

**OFFICE OF HAWAIIAN AFFAIRS
STATE OF HAWAII**

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS AND
UNIFORM GUIDANCE

Year Ended June 30, 2018



**OFFICE OF HAWAIIAN AFFAIRS
STATE OF HAWAI'I**

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PART I

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS**

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT
AUDITING STANDARDS***

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of the Office of Hawaiian Affairs,
State of Hawai'i

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information as well as the budgetary comparison for the general fund of the Office of Hawaiian Affairs (OHA), State of Hawai'i, as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise OHA's basic financial statements, and have issued our report thereon dated March 25, 2019. Our report includes a reference to another auditor who has audited the financial statements of Hi'ilei Aloha, LLC as described in our report on OHA's financial statements. This report includes our consideration of the results of the other auditor's testing of internal control over financial reporting and compliance and other matters that are reported on separately by the other auditor. However, this report, insofar as it relates to the results of the other auditor, is based solely on the report of the other auditor.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered OHA's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of OHA's internal control. Accordingly, we do not express an opinion on the effectiveness of OHA's internal control.

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. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether OHA's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 our audit, and accordingly, we do not express such an opinion. The results of our tests and tests of the other auditor disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

N&K CPAs, Inc.

Honolulu, Hawaii
March 25, 2019

PART II

REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM; REPORT ON INTERNAL CONTROL OVER COMPLIANCE; AND REPORT ON SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS REQUIRED BY UNIFORM GUIDANCE AND NATIVE HAWAIIAN LOAN FUND FINANCIAL STATEMENTS

**REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM; REPORT
ON INTERNAL CONTROL OVER COMPLIANCE; AND REPORT ON SCHEDULE OF
EXPENDITURES OF FEDERAL AWARDS REQUIRED BY UNIFORM GUIDANCE
AND NATIVE HAWAIIAN LOAN FUND FINANCIAL STATEMENTS**

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of the Office of Hawaiian Affairs,
State of Hawai'i

Report on Compliance for Each Major Federal Program

We have audited the Office of Hawaiian Affairs (OHA), State of Hawai'i's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of OHA's major federal programs for the year ended June 30, 2018. OHA's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions applicable to its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of OHA's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of the Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about OHA's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of OHA's compliance.

Opinion on Each Major Federal Program

In our opinion, OHA complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2018.

Report on Internal Control over Compliance

Management of OHA is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered OHA's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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 OHA's internal control over compliance.

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 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.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance and Native Hawaiian Revolving Loan Fund Financial Statements

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information as well as the budgetary comparison of the general fund of OHA as of and for the year ended June 30, 2018, and the related notes to the financial statements which collectively comprise OHA's basic financial statements. We issued our report thereon dated March 25, 2019, which contained unmodified opinions on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis, as required by the Uniform Guidance and is not a required part of the basic financial statements. The accompanying Native Hawaiian Revolving Loan Fund financial statements are presented for the purpose of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information, except for the portion marked "unaudited," on which we express no opinion, has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards and the Native Hawaiian Revolving Loan Fund financial statements are fairly stated in all material respects in relation to the basic financial statements as a whole.

N&K CPAs, Inc.

Honolulu, Hawaii
March 25, 2019

PART III
SUPPLEMENTARY INFORMATION

Office of Hawaiian Affairs, State of Hawai'i
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended June 30, 2018

Federal Grantor/Pass-through Grantor/Program Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Total Federal Expenditures
Department of Transportation			
Pass-through Department of Transportation - State of Hawai'i Highway Planning and Construction	20.205	20358600	\$ <u>356,977</u>
Total Department of Transportation			<u>356,977</u>
Environmental Protection Agency			
Brownfields Assessment and Cleanup Cooperative Agreements	66.818	N/A	<u>16,407</u>
Total Environmental Protection Agency			<u>16,407</u>
Department of Health and Human Services			
Native American Program, Native Hawaiian Revolving Loan Program	93.612	N/A	<u>1,988,654</u>
Total Department of Health and Human Services			<u>1,988,654</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			\$ <u><u>2,362,038</u></u>

The accompanying notes are an integral part of this schedule.

Office of Hawaiian Affairs, State of Hawai'i
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended June 30, 2018

NOTE A - BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal award activity of OHA under programs of the federal government for the year ended June 30, 2018. The information in the Schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of OHA, it is not intended to and does not present the financial position, changes in financial position, or cash flows of OHA.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are reported in accordance with the modified-accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

NOTE C - INDIRECT COST RATE

OHA has not elected to use the 10-percent de minimis indirect cost rate as allowed under the Uniform Guidance.

NOTE D - NATIVE HAWAIIAN REVOLVING LOAN PROGRAM

The Native Hawaiian Revolving Loan Program is administered directly by OHA and balances and transactions related to this program are included in OHA's basic financial statements. Loans issued during the year are included in the federal expenditures presented in the Schedule. The balance of loans outstanding at June 30, 2018 was \$6,401,523.

Office of Hawaiian Affairs, State of Hawai'i
Native Hawaiian Revolving Loan Fund
BALANCE SHEET
June 30, 2018

ASSETS

ASSETS

Cash in banks	\$	6,890,445
Cash held by investment managers		346,736
Interest and dividends receivable		80,274
Prepaid expenses		1,999
Notes receivable, net of allowance		4,870,767
Investments		<u>13,148,976</u>
Total assets	\$	<u><u>25,339,197</u></u>

LIABILITIES AND FUND BALANCE

LIABILITIES

Accounts payable	\$	56,603
Due to other funds		<u>70</u>
Total liabilities		<u>56,673</u>

FUND BALANCE

Restricted for:		
Long-term portion of notes receivable		3,402,511
Native Hawaiian loan program		<u>21,880,013</u>
Total fund balance		<u>25,282,524</u>
Total liabilities and fund balance	\$	<u><u>25,339,197</u></u>

Office of Hawaiian Affairs, State of Hawai'i
Native Hawaiian Revolving Loan Fund
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGE IN FUND BALANCE
Year Ended June 30, 2018

REVENUES

Loan interest income	\$	291,311
Investment earnings		83,811
Other revenue		<u>43,011</u>
Total revenues		<u>418,133</u>

EXPENDITURES

Salaries and fringe benefits		461,258
Services		196,612
Capital expenditures		46,579
Advertising		43,236
Investment manager fee		26,511
Rent		23,982
Repairs and maintenance		22,000
Other expenses		10,812
Legal services		9,553
Travel		3,507
Recoveries of bad debt		<u>(255,746)</u>
Total expenditures		<u>588,304</u>

NET CHANGE IN FUND BALANCE (170,171)

FUND BALANCE AT JULY 1, 2017 25,452,695

FUND BALANCE AT JUNE 30, 2018 \$ 25,282,524

**Office of Hawaiian Affairs, State of Hawai'i
Native Hawaiian Revolving Loan Fund
STATEMENT OF CASH FLOWS (UNAUDITED)
Year Ended June 30, 2018**

Cash flows from operating activities	
Net change in fund balance	\$ (170,171)
Adjustments to reconcile net change in fund balance to net cash used in operating activities:	
Recoveries of bad debt	(255,746)
Net change in fair value of investment securities	114,601
Amortization of discount on investment securities	22,009
Increase in:	
Interest and dividends receivable	(12,812)
Prepaid expenses	(1,999)
Increase (decrease) in:	
Accounts payable	(4,358)
Due to other funds	<u>70</u>
Net cash used in operating activities	<u>(308,406)</u>
Cash flows from investing activities	
Purchase of investments	(10,100,664)
Proceeds from maturities of investments	10,122,500
Notes receivable issued	(1,400,350)
Proceeds from repayment of notes receivable	<u>2,340,573</u>
Net cash provided by investing activities	<u>962,059</u>
NET INCREASE IN CASH	653,653
Cash at beginning of year	<u>6,583,528</u>
Cash at end of year	\$ <u>7,237,181</u>
Cash consists of:	
Cash in banks	\$ 6,890,445
Cash held by investment manager	<u>346,736</u>
	\$ <u>7,237,181</u>

PART IV
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Office of Hawaiian Affairs, State of Hawai'i
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended June 30, 2018

SECTION I - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP: Unmodified

Internal control over financial reporting:

Material weakness(es) identified?	___	yes	___	<input checked="" type="checkbox"/>	no
Significant deficiency(ies) identified?	___	yes	___	<input checked="" type="checkbox"/>	none reported

Noncompliance material to financial statements noted? ___ yes no

Federal Awards

Internal control over major federal programs:

Material weakness(es) identified?	___	yes	___	<input checked="" type="checkbox"/>	no
Significant deficiency(ies) identified?	___	yes	___	<input checked="" type="checkbox"/>	none reported

Type of auditor's report issued on compliance for major federal programs: Unmodified

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? ___ yes no

Identification of major federal programs:

CFDA Number	Name of Federal Program
93.612	Native American Program, Native Hawaiian Revolving Loan Program

Dollar threshold used to distinguish between type A and type B programs: \$ 750,000

Auditee qualified as low-risk auditee? ___ yes ___ no

SECTION II - FINANCIAL STATEMENT FINDINGS

None

SECTION III - FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

None

PART V

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Office of Hawaiian Affairs, State of Hawai'i
STATUS REPORT
Year Ended June 30, 2018

No prior audit findings which apply under the current criteria of the Uniform Guidance were noted.