Housing and Urban Development, with several line items indicating critical information.
  - For 3 out of 60 tenant files tested, we noted that the incorrect date of birth was indicated on the HUD-50058 form.
  - For 1 out of 60 tenant files tested, we noted that the asset verification was incorrectly reported on the HUD-50058 form.
  - For 3 out of 60 tenant files tested, we noted that HAP was incorrectly calculated and reported due to incorrect gross income calculations.

**Recommendation:** We recommend that the City be more diligent in performing such procedures and continue to enforce the quality control review of tenant files. Such a quality control review could identify areas requiring more attention by management and ultimately reduce the number of errors.

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## 2014-06 Special Test - Housing Assistance Payment

During our testing of the special test (housing assistance payment) requirements of the Housing Voucher Cluster program, we noted the following:

- 1) In accordance with the OMB Circular A-133 Compliance Supplement for the Housing Voucher Cluster (CFDA No. 14.871, 14.879), the City should verify that the HAP contracts or contract amendments agree with the amount recorded on the HAP register and the amount on line 12u of the HUD-50058 form.
  - For 5 out of 60 tenant files tested, we noted that HAP was incorrectly calculated and paid to tenants.

**Recommendation:** We recommend that the City be more diligent in performing such procedures and continue to enforce the quality control review of tenant files. Such a quality control review could identify areas requiring more attention by management and ultimately reduce the number of errors.

## *Community Development Block Grants (Entitlement Grants) Cluster*

### 2014-07 Subrecipient Monitoring

During our testing of the subrecipient monitoring requirements of the Community Development Block Grant (“CDBG”) program, we noted that the “Monitoring Risk Analysis” schedule was not updated for fiscal year 2014. This schedule is utilized as a risk analysis that the City and County of Honolulu Department of Community Services (“DCS”) uses to determine high-risk subrecipients subject to on site monitoring.

**Recommendation:** We recommend that the City’s DCS implement procedures to ensure that the “Monitoring Risk Analysis” schedule is updated at the beginning of each fiscal year and procedures are performed to ensure on-going monitoring occurs.

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## Status of Prior Year Comments

### 2013-01 Accounting for Capital Assets

During our testing of the City's governmental activities capital assets as of June 30, 2013, we noted the following issues:

- Two capital assets totaling \$113.5 million were misclassified as infrastructure rather than buildings and improvements in fiscal year 2012. The City reclassified these capital assets in fiscal year 2013. The cause of this error was due to a lack of proper review by City personnel prior to the capital assets being transferred out of construction work-in-progress.
- Approximately \$25.3 million of capital assets written off in the current year should have been expensed prior to fiscal year 2013. The cause of this error was due to untimely reviews and follow-up with the appropriate project managers to determine that the capital assets should have been written off in prior years.
- Approximately \$6.7 million of capital assets were improperly expensed in the current year rather than being capitalized. The cause of this error was due to untimely reviews and follow-up. The City was also unable to reconcile \$1.4 million in the reconciliation of the governmental funds of capital outlays as expenditures to the change in net position of governmental activities.

**Status:** Unresolved. See current year finding 2014-5 in the Single Audit Reports.

### 2013-02 Subrecipient Monitoring and Eligibility

During our testing of the Shelter Plus Care program, we noted the following issues:

- No site visit was performed for one subrecipient during fiscal year 2013. Per the Office of Management and Budget Circular A-133 Compliance Supplement, Part 3 for Subrecipient Monitoring, During-the-Award Monitoring, "the program should monitor the subrecipient's use of Federal awards through reporting, site visits, regular contact or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations and the provisions of contracts or grant agreements and that performance goals are achieved."
- Two out of 19 participant files that we tested did not include a final approval signature by the Housing Program Director.



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- Two out of 20 participant files that we tested were missing a current Housing Assistance Payment (“HAP”) contract that should be executed annually by the participant, the program staff, and the landlord. The HAP contract indicates the participant’s portion of rent owed and the portion the program is responsible to pay on behalf of the participant.

**Status:** Resolved. No similar instances were noted in the current year.

### **2013-03 Matching**

During our testing of the Shelter Plus Care program, we noted that the Adult Mental Health Division (“AMHD”) match amount included in the Annual Progress Report (“APR”) did not agree to the City’s calculation by approximately \$141,000, due to incorrect estimates by AMHD.

Per 24 Code of Federal Regulations section 582.110(c), a grantee must provide or ensure the provision of supportive services are at least equal in value to the aggregate amount of rental assistance funded by the Department of Housing and Urban Development (“HUD”).

**Status:** Resolved. No similar instances were noted in the current year.

### **2013-04 Subrecipient Monitoring**

During our testing of the subrecipient monitoring requirements of the Community Development Block Grant (“CDBG”) program, we noted that the “Monitoring Risk Analysis” schedule was not updated for fiscal year 2013. This schedule is utilized as a risk analysis that the City and County of Honolulu Department of Community Services (“DCS”) uses to determine high-risk subrecipients subject to on site monitoring.

We were informed that the cause of this control deficiency was a lack of knowledge of proper procedures by the Acting Director of DCS.

**Status:** Unresolved. No changes were noted in the current year. See current year comment 2014-07.

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**2013-05 Procurement**

During the Federal Transit Authority procurement testing for Oahu Transit Services (“OTS”), we noted there was no sign-in sheet with names and addresses of required witnesses at a bid opening.

Per Hawaii Administrative Rules 2-122-30a, the name(s) and address(es) of the required witnesses shall be recorded at the time of the bid opening.

**Status:** Resolved. No similar instances were noted in the current year.

DEPARTMENT OF BUDGET AND FISCAL SERVICES  
**CITY AND COUNTY OF HONOLULU**  
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KIRK CALDWELL  
MAYOR



NELSON H. KOYANAGI, JR.  
DIRECTOR

GARY T. KUOKAWA  
DEPUTY DIRECTOR

February 27, 2015

Mr. Edwin Young  
Office of the City Auditor  
1001 Kamokila Blvd., Suite 216  
Kapolei, Hawaii 96707

Dear Mr. Young:

SUBJECT: Management Advisory Report for the Fiscal Year Ended June 30, 2014

Enclosed is the response to the recommendations included in KMH LLP's preliminary draft of the management advisory report resulting from the audit of the City and County of Honolulu for the fiscal year ended June 30, 2014. The response includes actions taken or contemplated, anticipated completion dates, and the City personnel responsible for the corrective action.

Sincerely,

A handwritten signature in black ink, appearing to read "Nelson H. Koyanagi, Jr.", is written over a horizontal line.

Nelson H. Koyanagi, Jr., Director  
Budget and Fiscal Services

Enclosures

APPROVED:

A handwritten signature in blue ink, appearing to read "Roy K. Amemiya, Jr.", is written over a horizontal line.

Roy K. Amemiya, Jr.  
Managing Director

**RESPONSE TO MANAGEMENT ADVISORY REPORT  
COMMENTS AND RECOMMENDATIONS  
Year Ended June 30, 2014**

**CURRENT YEAR COMMENTS AND RECOMMENDATIONS**

**Comment No. 2014-01: Deferred Inflows or Outflows of Resources Related to Advance Refunding of Bonds**

Audit Recommendation: We recommend that the City be more diligent in its calculation of any deferred inflows or outflows of resources related to advance refunding in accordance with GASB No. 7.

Administration's Comment: Upon the issuance of advance refunding bonds, the unamortized bond premium or discount pertaining to the refunded bonds will be classified as deferred inflows or outflows of resources in accordance with Governmental Accounting Standards Board (GASB) Statement No. 65 and will be amortized in accordance with GASB Statement No. 7.

Anticipated Completion Date: September 2014 for fiscal year 2014, and by June of each year whenever applicable

Contact Person(s): Danilo Maximo, Accountant V, Department of Budget and Fiscal Services

**Comment No. 2014-02: Sewer Fund Inventory**

Audit Recommendation: Although the resulting difference of approximately \$146,000 was not significant, management should review the parameters of its inventory reports to avoid future errors.

Administration's Comment: The Department of Environmental Services staff has reviewed the parameters of the inventory report and made corrections to the parameters to insure that future reports are correct.

Anticipated Completion Date: February 2015

Contact Person(s): John Pedersen, Data Processing Systems Analyst, Department of Environmental Services

**Comment No. 2014-03: Public Transportation System – Deferred Revenue**

Audit Recommendation: We recommend that PTS establish procedures to reconcile and analyze deferred revenue balances periodically.

Administration's Comment: Procedures have been established to analyze the deferred revenue balance on an annual basis and to make adjustments as deemed necessary.

Anticipated Completion Date: December 2014

Contact Person(s): Melvin Higa, Controller, Oahu Transit Services  
Jenny Lemaota, Vice President of Finance, Oahu Transit Services

## RESPONSE TO MANAGEMENT ADVISORY REPORT

### COMMENTS AND RECOMMENDATIONS

Year Ended June 30, 2014

#### **Comment No. 2014-04, 2013-02 and 2010-06: Eligibility**

Audit Recommendation: We recommend that the City be more diligent in performing such procedures and continue to enforce the quality control review of tenant files. Such a quality control review could identify areas requiring more attention by management and ultimately reduce the number of errors.

#### **Comment No. 2014-05: Reporting – Special Reporting**

Audit Recommendation: We recommend that the City be more diligent in performing such procedures and continue to enforce the quality control review of tenant files. Such a quality control review could identify areas requiring more attention by management and ultimately reduce the number of errors.

#### **Comment No. 2014-06: Special Test – Housing Assistance Payment**

Audit Recommendation: We recommend that the City be more diligent in performing such procedures and continue to enforce the quality control review of tenant files. Such a quality control review could identify areas requiring more attention by management and ultimately reduce the number of errors.

Administration's Comment for No. 2014-04, 2014-05 and 2014-06: Program supervisors currently conduct quality control reviews as required for the Section 8 Management Assessment Program pursuant to 24 CFR 985.2. Supervisors will be monitored each month to ensure the reviews are completed and the errors discussed with staff. In addition, supervisors will conduct an in-house retraining session on the annual reexamination checklist and calculation procedures. The staff will continue to participate in periodic training sessions from the technical assistance provider.

Anticipated Completion Date: June 2015

Contact Person(s): Jayne Lee, Section 8 Administrator, Department of Community Services

#### **Comment No. 2014-07 and 2013-04: Subrecipient Monitoring**

Audit Recommendation: We recommend that the City's DCS implement procedures to ensure that the "Monitoring Risk Analysis" schedule is updated at the beginning of each fiscal year and procedures are performed to ensure on-going monitoring occurs.

Administration's Comment: As required by the U.S. Department of Housing and Urban Development in 2013, the City participated in the Technical Assistance (TA) program. The program's work plan dated May 2013 – February 2014 included a task the TA team was to complete, that is, to work with the Grantee to develop new monitoring procedures and tools for CDBG funded activities. In December 2013, the TA team again reiterated its intent to work with the City to develop new monitoring procedures and tools such as workflow charts and checklists for use by City staff. The TA team's help in developing City monitoring procedures and tools amounted to the delivery in August 2014 of the subrecipient monitoring plan for a county in Texas which City staff did not find useful or timely. As a result, the City returned to its existing monitoring practices which is more pertinent to its locale.

Anticipated Completion Date: February 2015 for the risk analysis with updates prepared annually beginning in July 2015, and March 2015 for the commencement of monitoring of open projects

Contact Person(s): Keith Ishida, Administrator, Department of Community Services