



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, 2005

Management Letter

Conducted by
Nishihama & Kishida, CPA's, Inc.

CITY AND COUNTY OF HONOLULU
MANAGEMENT ADVISORY REPORT
Fiscal Year Ended June 30, 2005

CITY AND COUNTY OF HONOLULU

TABLE OF CONTENTS

	<u>Page</u>
MANAGEMENT ADVISORY REPORT	
Management Letter	3
 CURRENT FINDINGS AND RECOMMENDATIONS	
05-1 Demonstrate Financial Assurance For Landfill Postclosure Care Costs Under State Approved Mechanism	4 - 5
05-2 Continue Risk-Based Monitoring of Section 8 Housing Choice Voucher Program	5 - 6
05-3 Improve Documentation Of Subrecipient Monitoring	6 - 7
 STATUS OR PRIOR YEAR'S RECOMMENDATIONS	
Status Report	8 - 12
 CORRECTIVE ACTION PLAN	
Response of the City and County of Honolulu	14 - 18



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CERTIFIED PUBLIC ACCOUNTANTS

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To the Chair and Members of the City Council
City and County of Honolulu
Honolulu, Hawaii

In planning and performing our audit of the financial statements of the City and County of Honolulu, State of Hawaii (City) for the fiscal year ended June 30, 2005, we considered the City's internal control to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on internal control.

However, during our audit, we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The comments that accompany this report summarize our findings and recommendations regarding these matters. This letter does not affect our report dated November 30, 2005, on the financial statements of the City.

Nishihama & Kishida, CPA's, Inc.

Honolulu, Hawaii
November 30, 2005

CURRENT FINDINGS AND RECOMMENDATIONS

05-1 Demonstrate Financial Assurance for Landfill Postclosure Care Costs Under State Approved Mechanism

The City did not adequately demonstrate financial assurance for the costs of postclosure care of the Waipahu and Kapaa municipal solid waste landfills (MSWLF) that have been closed and no longer operating as required by Section 11-58.1-18(c) of the Hawaii Administrative Rules.

Section 11-58.1-18(c) of the Hawaii Administrative Rules states in part, "The owner or operator of each MSWLF unit must establish, in a manner in accordance with subsection (e), financial assurance for the costs of post-closure care as required.... The owner or operator must provide continuous coverage for postclosure care until released from financial assurance" Financial assurance must be provided until the State of Hawaii's Department of Health verifies that post-closure care which usually lasts for 30 years has been completed in accordance with the post-closure plan.

Subsection (e) describes the allowable mechanisms used to demonstrate financial assurance which includes establishing a trust fund, obtaining surety bond guaranteeing payment or performance of postclosure care, obtaining letter of credit, obtaining insurance, or other mechanism approved by the State of Hawaii's Department of Health.

The City proposed to the State of Hawaii a mechanism modeled after the local government financial test provided by federal regulations. The City has not received approval from the State of Hawaii to date.

The local government financial test requires certain documentation that demonstrates the government's financial strength at the close of each year. Financial assurance items under the local government financial test must be updated and in place within 180 days following the close of the government's fiscal year.

The City demonstrated financial assurance under the local government financial test for the fiscal year ended June 30, 1996 but since then has not documented the required update for financial assurance.

Upon our notification that the City needed to obtain approval of its financial assurance mechanism and document financial assurance, the City took steps in reactivating the process of obtaining the necessary approval and preparing the necessary documentation for the fiscal year ended June 30, 2005.

Recommendation

The City should obtain approval of its landfill financial assurance mechanism from the State of Hawaii' Department of Health and ensure that it demonstrates financial assurance for postclosure costs for the Waipahu and Kapaa landfills by 180 days after the end of each fiscal year until released of the responsibility as provided by state and federal laws.

05-2 Continue Risk-Based Monitoring of Section 8 Housing Choice Voucher Program

During our testing of the Section 8 Housing Choice Voucher Program, we noted 2 instances out of 40 items tested, in which the City's calculation of the total tenant payment (TTP) and the housing assistance payment (HAP) applicable to program participants were erroneously calculated. The first error was the result of a mathematical error that was made during the calculation of the subsidy. The second error occurred due to the use of an outdated payment standard.

We also noted 2 instances out of 40 items tested, in which adequate documentation was not maintained in the tenant file to support the City's eligibility determination. Specifically, sufficient documentation was not maintained to support whether the program participant met the definition of a "family" and whether the participant qualified for eligible immigrant status.

The City's current internal control structure places a significant degree of reliance on the work performed by its Housing Assistance Specialists (HAS). In addition to other duties, the HAS are responsible for the eligibility determination of the Section 8 Housing Choice Voucher Program participants and the calculation of the TTP and HAP. However, the work performed by the HAS are not reviewed by their supervisors on a daily basis.

Review procedures are an important component of an effective internal control structure. Due to the large volume of individuals that a HAS is assigned, it is critical that each HAS be made aware, in a timely manner, of any mistakes that he/she is making. This is especially true for any misinterpretations of program requirements. This would reduce the likelihood that a similar error will be made in the future.

In September 2004, the City implemented procedures to address the need for the timely review of the work performed by all HAS. On a monthly basis, a sample of participant files are reviewed by HAS supervisors to ensure compliance with program requirements. The City's objective is to review approximately 10% of all

participant files over the course of a year, with representation of all HAS. Despite the implementation of these procedures, errors continued to occur during the fiscal year ended June 30, 2005. As a result, the City revised its procedures, effective September 2005, by placing additional emphasis on those individuals who appear to be susceptible to making errors and who would therefore benefit from additional monitoring and training. The City continues to conduct the 10% minimum quality review of its case files annually with representation of all HAS.

Recommendation

The City should continue its effort in performing on-going quality control reviews of the Section 8 Housing Choice Voucher Program. The City should put an emphasis on identifying personnel who are more prone to errors in order to assist them in addressing the problem.

05-3 Improve Documentation of Subrecipient Monitoring

The City serves as the pass-through entity of federal awards to various subrecipients and is therefore responsible for ensuring that all of its subrecipients are complying with the applicable federal rules and regulations. During 2005, the City passed-through approximately \$21,880,000 in federal awards to its subrecipients.

The majority of these pass-through awards are administered by the City's Department of Community Services (DCS). Due to a limited number of available staff, DCS is unable to perform on-site monitoring for all of its subrecipients. As a result, it is necessary for the City to perform other forms of during-the-award monitoring in order to ensure that the City's subrecipients are complying with the applicable program guidelines. These procedures include regular contact, through telephone conversations or email correspondence, and the review of financial and performance reports submitted by the subrecipients. However, during our testing, we noted several instances where the City did not have adequate documentation regarding its review of financial reports submitted by its subrecipients.

Specifically, we noted 5 instances out of 25 items tested, in which the City did not have sufficient documentation of correspondence with subrecipients regarding findings noted in the subrecipients' audited financial statements. We also noted 3 instances out of 25 items tested, in which the City's subrecipient file was either missing the subrecipient's most recently issued audited financial statements or the financial statements in the file did not appear to be complete.

Federal subrecipient monitoring requirements call for the pass-through entity to review audit reports from subrecipients required to have an audit in accordance with OMB Circular A-133, *Audits of States, Local Governments and Non-profit Organizations*. Pass-through entities are also required to issue timely decisions on any findings noted and to ensure that subrecipients take timely corrective action on any deficiencies identified.

Our understanding is that the DCS generally handles any findings noted through verbal communication with its subrecipients if the finding is not directly related to federal funding passed through from the City. In instances where the findings would have a direct bearing on the implementation of a federally funded project, it is the policy of the DCS to write to the subrecipient to follow up on the status of the finding and the time frame in which the finding will be resolved.

Although policies exist to address the federal subrecipient monitoring requirement, it is important that the policies be designed in a manner that will eliminate, as much as possible, the need for a subjective interpretation regarding those findings that should be documented in writing and those that can be handled verbally. This would reduce the risk of personnel not adequately documenting their follow up with subrecipients due to the misinterpretation of the applicability of a particular finding to a federally funded project.

Recommendation

The City should implement procedures to adequately document correspondence with its subrecipients regarding all findings that were noted during the City's review of its subrecipients' audited financial statements. This includes the City's decision on any audit findings noted and the corrective action taken by its subrecipients. If a finding noted during the City's review is determined to be not applicable to the City-funded project and therefore no further follow up is deemed necessary, that fact should be documented as well as the rationale that supports this determination.

STATUS REPORT

This section contains the current status of the prior auditor's recommendations. The recommendations are referenced to the pages of their management letter report for the fiscal year ended June 30, 2004, dated December 23, 2004.

Recommendations	Status
04-1 Rental Integrity Monitoring of Section 8 Housing Choice Voucher Program (page 1)	
The City should resolve the following findings and observations related to an issued report from the Office of Public Housing dated September 3, 2004:	Accomplished. Pursuant to a letter from the U.S. Housing and Urban Development (HUD) to the City dated June 1, 2005, HUD has determined this finding to be closed.
<ol style="list-style-type: none">1. The City did not properly calculate income, social security benefits, interest earned from assets and medical deductions that resulted in an overpayment or underpayment of housing assistance payments or tenant rent.2. The City had improperly transferred data from the tenant file to the HUD-50059, Family Report, and to the Multifamily Tenant Characteristics System.3. The City has not utilized the Quality Control Plan to monitor program compliance in tenant files.4. Certain files were missing birth certificates, missing signatures on the HUD-9886 form and missing documents to verify the U.S. citizenship of a head of household.	

04-2 Findings Based on Federal Agency's On-Site Review (pages 1 - 2)

The City should resolve the following findings related to an issued report from the FTA dated September 30, 2003:

1. Technical - The City did not consistently update milestones or provide reasons why milestones were not met on its Milestone Progress Reports (MPRs). Additionally, the City did not notify FTA of all change orders in excess of \$100,000 on its MPRs during the review period.
2. Satisfactory Continuing Control - The City was unable to document that it had ever sought or received FTA approval to lease a portion of the Kalihi-Palama bus facility to the Oahu Transit Services Credit Union. The FTA also noted that the City must re-evaluate its active fleet size of buses to comply with FTA guidelines for spare ratio.
3. Disadvantaged Business Enterprise (DBE) - The City did not monitor its contractors to ensure that DBE obligations are fulfilled.
4. Buy America - The City did not perform separate pre-award and post-delivery Buy America audits and certifications related to two option orders under a single bus procurement.
5. Title VI - Several of the City's service standards and policies were not quantifiable or sufficient for assessing the Title VI compliance. The City has not performed any compliance assessments in the past four years pursuant to FTA Circular 4702.1.

Accomplished. Pursuant to a letter from the Federal Transit Administration (FTA) to the City dated March 18, 2005, FTA has determined the findings stated in the fiscal year 2003 Triennial Review Report to be closed.

Recommendations

Status

04-2 Findings Based on Federal Agency's On-site Review (pages 1 - 2)

6. Americans with Disabilities Act (ADA) - Some of the City's ADA policies and procedures for FTA funded services did not meet ADA requirements.
7. Drug and Alcohol Program - The City was unable to document that the private operator of a City trolley service had a Drug and Alcohol Policy/Program for its safety-sensitive employees that conformed to FTA regulations.

04-3 Late Filings of Federal Report (page 2)

To comply with federal regulations, the City should establish procedures to ensure that the Report of Disadvantaged Business Enterprise (DBE) Awards and Commitments is completed and filed timely.

Not accomplished. The City filed the September 30, 2004 Report of Disadvantaged Business Enterprises Awards and Commitments on March 31, 2005, rather than on the required date of December 1, 2005. Due to an oversight, the March 31, 2005 report has not been filed. We were informed that the City has been unable to file the required report in a timely manner due to a lack of adequate staff.

04-4 Section 8 Housing Choice Vouchers Could Not Be Located (page 3)

To ensure that proper documentation is maintained in tenant's files related to the tenant's current housing assistance, the City should include the housing choice vouchers related to the tenant's current rental agreement.

Accomplished. Pursuant to a letter from HUD to the City dated June 1, 2005, HUD has determined this finding to be closed.

04-5 Bank Reconciliations Should Be Improved (page 3)

To ensure bank reconciliations are properly and timely prepared, the City should exclude items that cancel each other out as reconciling items on the bank reconciliations. A supervisor should carefully review the bank reconciliations.

Not accomplished. Bank reconciliations prepared during the fiscal year ended June 30, 2005 continued to include items that canceled each other out.

Recommendations	Status
<p>03-1 Lack of Monitoring of Subrecipient Loans (page 5)</p>	<p>Accomplished. The City has established post-development monitoring procedures to ensure compliance with subrecipient loan agreements, including timely residual receipts payments. The City defines residual receipts in new subrecipient loan agreements and in the promissory notes that accompany existing loan agreements that do not define residual receipts.</p>
<p>03-4 Adequacy of Workers Compensation Reserve (pages 5 - 6)</p>	<p>Accomplished. The actuarial report for fiscal year 2005 assumed no loss limit.</p>
<p>03-6 Allowance for Extra Work Should Not Be Encumbered (page 6)</p>	<p>The City has discontinued the execution of contracts and encumbrance of related funds for "allowance for extra work" that is not clearly defined.</p>
<p>02-2 Loan Agreement Should Be Properly Executed (pages 6 - 7)</p>	<p>Not accomplished. The loan agreement has not been executed.</p>
<p>01-3 Inadequate Monitoring of Property Management Companies (page 7)</p>	<p>Accomplished. Budgets for fiscal year 2005 were approved before the beginning of the fiscal year.</p>

Recommendations

Status

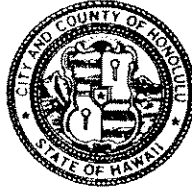
**00-3 Accounting for Infrastructure Costs
Should Be Improved** (page 7 - 8)

To improve accounting for infrastructure costs, the City's GIS system should be kept current, accurate and completed. The City should also perform periodic assessments on the infrastructure values to determine whether any write-downs are necessary. The City should also ensure that appropriate cost information is obtained from developers and recorded on a timely basis.

The City has established procedures to identify dedications to be recorded in the GIS system and to obtain related cost information.

CORRECTIVE ACTION PLAN

DEPARTMENT OF BUDGET AND FISCAL SERVICES
CITY AND COUNTY OF HONOLULU
530 SOUTH KING STREET, ROOM 208 • HONOLULU, HAWAII 96813
PHONE: (808) 523-4616 • FAX: (808) 523-4771 • INTERNET: www.honolulu.gov



MUFI HANNEMANN
MAYOR

MARY PATRICIA WATERHOUSE
DIRECTOR

PATRICK T. KUBOTA
DEPUTY DIRECTOR

February 8, 2006

Mr. Leslie I. Tanaka, City Auditor
Office of the City Auditor
City and County of Honolulu
1000 Uluohia Street, Suite 313
Honolulu, Hawaii 96707

Dear Mr. Tanaka:

Re: Management Advisory Report for the Fiscal Year 2004-2005

Enclosed is the response to the recommendations included in Nishihama & Kishida, CPAs Inc 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, 2005. The response includes actions taken or contemplated, anticipated completion dates, and City personnel responsible for the corrective action.

Sincerely,

A handwritten signature in black ink, appearing to read "M. Waterhouse", is written over a horizontal line.

MARY PATRICIA WATERHOUSE
Director of Budget and Fiscal Services

MPW:ve
Attachments

APPROVED:

A handwritten signature in black ink, appearing to read "Wayne M. Hashiro", is written over a horizontal line.

WAYNE M. HASHIRO, P.E.
Acting Managing Director

cc: Managing Director
BFS – Internal Control

**RESPONSE TO MANAGEMENT ADVISORY REPORT
FINDINGS AND RECOMMENDATIONS
For the Year Ended June 30, 2005**

CURRENT YEAR FINDINGS AND RECOMMENDATIONS

Finding No. 05-1: Demonstrate Financial Assurance For Landfill Postclosure Care Costs Under State Approved Mechanism

Audit Recommendation: The City should obtain approval of its landfill financial assurance mechanism from the State of Hawaii Department of Health and ensure that it demonstrates financial assurance for postclosure costs for the Waipahu and Kapaa landfills by 180 days after the end of each fiscal year until released of the responsibility as provided by state and federal laws.

Administration's Comment: The required documentation demonstrating financial assurance for postclosure costs have been prepared. The City issued a request to the State of Hawaii Department of Health to review the landfill financial assurance mechanism and is currently awaiting their approval. Documentation demonstrating financial assurance for postclosure costs will be completed in a timely manner each year as required.

Anticipated Completion Date: January 2006

Contact Person: Beverly Braun, Risk Manager, Budget and Fiscal Services (BFS)

Finding No. 05-2: Continue Risk-Based Monitoring of Section 8 Housing Choice Voucher Program

Audit Recommendation: The City should continue its effort in performing on-going quality control reviews of the Section 8 Housing Choice Voucher Program. The City should put an emphasis on identifying personnel who are prone to errors in order to assist them in addressing the problem.

Administration's Comment: The City is committed to providing its Housing Assistance Specialists (HAS) with the necessary training and guidance to insure compliance with the Section 8 Housing program requirements. Besides performing quality control reviews, and formal training, additional instruction will be provided to select individuals as needed.

Anticipated Completion Date: September 2005

Contact Person: Sandy Toma, Program Administrator, Department of Community Services (DCS)

**RESPONSE TO MANAGEMENT ADVISORY REPORT
FINDINGS AND RECOMMENDATIONS
For the Year Ended June 30, 2005**

Finding No. 05-3: Improve Documentation of Subrecipient Monitoring

Audit Recommendation: The City should implement procedures to adequately document correspondence with its subrecipients regarding all findings that were noted during the City's review of its subrecipients' audited financial statements. This includes the City's decision on any audit findings noted and the corrective action taken by its subrecipients. If a finding noted during the City's review is determined to be not applicable to the City-funded project and therefore no further follow up is deemed necessary, that fact should be documented as well as the rationale that supports this determination.

Administration's Comment: Although OMB Circular A-133 is applicable to subrecipients who expend federal funds of \$500,000 in a year, not all of the City's subrecipients meet the expenditure criteria and are not subject to the A-133 requirements. The City will implement procedures to provide written documentation of its requests and review of subrecipients' audited financial statements and related audit findings.

Anticipated Completion Date: June 2006

Contact Person(s): Deborah Kim Morikawa, Director, DCS
Randy Wong, Division Chief, DCS
Ernie Martin, Division Chief, DCS

**RESPONSE TO MANAGEMENT ADVISORY REPORT
FINDINGS AND RECOMMENDATIONS
For the Year Ended June 30, 2005**

PRIOR YEAR COMMENTS AND RECOMMENDATIONS

Finding No. 04-3: Late Filing of Federal Report

Audit Status: Not accomplished. The City filed the September 30, 2004 Report of Disadvantaged Business Enterprises Awards and Commitments on March 31, 2005, rather than on the required date of December 31, 2005. Due to an oversight, the March 31, 2005 report has not been filed. We were informed that the City has been unable to file the required report in a timely manner due to a lack of adequate staff.

Recommendation: To comply with federal regulations, the City should establish procedures to ensure that the Report of Disadvantaged Business Enterprise (DBE) Awards and Commitments is completed and filed timely.

Administration's Comment: We do not believe that establishing procedures will ensure the timely completion and filing of reports because the position whose primary responsibility is to carry out the DBE program requirements remained vacant in FY 2005. Current Department of Transportation Services' staff have limited time to carry out the duties of a full-time DBE Liaison Officer in addition to their regular workload. Filling the position will be instrumental in submitting reports in a timely manner.

The Fiscal Year 2006 Executive Operating Budget and Program approved only 3 months of salary for the vacant position whose primary duties will be to cover the DBE program. Accordingly, we were not able to fill the position by December 2005, the anticipated completion date identified in our FY 2004 response. Recruitment was initiated and the vacancy was advertised on January 29, 2006.

Anticipated Completion Date: March 2006

Contact Person: Kenneth Hamayasu, Division Chief, Department of Transportation Services

Finding No. 04-5: Bank Reconciliations Should Be Improved

Audit Status: Not accomplished. Bank reconciliations prepared during the fiscal year ended June 30, 2005 continued to include items that canceled each other out.

**RESPONSE TO MANAGEMENT ADVISORY REPORT
FINDINGS AND RECOMMENDATIONS
For the Year Ended June 30, 2005**

Recommendation: To ensure bank reconciliations are properly and timely prepared, the City should exclude items that cancel each other out as reconciling items on the bank reconciliations. A supervisor should carefully review the bank reconciliations.

Administration's Comment: The City will continue its efforts to streamline the preparation and review of bank reconciliations.

Anticipated Completion Date: June 2006

Contact Person(s): Nelson Koyanagi Jr, Chief Accountant, BFS
Robert Morita, Executive Assistant, BFS

Finding No. 02-2: Loan Agreements Should Be Properly Executed

Audit Status: Not accomplished. The loan agreement has not been executed.

Administration's Comment: All loan agreements are currently fully executed prior to the disbursement of funds. The City is continuing to work with the subrecipient and its lawyers to resolve the contract issues and obtain a signed loan agreement.

Anticipated Completion Date: December 2006

Contact Person(s): Charles Woodward, Division Chief, Facilities Maintenance (DFM)
Randy Wong, Division Chief, DCS