

DEPARTMENT OF THE ATTORNEY GENERAL
STATE OF HAWAII

MANAGEMENT LETTER

FOR THE YEAR ENDED JUNE 30, 2012

Akamine, Oyadomari & Kosaki
Certified Public Accountants, Inc.

Akamine, Oyadomari & Kosaki

CERTIFIED PUBLIC ACCOUNTANTS, INC.

March 25, 2013

Ms. Jan K. Yamane, Acting State Auditor
Office of the Auditor
State of Hawaii

Mr. David M. Louie, Attorney General
Department of the Attorney General
State of Hawaii

Dear Ms. Yamane and Mr. Louie:

In planning and performing our audit of the financial statements of the Department of the Attorney General (Department), State of Hawaii, as of and for the year ended June 30, 2012, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States, we considered the Department's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses 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. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We did not identify any deficiencies in internal controls that we considered to be material weaknesses, as defined above.

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, including applicable provisions of the Hawaii Public Procurement Code (Chapter 103D of the Hawaii Revised Statutes), and procurement rules, directives and circulars, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on

compliance with those provisions was not an objective of an audit and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance:

- Deficit in CSEA Agency Fund should be addressed and resolved.

We have also audited the compliance of the Department of the Attorney General of the State of Hawaii (AG), with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the AG's major federal programs for the year ended June 30, 2012.

In planning and performing our audit, we considered the AG's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the AG's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies.

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

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described below to be significant deficiencies:

- Controls over monitoring of sub-recipients should be implemented.
- Documentation of expenditures should be properly maintained.

We are also submitting the status of recommendations made in our letter of March 27, 2012.

Our comments deal exclusively with accounting, operational, and recordkeeping systems and procedures and should not be regarded as reflecting upon the integrity or capabilities of anyone in the Department of the Attorney General.

This communication is intended solely for the information and use of management and others within the Department of the Attorney General and the Office of the Auditor, State of Hawaii, and is not intended to be and should not be used by anyone other than these specified parties.

We would like to take this opportunity to thank the staff of the Department, for their cooperation and assistance during our audit. After you and your associates have had an opportunity to review our comments, we would be pleased to answer any questions you may have.

Very truly yours,

Akamine, Oyadomari & Kosaki CPAs, Inc.

**Department of the Attorney General
State of Hawaii**

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CURRENT FINDINGS AND RECOMMENDATIONS
FOR THE YEAR ENDED JUNE 30, 2012

**Department of the Attorney General
State of Hawaii
Current Findings and Recommendations
For the year ended June 30, 2012**

Compliance Matters Affecting Financial Reporting

Deficit in CSEA Agency Fund should be addressed and resolved.

The Department of the Attorney General (AG) maintains four agency funds including an Agency Fund for the Child Support Enforcement Agency (CSEA), a division of the Department of the Attorney General, which provides for a system of collections, disbursements, and enforcement of court ordered child support payments. Amounts collected for child support are custodial in nature and are under the control of the CSEA as a fiduciary and are not available for use in government operations.

Cash receipts collected from non-custodial parents are deposited into the CSEA bank account for disbursement to custodial parents. Transactions are recorded in the CSEA Agency Fund.

At June 30, 2012 the balance sheet of the CSEA Agency Fund comprised:

Cash, net of outstanding checks of \$2,924,000 of which \$2,248,000 were over one year old	\$ 8,505,000
Liability to agency recipients	<u>11,322,000</u>
Deficit	<u><u>\$ 2,817,000</u></u>

The deficit of \$2,817,000 is comprised of the following:

Unrecovered nonsufficient funds support payments from non-custodial parents	\$ 1,072,000
Uncollected amounts due from custodial parents resulting from overpayment of child support payments	1,009,000
State's portion of IRS tax intercept fees to enforce collecting child support payments	498,000
Other	<u>238,000</u>
	<u><u>\$ 2,817,000</u></u>

Federal regulations provide for child support payments from the non-custodial parent to be remitted to the custodial parent within two business days upon receipt by the CSEA. Certain support payments, however, are held and not immediately disbursed due to payments received with insufficient information to identify the intended custodial parent, child support payment checks returned as undeliverable to the custodial parent, amounts intercepted and withheld from the delinquent non-custodial parent's income tax return refund which are subject to challenge, prepaid child support payments made by the non-custodial parent not yet due to the custodial parent, and amounts held for overpayments for public assistance to the custodial parent.

The total support payments held was approximately \$11,322,000 at June 30, 2012. CSEA has over the years accumulated a deficit of \$2,817,000 in the Agency Fund at June 30, 2012. Since the child support moneys are custodial in nature, the Agency Fund should not be operating with a deficit.

The deficit was caused by the following.

Since Federal regulations require disbursement of child support payments to custodial parents within two business days of receipt, CSEA disbursed amounts received without knowing whether the non-custodial parent had sufficient funds at the bank. Nonsufficient funds (NSF) checks rejected by the bank result in amounts due from non-custodial parents. Recovery of such funds were dependent on collecting from the non-custodial parent and not by reducing future child support payments to the custodial parent.

Errors in the payment process gave rise to uncollected recoupments due from the custodial parent resulting from overpayment of child support payments. CSEA's ability to collect such overpayment from the custodial parent by reducing future child support payments was limited.

CSEA enforcement actions against delinquent non-custodial parents included intercepting tax return refunds. The IRS assessed a fee for the intercept. While two thirds of the intercept fees were paid by CSEA federal grant funds, the remaining one third is the responsibility of the CSEA. This portion represents the State's matching portion under the federal grant and is not recoverable from the custodial parent.

Over the years the Agency trust fund moneys have been used by CSEA to pay for all of the above items and as of June 30, 2012 obligations exceeded cash, resulting in a \$2,817,000 deficit in the CSEA Agency Fund. The present deficit is being funded by the "float" created by outstanding uncashed checks (\$2,248,000 over one year old) and from obligations due to parents not being immediately payable. Any recovery from parents for either NSF payments or overpayments of support is problematic.

As a result of the deficit there is presently not enough cash in the Agency Fund to pay all of the Agency Fund obligations.

Recommendation: We continue to recommend that the AG resolve the deficit position in its Agency Fund.

**Significant Weaknesses in Internal Control Over Compliance Affecting
the Department's Federal Programs**

Controls over compliance with sub-recipient monitoring program should be implemented.

Federal regulations provide that grantees are responsible for monitoring sub-recipients of grants to assure compliance with applicable Federal requirements. Crime Prevention Justice Assistance (CPJA) monitoring program includes review of progress reports from sub-recipients and on-site visits of the sub-recipients.

We noted that semi-annual progress reports due from sub-recipients within 30 days after the end of the reporting period were not received by the CPJA as follows:

	CFDA #16.588 Stop Violence Against Women Formula Grant	CFDA #16.738 Edward Byrne Memorial Justice Assistance Grant
Sub-recipient	Prosecuting Attorney, City and County of Honolulu 09-EF-07	Maui County Police Department 09-DJ-07
Progress reporting period	4/1/2011-9/30/2011 10/1/2011-3/31/2012	1/1/2012-6/30/2012

During our review of the CPJA on-site monitoring program we noted that there was no on-site monitoring visit conducted for Hawaii Pacific Health (09-WF-02) a sub-recipient for the CDFA #16.588 Stop Violence Against Women Formula Grant.

On-site visits were conducted by the CPJA for CDFA #16.575 Crime Victim Assistance Grant but the results of the visits were not documented in project monitoring reports in a timely manner as follows:

<u>Sub-recipient</u>	<u>Sub-recipient #</u>	<u>Date of on-site visit</u>	<u>Project monitoring report date</u>
Prosecuting Attorney, City and County of Honolulu	08-VA-02	10/28/2010	10/12/2012
Prosecuting Attorney, County of Kauai	08-VA-03	4/23/2012	10/12/2012
Prosecuting Attorney, County of Hawaii	08-VA-04	10/7/2010	10/12/2012

The CPJA did not have controls in place to insure compliance with its monitoring program for receipt of sub-recipient status reports, on-site visits of sub-recipients, and for the timely completion of project monitoring reports for on-site visits.

Failure to properly monitor sub-recipients could lead to sub-recipients noncompliance with the applicable federal grant requirements.

Recommendation:

We recommend that the CPJA implement controls to insure compliance with its sub-recipient monitoring program.

Documentation of expenditures should be properly maintained.

Federal regulations provide that grantees are responsible for maintaining documentation of expenditures charged to grant funds.

In our testing of expenditures for Federal grants at Hawaii Criminal Justice Data Center (HCJDC), we noted two expenditures out of forty selected in our sample did not have proper supporting documentation. Neither summary warrant vouchers nor the related invoices for the expenditures could be located by HCJDC personnel. Both the expenditures were with vendor Commerce Solutions, Inc. in the amount of \$5,863.76 and \$5,673.46 charged to CFDA #16.710 Public Safety Partnership and Community Oriented Policing Services (COPS) grant. We were not able to ascertain whether expenditures were authorized, supported by an invoice, and properly chargeable to the federal grant.

HCJDC believes that the summary warrant voucher and related invoices were misplaced.

Expenditures paid with Federal grant funds could be disallowed by the U.S. Department of Justice, the grantor, in the absence of proper documentation.

Recommendation:

We recommend that HCJDC implement the necessary procedures and controls to provide for the proper retention of expenditure documentation.

**STATUS OF FINDINGS AND RECOMMENDATIONS
CONTAINED IN THE MANAGEMENT LETTER
DATED MARCH 27, 2012**

**Department of the Attorney General
State of Hawaii**

Findings and recommendations contained in the management letter dated March 27, 2012

Compliance matters affecting financial reporting

Deficit in CSEA Agency Fund should be addressed and resolved.

The deficit in the CSEA Agency Fund amounted to \$2,401,000 at June 30, 2011. We had recommended that the Department address and resolve the deficit position of the CSEA Agency fund.

Current status:

The deficit in the CSEA Agency Fund amounted to \$2,817,000 at June 30, 2012. See current findings for further current details relating to this matter.

Federal Award Findings and Questioned Costs

Controls should be implemented over draw downs of Federal grants and expenditures charged to grants.

Funds from a grant draw down in August 2008 by HCJDC was not being tracked by the Division. As a result the funds remained in the State's bank accounts until May 2010. During fiscal 2011 the HCJDC expended a portion of the grant funds after the grant had long expired. The expenditures were also unrelated to the grant's original purpose.

We recommended that appropriate procedures and controls be implemented to ascertain that all draw downs on grants have been received on a timely basis and that all expenditures charged to the related grant are appropriate and timely. We also recommended that HCJDC make a determination of the proper disposition of expenditures made after the grant expiration as well as any unspent grant monies.

Current Status:

Controls have been implemented. No similar findings were noted during the 2012 audit. The grantor has been reimbursed for the inappropriate expenditures charged to the grant as well as unspent grant funds.

Controls over monitoring of sub-recipients should be implemented.

During our 2011 audit we noted that there was no written documentation to evidence monitoring of certain sub-recipients by the CPJA. We had recommended that the CPJA implement the necessary procedures and controls to provide for proper monitoring of all sub-recipients.

Current status:

Exceptions continue to be noted during our 2012 audit. See current audit finding.

**Department of the Attorney General
State of Hawaii**

Other Findings

Cash Outside State Treasury Should be Collateralized Through Pledging of Securities

The Department maintains certain funds in two checking accounts in a Hawaii bank which are held separately from the State Treasury managed by the Department of Budget and Finance. One bank account is a fiduciary account that is used for Child Support Enforcement Agency (CSEA) transactions and is recorded in the Department's Agency Fund. Child support payments are collected from non-custodial parents and are deposited into the bank account. Funds are then disbursed to custodial parents.

The second bank account is used to account for the Federal share of child support payment collections retained by CSEA under the Personal Responsibility and Work Reconciliation Act of 1996 (PRWORA) and the Temporary Assistance for Needy Families (TANF) program. The bank account is recorded in the Department's CSEA Special Revenue Fund.

From December 31, 2010 through December 31, 2012, the Federal Deposit Insurance Corporation (FDIC) provided temporary full insurance coverage on both bank accounts. On January 1, 2013 FDIC coverage is limited to \$250,000 per depositor.

To mitigate the risk that the Department's deposits may suffer a financial loss, we had recommended the Department obtain from the bank, collateral in the form of securities pledged to the Department. The market value of the securities pledged should equal or exceed the amount of cash normally held by the Department in the bank account

Current Status:

At June 30, 2012 the book value and bank account balances amounted to:

	Book Balance	Bank account balance
Agency account	\$ 8,505,000	\$ 11,475,000
CSEA TANF account	\$ 4,672,000	\$ 4,613,000

The difference between the book balance and bank account balance are principally due to outstanding checks for the fiduciary account and deposits in transit for the CSEA TANF account.

As of January 1, 2013 the bank account balance substantially exceeded the FDIC coverage.

The Department has discussed with the bank the pledging of securities. During the discussions a question was raised as to whether the Hawaii Revised Statutes permitted the bank to pledge securities for these deposits.

Hawaii Revised Statutes (HRS) Section 412: 4-112 provides that no financial institution shall give a preference to any depositor by pledging the assets of the financial institution, except as

otherwise authorized. A financial institution may pledge to secure deposits or borrowing of public funds. Public funds are defined as funds belonging to the State or to the official credit of the Director of Finance. HRS section 38-2 provides that all moneys in the State Treasury may be deposited by the Director of Finance (Director) to the credit of the State in any depository which the Director with the approval of the Governor, may select, and any sums so deposited shall be deemed to be in the State Treasury provided that the depository in which the money is deposited furnishes security. All deposits of money, except time deposits, shall be paid upon demand on checks signed by the Director and counter signed by the State Comptroller.

The two CSEA bank accounts are under the control of the Department and its Child Support Enforcement Agency. The agency bank account is managed by CSEA as a fiduciary for the custodial parents and their children. The TANF funds are State funds under the control of CSEA and are used to fund CSEA operations.

The Department is presently researching whether the two CSEA bank accounts legally constitute public funds.

Due to the change in the FDIC coverage, effective January 1, 2013 most of the deposits in the two bank accounts are uninsured. We recommend that the legal issues relating to what constitutes public funds be resolved and a determination made as to whether bank securities can be pledged to protect the State from the risk of financial loss.

Petty Cash Should be Reconciled

The Department's fiscal office maintains a \$15,000 petty cash account. We were informed that the last time the account had been reconciled was in September 2009. The account is comprised of cash in a bank account, cash on hand, and outstanding unreimbursed petty cash vouchers.

Current Status:

As of June 30, 2012 the petty cash account had not been reconciled and we were unable to substantiate \$4,483 of the account balance.

To safeguard petty cash and improve controls we recommend that the petty cash account be reconciled on a monthly basis. This reconciliation should also be reviewed by a responsible individual.