

**Department of Agriculture
State of Hawaii
Financial and Compliance Audit
Year Ended June 30, 2007**

Hattori & Co., CPAs, Inc.
Honolulu, Hawaii



**DEPARTMENT OF AGRICULTURE
STATE OF HAWAII**

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Hattori & Co., CPAs, Inc.



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Ms. Sandra Lee Kunimoto
Chairperson, Board of Agriculture
State of Hawaii

Dear Ms. Kunimoto:

This is our report on the financial and compliance audit of the Department of Agriculture of the State of Hawaii (Department) for the year ended June 30, 2007, including the accompanying notes to those financial statements, and the independent auditors' report thereon. Our audit was performed in accordance with the requirements of the Single Audit Act Amendments of 1996 and with terms of our contract with the Department.

AUDIT OBJECTIVES

The primary purpose of the audit was to form an opinion and issue an independent auditors' report on the fairness of the presentation of the Department's financial statements for the fiscal year ended June 30, 2007, to report on its internal control structure and to report on its compliance with applicable laws and regulations in accordance with the requirements established by the Single Audit Act Amendment of 1996, and the provisions of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

The specified objectives of the audit were:

- 1) To satisfy the audit requirements of Circular A-133 issued by the United States Office of Management and Budget.
- 2) To provide a basis for an opinion on the fairness of the presentation of the Department's financial statements.
- 3) To determine whether expenditures have been made and all revenues and other receipts to which the Department is entitled have been collected and accounted for in accordance with the laws, rules and regulations, and policies and procedures of the State of Hawaii and, where applicable, the Federal government.
- 4) To evaluate the adequacy of the Department's system of internal accounting control in assuring that there is effective control over and proper accounting of revenues, expenditures, assets and liabilities.
- 5) To determine whether the Department has materially complied with the fiscal provisions of grant agreements and applicable Federal laws, regulations and circulars with regard to Federal grant activities.

AUDIT SCOPE

Our audit was performed in conformity with auditing standards generally accepted in the United States of America, Governmental Auditing Standards issued by the Comptroller General of the United States, and the provisions of OMB Circular A-133 as they pertain to financial and compliance audits. Accordingly, the audit consisted of procedures to understand the Department and its operations, to test the Department's internal control structure and to test selected transactions and accounting records in order to formulate an opinion on its financial statements and schedule of expenditures of federal awards.

Attari & Co., CPAs, Inc.

Honolulu, Hawaii
March 8, 2008

Financial Audit



INDEPENDENT AUDITOR'S REPORT

To The Board of Agriculture
State of Hawaii

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Department of Agriculture, State of Hawaii as of and for the year ended June 30, 2007, which collectively comprise the department's basic financial statements. These financial statements are the responsibility of the department's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall combined financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 2, the financial statements of the department present the financial position and changes in financial position of only that portion of the governmental activities, each major fund, and the aggregate remaining fund information of the State of Hawaii that is attributable to the transactions of the department. They do not purport to, and do not, present the financial position of the State of Hawaii as of June 30, 2007, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the government activities, each major fund, and the aggregate remaining fund information of the department as of June 30, 2007, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on page 5 to 11 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated March 8, 2008 on our consideration of the department's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is

INDEPENDENT AUDITOR'S REPORT, CONTINUED

an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the department's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the basic financial statements of the department. The schedule of expenditures of federal awards has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Kuttari & Co., CPAs, Inc.

Honolulu, Hawaii
March 8, 2008

**Department of Agriculture
State of Hawaii
Management Discussion and Analysis**

Our discussion and analysis of the Department of Agriculture of the State of Hawaii (Department)'s financial performance provides an overview of the Department's financial activities for the fiscal year ended June 30, 2007. We encourage the readers to read the information presented here in conjunction with the basic financial statements.

Overview of the Basic Financial Statements

This discussion and analysis is intended to serve as an introduction to the Department's basic financial statements comprising of three major components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the basic financial statements. This report also contains other required supplementary information in addition to the basic financial statements themselves.

Government-Wide Financial Statements

The government-wide financial statements consist of the statement of net assets and the statement of activities. The statement of net assets and the statement of activities provide information about the activities of the Department as a whole and present a longer-term view of the Department's finances. These statements include *all* assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The statement of net assets and statement of activities report the Department's *net assets* and changes in them. The Department's net assets or the difference between assets and liabilities is one way to measure the Department's financial health, or *financial position*. Over time, *increases or decreases* in the Department's net assets are one indicator of whether its *financial health* is improving or deteriorating. Other non-financial factors such as changes in local, state and federal legislation and public policy may also have an affect on the Department's various programs and should also be considered in assessing the *overall health* of the Department.

We have reported the Department's governmental activities in the statement of net assets and the statement of activities. All of the Department's basic services are reported here, including the animal industry, agricultural loan, quality assurance, agricultural development, agricultural resource management and plant industry divisions, aquaculture development program, general administration, and the agribusiness development corporation. General fund appropriations, fees, agricultural loan interest, and state and federal grants finance most of these activities. The Department is not considered to have business-type activities and component units.

Fund Financial Statements

Fund financial statements tell how governmental activities and services were financed in the short term as well as what remains for future spending. Fund financial statements also report the Department's operations in more detail than the government-wide statements by providing information about the Department's most significant funds.

Generally, the Department's funds are required to be established by State law. However, the Department establishes many other funds to show that it is meeting legal responsibilities for using certain taxes, grants, and other money (like grants received from the U.S. Department of Agriculture).

**Department of Agriculture
State of Hawaii
Management Discussion and Analysis**

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Department, like the State as whole and other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the Department can be divided into two categories: (1) governmental funds, and (2) fiduciary funds.

Governmental Funds

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. The Department's basic services are reported in governmental funds. These funds are reported using an accounting method called *modified accrual* accounting, which measures cash and all other *financial* assets that can readily be converted to cash. The governmental fund statements are comprised of the balance sheet, and statement of revenues, expenditures, and changes in fund balances. The relationship (or differences) between *activities* (reported in the statement of net assets and the statement of activities) and governmental *funds* are reported on the reconciliation of the statement of revenues, expenditures, and changes in fund balances – governmental funds to the statement of activities.

Fiduciary Funds

Fiduciary funds are used to account for resources held for the benefit of parties outside the State. The Department is the trustee, or *fiduciary*, for private-purpose trust and agency funds. The fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the Department's own programs. All of the Department's fiduciary activities are reported in a separate statement of fiduciary net assets. A statement of changes in fiduciary net assets is also included for the Department's private-purpose trust funds. The Department is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

Notes to Basic Financial Statements

The notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Other Required Supplementary Information

In addition to the basic financial statements and accompanying notes, this report contains the statement of revenues, expenditures and changes in fund balances (budget and actual) for both general fund and major special revenue funds.

Government-Wide Financial Analysis

The Department's condensed financial information of its governmental activities for the year ended June 30, 2007 and June 30, 2006 is provided in Tables 1 and 2 below.

**Department of Agriculture
State of Hawaii
Management Discussion and Analysis**

**Table 1
Net Assets
(in Millions)**

	<u>2007</u>	<u>2006</u>
Current and other assets	\$ 55.2	36.1
Loans receivable	15.1	16.4
Capital assets	<u>73.3</u>	<u>74.3</u>
Total assets	<u>143.6</u>	<u>126.8</u>
Long-term liabilities	10.0	10.1
Other liabilities	<u>3.0</u>	<u>3.0</u>
Total liabilities	<u>13.0</u>	<u>13.1</u>
Net assets:		
Invested in capital assets	73.3	74.3
Restricted	48.8	47.5
Unrestricted (deficit)	<u>8.5</u>	<u>(8.1)</u>
Total net assets	<u>130.6</u>	<u>113.7</u>
Total liabilities and net assets	\$ <u>143.6</u>	<u>126.8</u>

**Table 2
Changes in Net Assets
(in Millions)**

	<u>2007</u>	<u>2006</u>
Revenue		
Program revenues:		
Charges for services	\$ 8.5	8.0
Operating grants and contributions	2.7	2.0
Capital grants and contributions	3.7	.8
State allotted appropriations	35.2	15.0
Non-imposed employee fringe benefit	4.2	3.9
Transfers	<u>(0.7)</u>	<u>1.2</u>
Total revenues	<u>\$ 53.6</u>	<u>30.9</u>
Program expenses		
Productivity improvement and management assistance	\$ 14.2	12.7
Product development and marketing	5.1	4.7
General support for agriculture	5.5	3.9
Agricultural water development and irrigation services	7.0	4.3
Pollution control	2.0	2.2
Protection of the consumer	1.0	1.0
Aquaculture development	0.7	0.8
Agriculture loans	<u>1.2</u>	<u>0.9</u>
Total expenses	<u>36.7</u>	<u>30.5</u>
Increase in net assets	<u>\$16.9</u>	<u>0.4</u>

The Department's total assets exceed liabilities by \$130.6 million at the end of the fiscal year. Net assets of the Department's governmental activities increased by 16.9 million or 14.9% (\$130.6 million compared to \$113.7 million) over the prior fiscal year. The largest portion of the Department's net assets (\$73.3 million)

**Department of Agriculture
State of Hawaii
Management Discussion and Analysis**

reflects its investment in capital assets (e.g., land, infrastructure, buildings, and equipment) less any related debt used to acquire those assets that is still outstanding. The Department uses these assets to provide services to citizens; consequently, these capital assets are not available for future spending. A portion of the Department's net assets (\$48.8 million) represents resources that are subject to external restrictions, enabling legislation, or other legal requirements on how they may be used. The remaining unrestricted net assets, the part of net assets that can be used to finance day-to-day operations without constraints, totaled \$8.5 million.

The Department's total revenues increased by \$22.7 million primarily due to increases in state allotted appropriations which included \$11,886,000 appropriated for repair and maintenance of various irrigation systems pursuant to Act 233, SLH 2006, \$5,610,000 transferred into the Department to mitigate damages at irrigation systems resulting from the October 6, 2006, Kiholo Bay Earthquake, and \$500,000 also transferred into the Department to mitigate health and safety hazards at the Kailua Reservoir resulting from the March 2006 Flooding.

The Department's total expenses increased by \$6.2 million primarily due to increased spending for agricultural water development and irrigation services to mitigate damages to irrigation systems resulting from the October 2006 Earthquake and the March 2006 Flooding.

Table 3 presents the cost of each of the Department's five largest programs as well as each program's net cost (total cost less revenues generated by the activities). The net cost shows the financial burden that was placed on Hawaii's taxpayers by each of these functions.

**Table 3
Governmental Activities
(in Millions)**

	<u>Total Cost of Services</u>		<u>Net Cost of Services</u>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Productivity improvement and management assistance	\$ 14.2	12.7	10.2	8.7
Product development and marketing	5.1	4.7	4.6	4.1
General support for agriculture	5.5	3.9	2.4	2.2
Agricultural water development and irrigation services	7.0	4.3	1.9	2.2
Pollution control	2.0	2.2	1.0	1.0
All others	<u>2.8</u>	<u>2.7</u>	<u>1.6</u>	<u>1.4</u>
Totals	<u>\$ 36.6</u>	<u>30.5</u>	<u>21.7</u>	<u>19.6</u>

The increase in total net cost of services from FY06 to FY07 in productivity improvement and management assistance is attributed to the increased level of spending for pest inspection activities in which \$2 million in additional general funds and 45 new positions were appropriated by the 2006 Legislature.

**Department of Agriculture
State of Hawaii
Management Discussion and Analysis**

Financial Analysis of the Department's Funds

The Department's governmental funds reported a combined fund balance of \$67.9 million, an increase of approximately \$18 million in comparison with the prior fiscal year. Of the approximately \$18 million increase in combined fund balance, approximately \$16.7 million is attributed to increases in the general fund balance primarily due to the \$11,886,000 appropriated for repair and maintenance of irrigation systems of which most were not expended in the current fiscal year. Pursuant to Act 233, SLH 2006, the funds do not lapse until June 30, 2008.

Financial Analysis of Significant General Fund Budget Variations

The difference of \$6,803,668 between the original and final budgeted amounts in State allotted appropriation revenues for FY07 represents the addition of \$693,668 in collective bargaining augmentations and \$5,610,000 and \$500,000 in health insurance premium savings transferred from the Department of Budget and Finance to perform work necessary to mitigate damages at irrigation systems resulting from the October 16, 2006, Koholo Bay Earthquake, and to perform additional work necessary to mitigate health and safety hazards at the Kailua Reservoir due to the March 2006 Flooding, respectively.

The \$665,558 in excess revenues over expenditure represents \$425,000 transferred to the Irrigation System Revolving Fund pursuant to Section 5 of Act 178, SLH 2006, as amended by Act 160, SLH 2006, \$140,558 transferred to the Hawaii Agricultural Development Revolving Fund pursuant to Section 7 of Act 178, SLH 2006, and amended by Act 160, SLH 2006, and \$100,000 transferred to the Animal Quarantine Special Fund pursuant to Section 4.3 of Act 160, SLH 2006.

The variance of \$839,753 between the final budgeted amount and the actual amount budgetary basis represents primarily \$500,000 of the \$5,610,000 in savings transferred from the Department of Budget and Finance to mitigate earthquake damages which department was instructed to lapse, \$100,000 of the \$200,000 appropriated for Hawaiian papaya deregulation information and promotion, and approximately \$200,000 in personal savings generated from vacant positions the Department was unable to fill during the year

General Fund Budgetary Highlights

Hawaii's economy saw extraordinary expansion in FY04, FY05 and FY06. In FY07, Hawaii's economy continued to expand, but at a moderate rate of about 6% before adjustment for inflation. The moderation of the economy is reflected in the lower visitor counts (a projected decline of 1.4%) and hotel occupancy rates, and the leveling off of construction and real estate activities. This moderation of the economy and the recent concern in the credit and financial markets raises uncertainty for the economy in the near future. Tax revenues reflect a moderate pace of growth with actual general fund tax collections showing a gain of only 3.4% in FY07, compared to the healthy growth of 10.9% in FY06, 16.0% in FY05, and 8.4% in FY04.

As a result of a healthy economy and general fund balance, the Legislature appropriated an additional \$2.2 million in general funds in FY07 to cover the salaries of 45 new general funded positions and related expenses for the Department to increase pest inspection activities statewide. During budget execution, the Governor provided departments with greater expenditure authority and authorized a full year allocation of general funds without restrictions. The hiring policy requiring the departments to obtain the Governor's prior approval before filling vacancies continued in FY07 and continued to have an impact on the Department's ability to readily fill vacancies.

**Department of Agriculture
State of Hawaii
Management Discussion and Analysis**

Capital Asset and Debt Administration

Capital Asset

At the end of June 30, 2007, the Department had \$73.3 million invested in a broad range of capital assets, including land, agricultural parks, buildings, equipment and motor vehicles (See Table 4 below.) This amount represents a net decrease (including additions and deductions) of \$1.0 million from last year.

**Table 4
Capital Assets at Year-end
(Net of Depreciation, in Millions)**

	<u>2007</u>	<u>2006</u>
Land	\$ 22.2	22.2
Buildings	18.9	19.9
Land improvements	15.2	15.2
Furniture and equipment	1.0	0.8
Motor vehicles	.6	.6
Construction in progress	<u>15.4</u>	<u>15.6</u>
Total	<u>\$ 73.3</u>	<u>74.3</u>

The decrease in net capital assets is primarily attributable to a net increase to accumulated depreciation over net additions to capital assets.

Debt Administration

At the end of the current fiscal year, the Department had total bonded debt outstanding of \$8.1 million backed by the full faith and credit of the State. The changes to the general obligation bond as of June 30, 2007 are as follows:

Balance at July 1, 2006	\$8,075,697
Increase	-
Decrease	188,874
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Balance at June 30, 2007	\$7,886,823

The State's total long-term debt decreased by \$0.2 million, or 2%, during the current fiscal year due to principal repayment.

Economic Factors and Next Year's Budgets and Rates

The State began FY08 as in FY07 with no general fund spending reductions. General fund revenues are still projected to grow but at a moderate rate for the duration of the four out-year planning period spanning from FY10 through FY13. At its August 28, 2007 meeting, the Council on Revenues reduced the estimated growth rates of general fund tax revenues from 6% to 5.7% in FY08, and from 4.1% to 3.8% in FY09. Revenue growth for FY10 through FY13 is projected to be in the range of 4.7% to 6.2%.

Hawaii's unemployment rate for the past three years stayed below 3% and remained among the lowest in the nation while the number of new jobs being created grew at an average rate of 2.1% during 2007. Hawaii's total personal income increased by 6.7% in the first half of 2007 and is projected to grow by 6.2% by the end of the year and by 5.9% in 2008. All these factors indicated a solid economy.

**Department of Agriculture
State of Hawaii
Management Discussion and Analysis**

For the FB 2007-2009 biennium, approximately \$1.1 million in additional general funds were appropriated each year to implement approximately \$700,000 in various long overdue repair and maintenance work and to fund approximately \$400,000 in expenses for 5 new general funded positions and related costs to prevent, control and eradicate alien species in Hawaii. In FY08, the Legislature added general fund appropriations of \$650,000 for various bee mite control projects and \$500,000 for a grant-in-aid to the Hawaii Farm Bureau Federation. The Legislature also added \$125,000 in general obligation bond funds for a capital improvement grant-in-aid to the Hawaiian Human Society.

Substantial increases in collective bargaining, specific appropriations, and grants to organizations beginning in FY07 have begun to significantly reduce the healthy general fund balance. With only a moderate growth expected in tax revenues in FY07, the general fund balance is projected to decrease to \$475.4 million at the end of FY08 and further decrease to \$213 million at the end of FY09. As a result of this economic and financial background, the Governor continued to emphasize maintaining fiscal prudence in managing public resources in the FY08 budget execution policies. While FY08 began with no general fund spending reductions, during the second half of FY08 the Governor has instructed each department to identify from their discretionary funds a 1% general fund reduction.

The Department's FY09 supplemental budget request includes no additional general fund increases but requests an increase of \$837,626 in non-general funds. Due to the lower than projected revenues, the 2008 Legislature in deliberating the FY09 supplemental budget is considering across-the-board general fund reductions to each Department's discretionary finds, reductions in vacant positions, and reductions to the executive supplemental budget requests for FY09.

Requests for Information

This financial report is designed to provide users of our report with a general overview of the Department's finances and to show the Department's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Department's Administrative Office at 1428 South King Street, Honolulu, Hawaii.

**DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
STATEMENT OF NET ASSETS
JUNE 30, 2007**

Governmental Activities

ASSETS

Cash and cash equivalent	\$	54,548,851
Receivables, net		647,419
Loans receivable, net		15,069,934
Capital assets		
Nondepreciable net assets		38,526,197
Other capital assets, net of depreciation		34,779,889

Total assets	\$	143,572,290
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LIABILITIES

Accounts payable and accrued liabilities	\$	1,378,041
Due to state general fund		6,997
Deferred revenues		306,741
Accrued vacation:		
Due within one year		1,147,027
Due in more than one year		2,258,560
Bond payable		
Due within one year		194,742
Due in more than one year		7,692,081

Total liabilities		12,984,189
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NET ASSETS (DEFICIT)

Investment in capital assets		73,306,086
Restricted for:		
Capital projects		11,946,274
Agricultural loan program		28,693,948
Other purpose		8,142,802
Unrestricted		8,498,991

Total net assets		130,588,101
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Total liabilities and net assets	\$	143,572,290
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The accompanying notes are an integral part of these combined financial statements.

**DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2007**

	Expenses	Charges For Services	Program Revenues		Net Revenue (Expense) and Changes in Net Assets
			Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
Functions/Programs					
Departmental Activities:					
Productivity improvement and management assistance	\$ 14,238,333	3,015,279	982,064	-	\$ (10,240,990)
Product development and marketing	5,069,907	440,459	89,963	-	(4,539,485)
General support for agriculture	5,467,339	2,826,001	259,668	-	(2,381,670)
Agricultural water development and irrigation services	7,056,568	1,460,463	68,097	3,647,513	(1,880,495)
Pollution control	2,017,636	720,410	279,794	-	(1,017,432)
Protection of the consumer	950,559	-	-	-	(950,559)
Aquaculture development	678,080	-	1,629	-	(676,451)
Agricultural loans	1,159,258	57,852	1,055,573	-	(45,833)
Total departmental activities	\$ 36,637,680	8,520,464	2,736,788	3,647,513	(21,732,915) (a)
General Revenues					
State allotted appropriations					35,165,354
Non-imposed employee fringe benefit					4,200,752
Intergovernmental revenues					-
Transfers					(718,012)
Total general revenues and special items					38,648,094 (a)
Other Revenue (Loss)					
Loss on disposal of fixed assets					(3,887) (a)
Change in Net Assets [sum of (a)]					
					16,911,292
Net assets, June 30, 2006					
					113,676,809
Net Assets, June 30, 2007					
					\$ 130,588,101

The accompanying notes are an integral part of these combined financial statements.

DEPARTMENT OF AGRICULTURE, STATE OF HAWAII
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2007

	General Fund	Irrigation & Drainage System Capital Projects	Financial Assistance for Agriculture	Plant Pest & Disease Control	Other Governmental Funds	Total Governmental Funds
ASSETS						
Cash	\$ 20,599,549	11,946,274	13,800,400	151,891	8,050,737	\$ 54,548,851
Loan Receivable	-	-	15,069,934	-	-	15,069,934
Total assets	\$ 20,599,549	11,946,274	28,870,334	151,891	8,050,737	69,618,785
LIABILITIES AND FUND BALANCES						
Liabilities:						
Vouchers Payable	\$ 555,647	-	-	29,219	16,304	\$ 601,170
Accrued Payroll	520,656	-	25,834	7,114	223,267	776,871
Due to State General Fund	6,997	-	-	-	-	6,997
Deferred Revenues	-	-	-	120,783	185,958	306,741
Total liabilities	1,083,300	-	25,834	157,116	425,529	1,691,779
Fund Balances(Deficit):						
Reserved for:						
Encumbrances	19,871,616	10,061,728	19,512	(45,994)	1,736,635	31,643,497
Continuing appropriation	-	1,884,546	15,385,409	40,769	5,888,573	23,199,297
Noncurrent assets	-	-	13,439,579	-	-	13,439,579
Unreserved	(355,367)	-	-	-	-	(355,367)
Total fund balances	19,516,249	11,946,274	28,844,500	(5,225)	7,625,208	67,927,006 (a)
Total liabilities and fund balances	\$ 20,599,549	11,946,274	28,870,334	151,891	8,050,737	\$ 69,618,785
Total governmental fund balances, above (a)						\$ 67,927,006
Capital assets used in governmental activities are not financial resources and therefore not reported in governmental funds						73,306,086
Receivables in the statement of activities that do not provide current financial resources are not reported in governmental funds						647,419
Some liabilities, such as compensated absences, are not due and payable in the current period and therefore not reported in governmental funds						(3,405,587)
Long term liabilities, such as bond payable, are not due and payable in the current period and therefore are not reported in governmental funds						(7,886,823)
Net assets of governmental activities						\$ 130,588,101

The accompanying notes are an integral part of these financial statements.

DEPARTMENT OF AGRICULTURE, STATE OF HAWAII
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2007

	General Fund	Irrigation & Drainage System Capital Projects	Financial Assistance for Agriculture	Plant Pest & Disease control	Other Governmental Funds	Total Governmental Funds
REVENUES						
Allotted appropriation	\$ 36,217,889	2,290,000	-	-	-	\$ 38,507,889
Intergovernmental revenues	-	1,357,512	-	680,314	720,206	2,758,032
Non-imposed employee fringe benefit	4,200,752	-	-	-	-	4,200,752
Interest on agricultural loans	-	-	531,662	-	-	531,662
Charges for services	-	-	57,852	-	8,610,525	8,668,377
Investment earnings	-	-	523,912	-	280,698	804,610
Total Revenues	40,418,641	3,647,512	1,113,426	680,314	9,611,429	55,471,322
EXPENDITURES						
Current:						
Productivity improvement and management assistance	9,248,468	-	-	685,539	3,587,312	13,521,319
Product development and marketing	4,674,543	-	-	-	373,796	5,048,339
General support for agriculture	2,417,840	-	-	-	3,069,638	5,487,478
Agricultural water development and irrigation services	2,814,503	-	-	-	1,605,877	4,420,380
Pollution control	1,241,370	-	-	-	900,342	2,141,712
Protection of the consumer	851,216	-	-	-	-	851,216
Aquaculture development	690,334	-	-	-	4,333	694,667
Agricultural loan administration	-	-	1,121,195	-	-	1,121,195
Capital outlay	-	3,646,851	-	-	-	3,646,851
Total Expenditures	21,938,274	3,646,851	1,121,195	685,539	9,541,298	36,933,157
Excess of revenue over(under) expenditure	18,480,367	661	(7,769)	(5,225)	70,131	18,538,165
Other financing sources:						
Lapsed appropriations	(1,052,535)	-	-	-	-	(1,052,535)
Operating transfers in	-	-	-	-	1,409,708	1,409,708
Operating transfers out	(665,558)	-	-	-	(244,150)	(909,708)
	(1,718,093)	-	-	-	1,165,558	(552,535)
Excess of revenues and other sources over(under) expenditures and other uses	16,762,274	661	(7,769)	(5,225)	1,235,689	17,985,630
Fund Balances - Beginning	2,753,975	11,945,613	28,852,269	-	6,389,519	49,941,376
Fund Balances - Ending	\$ 19,516,249	11,946,274	28,844,500	(5,225)	7,625,208	67,927,006

The accompanying notes are an integral part of these financial statements.

**DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGE
IN FUND BALANCE - GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2007**

Net change in fund balances - total governmental funds	\$ 17,985,630
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds	(1,006,524)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds	(147,911)
Some expenses reported in the statement of activities, such as compensated absences, do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds	(108,777)
Long term liabilities, such as bond payable, are not due and payable in the current period and therefore are not reported in the governmental funds.	188,874
<hr/> Change in net assets of governmental activities	<hr/> \$ 16,911,292

The accompanying notes are an integral part of these financial statements.

**DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
STATEMENT OF FIDUCIARY NET ASSETS
June 30, 2007**

	Private- Purpose Trusts
ASSETS	
Cash and cash equivalents	\$ 131,432
Total Assets	\$ 131,432
LIABILITIES	
Vouchers payable	\$ -
Accrued payroll	29,878
Due to others	71,784
Total Liabilities	101,662
NET ASSETS	29,770
	\$ 131,432

The accompanying notes are an integral part of these financial statements.

**DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2007**

	Private- Purpose Trust
REVENUES	
Other revenues	\$ 570,666
EXPENDITURES	
Expendable trust funds	545,308
Excess of revenues over expenditures	25,358
Net assets (deficit) at July 1, 2006	4,412
Net assets at June 30, 2007	\$ 29,770

The accompanying notes are an integral part of these financial statements.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(1) NATURE OF ORGANIZATION

The Department of Agriculture is a department of the State of Hawaii. The mission of the department is to stimulate growth in agriculture with programs that provide the foundation for agricultural enterprises to build successful businesses. The department administers and oversees programs that include plant quarantine, control of plant diseases and pests, livestock disease control, animal quarantine, agricultural park, aquaculture development, irrigation system, inspection and grading of commodities, monitoring the production and processing of milk, measurement standards, collection and dissemination of agricultural statistics and import and export statistics, granting agricultural loans, and market development and promotion of Hawaiian grown products.

The Board of Agriculture is responsible for the direction of the department's activities. The ten-member board is appointed by the governor, with the consent of the state senate, to serve a term of four years, with possible reappointment to an additional term.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting entity

The financial statements reflect only the activities of the department. The department has considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the department are such that exclusion would cause the department's financial statements to be misleading or incomplete. The Government Accounting Standards Board (GASB) has set forth criteria to be considered in determining financial accountability. The department has included in its financial statements the activities of the Agribusiness Development Corporation, a separate public instrumentality affiliated with the department for administrative purposes.

Basis of presentation

The accounting policies of the department utilized in the accompanying financial statements for the year ended June 30, 2007 conform to generally accepted accounting principles (GAAP) in the United States of America as prescribed by GASB. In June 1999, GASB issued Statement 34 - Basic Financial Statements - and Management's Discussions and Analysis - for State and Local Governments. The implementation of this statement created new major reporting requirements for state and local governments throughout the United States of America.

In conjunction with GASB Statement 34, other GASB statements are required to also be implemented. These include: Statement 33 - Accounting and Financial Reporting for Nonexchange Transactions, Statement 37 - Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus and Statement 38 - Certain Financial Statement Note Disclosures.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Government-wide financial statements

The statement of net assets and the statement of activities display information about the reporting entity (department or government as a whole). They include all funds of the reporting entity except for fiduciary funds.

The statement of activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges to customers who purchase, use, or directly benefit from goods or services provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. State allotments and other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than program revenues.

Net assets are reported in three categories: net assets invested in capital assets, net of related debt; restricted net assets; and unrestricted net assets. Net assets are restricted when constraints placed on them are either externally imposed or imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally it is the department's policy to use restricted resources first, then unrestricted resources as they are needed.

Fund financial statements

Fund financial statements of the department are organized on the basis of funds, each of which is considered to be a separate accounting entity. The department used fund accounting to report on its financial position and results of operations. Fund accounting is designed to demonstrate the legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single column.

Governmental fund types

Governmental fund types are those through which the acquisition, use and balances of the department's expendable available financial resources and the related liabilities are accounted for. The measurement focus is upon the availability and use of resources and of changes in financial position rather than upon net income determination. The following are the department's major governmental fund types:

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

General fund

The general fund is the general operating fund of the department. It is used to account for all financial activities except those required to be accounted for in another fund. The general fund presented is a part of the state's general fund and is limited only to those appropriations and obligations of the department.

Special revenue fund

Special revenue funds are used to account for the proceeds of specific revenue sources (other than expendable trust funds and major capital projects) that are legally restricted to expenditure for specified purposes.

Capital projects fund

Capital projects funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities.

Fiduciary funds

Trust and agency funds - Trust and agency funds are used to account for assets held by the department in a trustee or agency capacity. These include expendable trust funds that account for cash collected and expended by the department as trustee and agency funds that account for the cash collected and expended by the department in a custodial capacity.

Major funds

The following are the activities of the major funds accounted for in the fund financial statements:

- General fund
- Special revenue funds
- Financial assistance for agriculture - Accounts for revenues and expenditures of providing agricultural loans in the State of Hawaii.
- Plant pest and disease control - Accounts for revenues and expenditures of controlling plant pest and disease in the State of Hawaii.
- Capital projects funds
- Irrigation and drainage systems - Accounts for resources restricted for the acquisition or construction or irrigation and drainage systems.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The governmental-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. With this measurement focus, all assets and liabilities associated with the operation of these activities are included on the statement of net assets. Under the accrual basis of accounting, revenues are recorded when earned and expenses are recorded when the related liability is incurred, regardless of the timing of the related cash flows. Grant and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The fund financial statements, which include governmental funds, expendable trust funds, and agency funds, are accounted and reported using the current financial resources measurement focus and the modified accrual basis of accounting. With this measurement focus, only current assets and liabilities are generally included on the balance sheet. The revenues and expenditures represent increases and decreases in net current assets. Under the modified accrual basis of accounting, revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures are generally recognized when the related liability is incurred, except for vested but unpaid employee vacation and workers compensation benefits, which are recognized as expenditures when payable from expendable available resources.

In applying the susceptible to accrual concept to federal grant revenues, the legal and contractual requirements of the numerous individual programs are used as guidance. Under most of the department's federal programs, moneys must be expended for a specific purpose or project; therefore, revenue is recognized to the extent that expenditures are recognized.

Appropriations

Appropriations are authorizations granted by the legislature of the State of Hawaii permitting a state agency, within established fiscal and budgetary controls, to incur obligations and to make expenditures. Appropriations are allotted quarterly. The allotted appropriations lapse if not expended or encumbered at the end of the fiscal year, except for allotted appropriations related to capital improvement projects.

Encumbrances

Encumbrance accounting, under which purchase orders, contracts, and other commitments for the expenditure of resources are recorded to reserve that portion of the applicable appropriation. Encumbrances outstanding at fiscal year end are reported as reservations of fund balance since they do not constitute expenditures or liabilities and those the legislature provides specific lapsing dates.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fund balances

Reserved amounts in fund balances represent amounts that are not appropriable for expenditure or legally segregated for a specific future use. Portions of the fund balances are reserved for the following:

- Encumbrances for outstanding commitments that are generally liquidated in the subsequent fiscal year.
- Loan receivables, which are not currently available for expenditure at the balance sheet date.
- Expendable trust fund balances, which are restricted to the purpose of the account.
- Continuing appropriations for unencumbered allotment balances representing amounts that have been released and made available for encumbrance or expenditures, and are legally segregated for a specific use.

Cash and cash equivalents

Cash and cash equivalents include cash in the state treasury and cash in a Hawaii-based bank. The department's cash is held by the state treasury and pooled with funds from other state agencies and departments and deposited in approved financial institutions by the Director of Finance. At June 30, 2007, information related to the insurance and collateral of funds deposited into the state treasury was not available since such information is determined on a statewide basis and not for individual departments. Cash deposits into the state treasury are either federally insured or collateralized with obligations of the state or United States government. All securities pledged as collateral are held either by the state treasury or by the state's fiscal agents in the name of the state.

The Hawaii Revised Statutes (HRS) authorizes the Director of Finance to invest any moneys of the state, which in the Director's judgment, are in excess of the amount necessary for meeting the immediate requirements of the state.

Accounts Receivables

Receivables in the Special Revenue Funds consist primarily of amounts due from individuals for services provided to those individuals for a fee. The amounts reported as net receivables were established based on management's estimate of accounts collectible.

Loan Receivables

The department grants credit in the form of loans to farmers, all located in the State of Hawaii. Loans are collateralized by real estate, equipment, crops and other assets of borrowers. Payments

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

received are first applied against interest balances. Management discontinues accruing interest on loans after the loans are 90 days delinquent as to principal or interest. The unsecured portion of a loan and accrued interest is reserved as an allowance if payment for the loan is 90 days delinquent.

Capital assets

Capital assets (primarily land, buildings, improvements, furniture and equipment) are reported in the government-wide financial statements. Capital assets are defined by the department as those assets with estimated useful lives greater than one year and with an acquisition cost greater than:

Land - all capitalized	
Infrastructure	\$100,000
Buildings	100,000
Land improvements	100,000
Furniture and equipment	5,000
Vehicles	5,000

Purchased and constructed capital assets are valued at cost. Donated assets are recorded at their fair market value at the date of donation.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements.

Depreciation is recorded in the government-wide statement of activities. Depreciation is computed using the straight-line method over the following estimated useful lives:

Buildings	30 years
Land improvements	15 years
Furniture and equipment	7 years
Vehicles	5 years

The department began to report and depreciate new infrastructure assets effective for the year ended June 30, 2002. Infrastructure assets include irrigation and drainage systems, etc. Prior to fiscal year ended June 30, 2002, neither their historical costs nor related depreciation has historically been reported in the financial statements.

The department has elected to utilize the infrastructure transition option in the implementation of GASB Statement No. 34, Basis Financial Statements - and Management's Discussion and Analysis - for State and Local Governments, in fiscal year ending June 30, 2003 and began to implement the retroactive infrastructure provisions beginning that fiscal year.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Compensated Absence

It is the Department's policy to permit employees to accumulate earned but unused vacation and sick leave benefits. There is no liability for unpaid accumulated sick leave since sick leave is not convertible to pay upon termination of employment. All vacation pay is accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in the Governmental Funds only if they have matured, for example, as a result of employee resignations and retirements.

Long-Term Obligations

In the government-wide financial statements, long-term debt is reported as liabilities in the applicable governmental activities. Initial-issue bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective-interest method. The difference between the reacquisition price of refunding bonds and the net carrying amount of refunded debt (deferred amount on refunding) is amortized over the shorter of the life of the refunding debt or the remaining life of the refunded debt. Bonds payable are reported net of the unamortized portion of applicable premium, discount, or deferred amount on refunding. Bond issuance costs, including underwriters' discount, are reported as deferred bond issuance costs. Amortization of bond premiums or discounts, issuance costs, and deferred amounts on refunding is included in interest expense.

In the fund financial statements, Governmental Funds recognize bond premiums, discounts, and issuance costs during the period issued. The face amount of debt issued is reported as other financing sources. Premiums received are reported as other financing sources, while discounts are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Inter-fund Receivables/Payables

Reimbursements for expenditures paid by general fund on behalf of special revenue fund are classified as "due from other funds" and "due to other funds" on the governmental fund balance sheet.

Due to State of Hawaii

This account consists of reimbursements for expenditures paid by the State of Hawaii general fund on behalf of the special revenue funds.

Intra-fund and Inter-fund Transactions

Significant transfers of financial resources between activities included within the same fund are offset within that fund. Transfers of revenues from funds authorized to receive them to funds authorized to expend them have been recorded as operating transfers in the financial statements.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Grant and Deferred Revenue

Grants are recorded as intergovernmental receivables and revenues when the related expenditures are incurred. Grant funds received in advance prior to the incurrence of expenditures are recorded as deferred revenue.

Risk Management

The Department is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; and workers' compensation. A liability for a claim is established if information indicates that it is probable that a liability has been incurred at the date of the basic financial statements and the amount of the loss is reasonably estimable.

Deferred Compensation Plan

The State offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all state employees, permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

All plan assets are held in a trust fund to protect them from claims of general creditors. The State has no responsibility for loss due to the investment or failure of investment of funds and assets in the plan, but does have the duty of due care that would be required of an ordinary prudent investor. Accordingly, the assets and liabilities of the State's deferred compensation plan are not reported in the accompanying basic financial statements.

Use of Estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

(3) CASH AND CASH EQUIVALENTS

At June 30, 2007, the carrying amount of the department's cash and cash equivalents was \$54,548,851, which approximates the bank balance.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(4) LOANS RECEIVABLE

At June 30, 2007, loans receivable consisted of the following:

	Special Revenue
Hawaii Agriculture Loan Program	\$15,728,469
Hawaii Aquaculture Loan Program	908,038
Accrued interest	539,689
	17,176,196
Less allowance for doubtful receivables	2,106,262
	\$15,069,934

(5) ACCOUNTS RECEIVABLE

At June 30, 2007, accounts receivable consisted of the following:

Waiahole Water System	\$ 118,894
Lease Rental of Public Land	215,880
Sale of Water	354,290
Quarantine Fee	800,990
	1,490,054
Less allowance for doubtful receivables	842,635
	\$ 647,419

Approximately \$1,135,000 of the \$1,490,000 total receivable balance was over 90 days old.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(6) CAPITAL ASSETS

The changes to capital assets as of June 30, 2007 are as follows:

	Balance at July 1, 2006	Additions	Disposals and Transfers In (Out)	Ending Balance June 30,2007
<i>Capital Assets Being Depreciated</i>				
Land improvements	52,024,223	-	2,544,486	54,568,709
Buildings	29,157,609	-	(90,337)	29,067,272
Vehicles	2,945,234	145,257	(44,897)	3,045,594
Equipment	4,438,579	418,433	16,863	4,873,875
	88,565,645	563,690	2,426,115	91,555,450
Less accumulated depreciation				
Land improvements	37,719,324	2,558,258	-	40,277,582
Land improvements - not depreciable	-	-	-	-
Buildings	9,258,030	942,485	(19,492)	10,181,023
Vehicles	2,335,992	246,369	(113,447)	2,468,914
Equipment	3,614,217	248,053	(14,228)	3,848,042
	52,927,563	3,995,165	(147,167)	56,775,561
Subtotal	35,638,082	(3,431,475)	2,573,282	34,779,889
<i>Capital Assets Not Being Depreciated</i>				
Land	22,188,079	-	1	22,188,080
Land improvements - not depreciable	911,262	-	-	911,262
Construction in progress	15,575,186	3,859,500	(4,007,831)	15,426,855
Subtotal	38,674,527	3,859,500	(4,007,830)	38,526,197
Total capital assets	74,312,609	428,025	(1,434,548)	73,306,086

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(6) CAPITAL ASSETS (continued)

Depreciation expense for the year ended June 30, 2007 was charged to governmental activities as follows:

Agricultural water development and irrigation services	\$ 2,614,258
Productivity improvement and management assistance	742,328
General support for agriculture	234,256
Protection of the consumer	170,385
Product development and marketing	131,307
Pollution control	58,317
Agricultural loans	32,444
Aquaculture development	11,870
	\$ 3,995,165

The department adopted a new capitalization policy effective July 01, 2001. Furniture and equipment purchases are capitalized when greater than \$5,000 and buildings and land improvements are capitalized when greater than \$100,000.

(7) GENERAL OBLIGATION BOND

Pursuant to Act 111, SLH 1998, reimbursable general obligation bonds of \$8,500,000 were issued in 2001 and \$91,988 in other years to fund the acquisition of the Waiahole Water System. Section 14, Part IV of ACT 111, SLH 1998, requires the Agribusiness Development Corporation (ADC) to reimburse the general fund in accordance with a schedule determined by the Director of Finance, with the approval of the governor. The term of the bonds is 34 years with an interest rate of 3.00%. The principal repayment is due annually and the accrued interest is due semi-annually. The interest expense for the year ended June 30, 2007 approximated to \$245,000.

The changes to the general obligation bond as of June 30, 2007 are as follows:

Balance at July 1, 2006	\$8,075,697
Increase	-
Decrease	188,874
	\$7,886,823
Balance at June 30, 2007	\$7,886,823

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(7) GENERAL OBLIGATION BOND (continued)

Future bond principal repayment and interest payment for fiscal year ending after June 30, 2007 are as follows:

	Principal	Interest
2008	\$ 194,742	\$ 238,719
2009	200,794	232,626
2010	208,184	226,310
2011	210,070	219,873
2012	216,551	213,341
2013	224,864	206,556
2014	230,206	199,546
Thereafter	6,401,412	2,248,378
	\$7,886,823	\$3,785,349

(8) NON-IMPOSED EMPLOYEE FRINGE BENEFITS

Payroll fringe benefit costs of the department's employees funded by general fund appropriations are assumed by the state and are not charged to the department's operating funds. These costs, totaling \$4,200,752, have been reported as revenues and expenditures in the department's financial statements for the fiscal year ended June 30, 2007.

Payroll fringe benefit costs related to federally funded salaries are not assumed by the state and are recorded as expenditures in the department's financial statements.

(9) LEASES

The department, as lessor, has non-cancelable lease agreements for parcels of agricultural land located throughout the State of Hawaii. The lease agreements have minimum and, where applicable, additional rent based on a percentage of revenues and terms of up to 55 years. Minimum future lease revenue for fiscal year ending after June 30, 2007 approximates as follows:

2008	\$ 823,000
2009	822,000
2010	803,000
2011	801,000
2012	785,000
Thereafter	15,425,000
	\$19,459,000

Rental income from leases for parcels of agricultural land for the fiscal year ended June 30, 2007 totaled \$612,150, including \$22,536 for additional rent based on percentage of revenues.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(10) FUND BALANCE DEFICITS

The general fund had a deficit in the unreserved fund balance at June 30, 2007, of \$355,367. The deficit resulted primarily from expenditures being recorded on the accrual basis when incurred, and revenues being recognized only when the funds are measurable and available.

(11) VACATION

The changes to the general long-term debt compensated absences as of June 30, 2007 approximated the following:

Balance at July 1, 2006	\$3,296,810
Increase	108,777
Decrease	-
Balance at June 30, 2007	\$3,405,587

Compensated absences liabilities will be liquidated primarily by the general fund. In the past, approximately 80% has been paid by the general fund and the remainder by various other governmental funds.

(12) RETIREMENT BENEFITS

Retirement Plan Description

Substantially all eligible employees of the Department are required by Chapter 88 to become members of the Employees' Retirement System of the State of Hawaii (ERS), a cost-sharing multiple-employer public employee retirement plan. The ERS provides retirement benefits as well as death and disability benefits. The ERS is governed by a Board of Trustees. All contributions, benefits, and eligibility requirements are established by HRS Chapter 88 and can be amended by legislative action. The ERS publishes a comprehensive annual financial report that is available to the public. That report may be obtained by writing to the ERS, 201 Merchant Street, Suite 1400, Honolulu, Hawaii 96813.

Prior to June 30, 1984, the plan consisted of only a contributory option. In 1984, legislation was enacted to add a new noncontributory option for members of the ERS who are also covered under Social Security. Persons employed in positions not covered by Social Security are precluded from the noncontributory option. The noncontributory option provides for reduced benefits and covers most eligible employees hired after June 30, 1984. Employees hired before that date were allowed to continue under the contributory option or to elect the new noncontributory option and receive a refund of employee contributions.

All benefits vest after five and ten years of credited service under the contributory and noncontributory options, respectively.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(12) RETIREMENT BENEFITS (continued)

Both options provide a monthly retirement allowance based on the employee's age, years of credited service, and average final compensation (AFC). The AFC is the average salary earned during the five highest paid years of service, including the vacation payment, if the employee became a member prior to January 1, 1971. The AFC for members hired on or after that date is based on the three highest paid years of service, excluding the vacation payment.

On July 1, 2006, a new hybrid contributory option became effective pursuant to Act 179, SLH 2004. Members in the hybrid option are eligible for retirement at age 62 with 5 years of credited service or age 55 and 30 years of credited service. Members receive a benefit multiplier of 2% for each year of credited service in the hybrid option. The benefit payment options are similar to the current contributory option. Most of the new employees hired from July 1, 2006 are required to join the hybrid option.

Funding Policy

Most covered employees of the contributory option are required to contribute 7.8% of their salary. Police officers, firefighters, investigators of the departments of the County Prosecuting Attorney and the Attorney General, narcotics enforcement investigators, and public safety investigators are required to contribute 12.2% of their salary. The funding method used to calculate the total employer contribution requirement is the Entry Age Normal Actuarial Cost Method. Effective July 1, 2005, employer contribution rates are a fixed percentage of compensation, including the normal cost plus amounts required to pay for the unfunded actuarial accrued liability.

Based on the most recent information available, the State contributed 100% of its required contributions for the years June 30, 2006, 2005 and 2004. Required contributions are not available on a departmental basis. State-wide contribution requirements for the years June 30, 2006, 2005 and 2004, as well as covered payroll information, are included in the ERS comprehensive annual financial report referred to earlier.

Post-Retirement Health Care and Life Insurance Benefits

In addition to providing pension benefits, the State, pursuant to HRS Chapter 87, provides certain health care and life insurance benefits to all qualified employees.

For employees hired before July 1, 1996, the State pays the entire monthly health care premium for employees retiring with ten or more years of credited service, and 50% of the monthly premium for employees retiring with fewer than ten years of credited service.

For employees hired after June 30, 1996, and who retire with fewer than 10 years of service, the State makes no contributions. For those retiring with at least 10 years but fewer than 15 years of service, the State pays 50% of the retired employees' monthly Medicare or non-Medicare premium. For employees hired after June 30, 1996, and who retire with at least 15 years but fewer than 25 years of service, the State pays 75% of the retired employees' monthly Medicare or non-Medicare premium; for those retiring with over 25 years of service, the State pays the entire health care premium.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(12) RETIREMENT BENEFITS (continued)

Free life insurance coverage for retirees and free dental coverage for dependents under age 19 are also available. Retirees covered by the medical portion of Medicare are eligible to receive reimbursement of the basic medical coverage premium. Contributions are financed on a pay-as-you-go basis. Information regarding expenditures for post-retirement health care and life insurance benefits is included in the ERS comprehensive annual report.

Effective July 1, 2003, the Hawaii Employer-Union Health Benefit Trust Fund (EUTF) replaced the Hawaii Public Employees Health Fund under Act 88, SLH of 2001. The EUTF was established to provide a single delivery system of health benefits for state and county employees, retirees, and their dependents.

(13) COMMITMENTS AND CONTINGENCIES

A. Commitments

General Obligation Bonds

The Department has issued general obligation bonds in which repayments, including interest, are reimbursed from specific revenue sources of the Waiahole Water System Revolving Fund with terms corresponding to that of the related general obligation bonds (see note 8). At June 30, 2007, outstanding commitments to repay general obligation bonds approximated \$7,886,823.

Accumulated Sick Leave

Sick leave accumulates at the rate of one and three-quarters working days for each month service without limit. It can be taken only in the event of illness and is not convertible to pay upon termination of employment. However, a state employee who retires or leaves government service in good standing with sixty days or more of unused sick leave is entitled to additional service credit in the Employee's Retirement System. Accumulated sick leave at June 30, 2007 approximated \$12,163,312.

B. Contingencies

The Department has been named as defendant in a few lawsuits and claims arising in the normal course of operations. Losses not covered by insurance are typically paid through an appropriation from the State's General Fund. Accordingly, the management of the Department is of the opinion that the outcome of these lawsuits and claims will not have a material adverse effect on the financial position of the Department.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(14) Risk Management

The Department is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; and workers' compensation, however, the State has property crime and other liability insurance policies in force through various outside insurance carriers to mitigate this risk. The State generally retains the risk of losses up to deductible amounts per occurrence, and for amounts over the coverage limits. Losses not covered by the insurance policies are paid by DAGS' State Risk Management Revolving Fund (the Fund) or through Legislative Appropriations.

The State has real and personal property insurance covering all risk of direct physical loss including named hurricanes, flood and earthquakes, and terrorism with various limits of loss and deductible amounts.

The State has excess general liability insurance covering bodily injury and property damage, automobile and watercraft liability, public errors and omissions liability and employment practices and employee benefits liability. The State generally self-insures its automobile no-fault and workers' compensation losses. The DAGS' State Risk Management and Insurance Administration handle the State's property and automobile insurance claims. Losses from these claims are generally paid from the Fund. The State administers its workers' compensation losses through another department. A liability for a claim is established if information indicates that a liability has been incurred at the date of the basic financial statements and the amount of the loss can be reasonably estimated.

DAGS' State Risk Management and Insurance Administration handle tort claims of \$10,000 or less for most departments of the State and automobile liability claims of \$15,000 or less and pays these claims from the Fund. Claims over \$10,000 are handled by the State Department of the Attorney General. Deductibles for property losses are covered through the Fund.

(15) TRANSFERS

For the year ended June 30, 2007, transfers by fund were as follows:

<u>Transfer From:</u>	<u>Transfer To:</u>	<u>Amount</u>
General fund	Irrigation System Revolving Fund	\$ 425,000
General fund	Hawaii Agriculture Development Revolving Fund	140,558
General fund	Animal Quarantine Special Fund	100,000
		<hr/>
		\$ 665,558

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Notes to Financial Statements
June 30, 2007

(15) TRANSFERS (continued)

The general fund transferred \$425,000 to the Irrigation System Revolving Fund pursuant to Section 5 of Act 178, SLH 2005, as amended by Act 160, SLH 2006, \$140,558 to the Hawaii Agricultural Development Revolving Fund pursuant to Section 7 of Act 178, SLH 2005, as amended by Act 160, SLH 2006, and \$100,000 to the Animal Quarantine Special Fund pursuant to Section 4.3 of Act 160, SLH 2006. The Department of Land and Natural Resources transferred \$500,000 for the Croqui Frog Eradication and Control and the net fixed assets transferred and disposed of approximated \$2,573,000.

Required Supplementary Information

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
(Budget and actual) - General Fund
For the Year Ended June 30, 2007

	Budgeted Amount		Actual Amount Budgetary Basis	Variance with Final Budget Positive (Negative)
	Original	Final		
Budgetary fund balance at June 30, 2006	\$ -	\$ -	\$ -	\$ -
<i>Revenues</i>				
State allotted appropriation	17,403,221	24,206,889	24,206,889	-
Intergovernmental	-	-	-	-
Total Revenues	17,403,221	24,206,889	24,206,889	-
<i>Expenditures</i>				
Productivity improvement and management assistance	8,055,579	8,412,596	8,278,443	134,153
Product development and marketing	4,516,339	4,540,158	4,416,113	124,045
General support for agriculture	1,964,128	2,093,912	2,092,698	1,214
Agricultural water development and irrigation services	137,417	6,306,349	5,800,828	505,521
Pollution control	836,705	906,529	857,078	49,451
Protection of the consumer	674,481	682,068	674,433	7,635
Aquaculture development	553,014	599,719	581,985	17,734
Total Expenditures	16,737,663	23,541,331	22,701,578	839,753
Excess of revenue over(under) expenditure	665,558	665,558	1,505,311	(839,753)
<i>Other financing sources:</i>				
Operating transfers in				
Operating transfers out	(665,558)	(665,558)	(665,558)	-
Excess of revenues and other sources over(under) expenditures and other uses	-	-	839,753	(839,753)
Lapsed appropriations	-	-	(839,753)	839,753
Budgetary fund balance at June 30, 2007	\$ -	\$ -	\$ -	\$ -

The accompanying notes are an integral part of these financial statements.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Budgetary Comparison Schedule
Special Revenue Funds
For the Year Ended June 30, 2007

	Budgeted Amounts		Actual Amounts Budgetary Basis	Variance with Final Budget Positive (Negative)
	Original	Final		
Financial Assistance for Agriculture				
<i>Revenues</i>				
Current-year appropriations	\$ 6,054,203	\$ 6,096,203	\$ 1,113,425	\$ (4,982,778)
<i>Expenditures</i>				
Agricultural Loans	6,054,203	6,096,203	1,088,592	5,007,611
<hr/>				
<i>Excess of revenues and other sources over (under) expenditures and other uses</i>	\$ -	\$ -	\$ 24,833	\$ 24,833
<hr/>				
Plant and Pest Disease Control				
<i>Revenues</i>				
Current-year appropriations	\$ 620,621	\$ 634,889	\$ 599,444	\$ (35,445)
Current-year funds	-	-	-	-
<i>Expenditures</i>				
Productivity improvement and management	620,621	634,889	682,982	(48,093)
<hr/>				
<i>Excess of revenues and other sources over (under) expenditures and other uses</i>	\$ -	\$ -	\$ (83,538)	\$ (83,538)

The accompanying notes are an integral part of the financial statements.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Budgetary Comparison Schedule
Budget to GAAP Reconciliation
For the Year Ended June 30, 2007

	General Fund	Financial Assistance for Agriculture	Plant Pest and Disease Control
Excess of revenues and other sources over (under) expenditures and other uses - actual on budgetary basis	\$ 839,753	\$ 24,833	\$ (83,538)
Reserved for encumbrances at fiscal year-end	19,871,616	19,512	-
Revenue and expenditure accruals for the year not recognized for budgetary purposes, net of prior year accruals	351,131	8,363	83,538
Lapsed appropriations	(1,052,535)	-	-
Expenditures for prior fiscal years' encumbrances	(3,247,691)	(60,477)	
Excess of revenues and other sources over (under) expenditures and other uses - GAAP basis	\$ 16,762,274	\$ (7,769)	\$ -

The accompanying notes are an integral part of the financial statements.

Compliance Audit

Department of Agriculture
State of Hawaii
Schedule of Expenditures of Federal Awards
For Year Ended June 30, 2007

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Grant Number	Expenditures
<u>Department of Agriculture (USDA)</u>			
Cooperative National Plant Pest Survey and Detection	10.025	05-8510-0586-CA	\$ 121,348
Survey and Detection of the Red Imported Fire Ant in Hawaii		05-8510-0666-CA	6,569
Detection Surveys for Papaya Mealybug in Hawaii		05-8510-0794-CA	29,296
Survey for Giant Salvinia and Fireweed in Hawaii		04-8510-0793-CA	6,618
Survey for Glassy-Winged Sharpshooter in Hawaii		05-8510-0874-CA	33,693
Seed Inspection Services		P.O. #45-9147-6-9990	2,500
Voluntary Scrapie Flock Certification		05-9715-1572-CA	9,930
Voluntary Johne's Disease Herd Status Program		05-9715-1422-CA	43,527
Foreign Animal Disease Surveillance, Bovine Spongiform Encephalopathy Surveillance, Animal Emergency Management		05-9715-1487-CA	527
Swine Health Protection		05-9715-1448-CA	17,328
National Animal Identification System Implementation		07-9715-1480-CA	68,788
Live Bird Market Surveillance - Highly Pathogenic Avian Influenza Virus		06-9715-1614-CA	38,320
Molokai Bovine TB Mitigation		06-9715-1726-CA	15,997
HI Brown Tree Snake Detector Program		05-73-15-5388-GR	249,410
Biotechnology Program Development		05-2000-0027-GR	13,719
			657,570
Shell Egg Surveillance	10.162	12-25-A-3310	13,022
An Agricultural Market Information System for Small Farm Decision-Making in Hawaii	10.156	12-25-G-0303	27,875
Cooperative Pesticide Recordkeeping	10.163	12-25-A-4615	5,226
National Organic Certification Cost-Share Program		12-25-A-4460	3,970
			9,196
Economic Assessment of Select HI Agricultural Exports		12-25-G-0383	5,415
Disease Management in Pacific Aquaculture	10.200	2003-38500-13092	-
Exploration for Biological Control of Melon Fly in Indo-Malayan Region	10.001	58-5320-1-530	17,073
Upcountry Maui Watershed	10.904	65-9251-3-615	7,525
		69-9251-3-643	201,628
		69-9251-4-669	370,629
		69-9251-5-701	63,340
			643,122
Lower Hamakua Watershed, Hawaii	10.904	65-9251-1-565	2,500
		69-9251-2-602	3,377
		65-9251-3-616	2,400
		69-9251-3-624	21,039

Department of Agriculture
State of Hawaii
Schedule of Expenditures of Federal Awards
For Year Ended June 30, 2007

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Grant Number	Expenditures
		69-9251-3-625	26,725
		65-9251-4-671	14,480
		65-9251-4-699	487,019
			<u>557,540</u>
Plantation Irrigation Drainage Systems	10.904	68-9251-5-703	<u>75,000</u>
<u>Environmental Protection Agency (EPA)</u>			
Pesticide Enforcement	66.700	E-00915906	235,200
Pesticide Certification		E-00941906	33,197
			<u>268,397</u>
<u>Department of Commerce</u>			
Voluntary Inspection Services for Fish and Fishery Products		45ABNA0B1070	<u>1,746</u>
<u>Department of Interior</u>			
Office of Insular Affairs - Research and Development for the Brown Tree Snake	15.875	2005-2007 Interior Appropriation Acts	<u>202,756</u>
Bureau of Reclamation - Hawaii Water Resources Study	15.504	05-FC-300014	80,364
Hawaii State Irrigation Systems Water Conservation Improvement Study		06-FG-300021	22,526
			<u>102,890</u>
PASSTHROUGH GRANTS			
<u>Department of Homeland Security</u>			
Office for Domestic Preparedness	97.067	2005-GE-T5-0034	<u>23,605</u>
<u>Federal Emergency Management Agency</u>			
Hawaii State Dept. of Defense - Civil Defense		FEMA-1640-DR-HI	<u>177,603</u>
Total Expenditures of Federal Awards			<u>\$ 2,782,810</u>

Note: This Schedule of Expenditures of Federal Awards was prepared on accrual basis of accounting.



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

To the Board of Agriculture
State of Hawaii

We have audited the financial statements of the Department of Agriculture of the State of Hawaii, as of and for the year ended June 30, 2007, and have issued our report thereon dated March 8, 2008. We conducted our audit 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.

Compliance

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 grants, including applicable provisions of the Hawaii 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 our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the department's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Board of Agriculture, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Hullari & Co., CPAs, Inc.

Honolulu, Hawaii
March 8, 2008



**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH *OMB CIRCULAR A-133***

To the Board of Agriculture
State of Hawaii

Compliance

We have audited the compliance of Department of Agriculture with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2007. The department's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the department's management. Our responsibility is to express an opinion on the department's compliance based on our audit.

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 OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 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 the department'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. Our audit does not provide a legal determination of the department's compliance with those requirements.

In our opinion, the department complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2007.

Internal Control Over Compliance

The management of the department is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the department's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management of the State of Hawaii Department of Agriculture, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Attari & Co., CPAs, Inc.

Honolulu, Hawaii
March 8, 2008

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007

A. SUMMARY OF AUDITORS' RESULTS

1. Financial Statements

- Unqualified opinion issued on the financial statements.
- No material weaknesses in internal control over financial reporting were disclosed.
- Reportable conditions in internal control over financial reporting were disclosed.
- No material noncompliance to the financial statements was disclosed.

2. Federal Awards

- No material weaknesses in internal control over major programs were disclosed.
- No reportable condition in internal control over major programs was disclosed.
- Unqualified opinion issued on compliance for major programs.
- There were no audit findings required to be reported under OMB Circular A-133 Section 510 (a).

Identification of major programs:

<u>CFDA Number</u>	<u>Federal Program</u>
10.904	Watershed Protection and Flood Protection
10.504	Water Study

- Threshold used to distinguish between Type A and Type B programs was \$300,000.
- The Department did not qualify as a low-risk auditee.

B. FINANCIAL STATEMENT FINDINGS

07-1 Tracking construction in progress.

Criteria: Records supporting construction in progress for capital projects need to be maintained and reconciled to FAMIS on a monthly basis to ensure accuracy and completeness of costs for periodic reporting purposes as well as for transfer of costs upon completion of projects.

Condition: The department does not maintain adequate records of projects in progress and, therefore, no reconciliation to FAMIS as contracts progress.

Effect: The failure to adequately maintain adequate records and to reconcile projects costs to FAMIS increases the risk that errors could occur and not be detected in a timely manner.

Recommendation: Management needs to ensure that costs associated with projects in progress are controlled with the use of a subsidiary accounting record, by project, updated monthly, reconciled to FAMIS, and reviewed by supervisory personnel..

07-2 Internal records are not reconciled to FAMIS on a monthly basis.

Criteria: Subsidiary records supporting the FAMIS system account balances need to be reconciled on a periodic basis to insure that both the details of the subsidiary records and the FAMIS balances are accurate and reliable.

Condition: The department does not reconcile loan division master lists to FAMIS reports on a monthly basis. This condition was cited in the prior year audit.

Effect: Increases risk that errors or other discrepancies could occur and not be detected in a timely manner.

Recommendation: Establish policy to require monthly reconciliation of the loan master lists to the corresponding items in FAMIS. A simple reconciliation reflecting the master list balance, reconciling items (differences) to FAMIS balances, and the actual FAMIS balance should be documented each month, similar to reconciling a checkbook cash balance to a bank statement balance. The division should monitor and

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007

review the reconciliations to ensure monthly reconciliations are properly conducted according to the policy.

C. FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

None

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Summary Schedule of Prior Year Findings and Questioned Costs
Year Ended June 30, 2007

A. FINANCIAL STATEMENT FINDINGS

06-1 Loan files not properly maintained.

Condition: Insurance on loan collateral should be maintained by the borrower and documented in the files.

Status: Resolved

06-2 Required inspections are not documented.

Condition: According to the loan division's policies and procedures manual, initial on-farm visits should be performed within three months of loan disbursement and the subsequent visits should be limited to twice annually. Farm visits should be documented with a loan servicing report. Tests of loan files disclosed a lack of documentation pertaining to this requirement.

Status: Resolved

06-3 Internal records are not reconciled to FAMIS on a monthly basis.

Condition: The department does not reconcile loan division master lists (loan trial balance) to FAMIS reports on a monthly basis.

Status: Not resolved. Monthly reconciliations still not performed. See finding 07-2

Response of the Department of Agriculture

LINDA LINGLE
Governor



SANDRA LEE KUNIMOTO
Chairperson, Board of Agriculture

DUANE K. OKAMOTO
Deputy to the Chairperson

State of Hawaii
DEPARTMENT OF AGRICULTURE
1428 South King Street
Honolulu, Hawaii 96814-2512
Phone: (808) 973-9600 Fax: (808) 973-9613

March 20, 2007

Hattori & Co., CPAs, Inc.
1750 Kalakaua Avenue, Suite 1904
Honolulu, HI 96826

Gentlemen:

Thank you for the opportunity to review and provide comments on the draft report of the Financial and Compliance Audit of the Department of Agriculture for the fiscal year ended June 30, 2006

We appreciate the cooperative and professional manner in which the Hattori & Co. staff conducted themselves during this audit.

Please feel free to call Elaine Abe of my staff at 973-9606 if there are any questions, or if additional information is needed.

Sincerely,

A handwritten signature in black ink, appearing to read "Sandra Lee Kunimoto".

Sandra Lee Kunimoto, Chairperson
Board of Agriculture

Enclosure

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007

B. FINANCIAL STATEMENT FINDINGS

07-1 Tracking construction in progress.

Criteria: Records supporting construction in progress for capital projects need to be maintained and reconciled to FAMIS on a monthly basis to ensure accuracy and completeness of costs for periodic reporting purposes as well as for transfer of costs upon completion of projects.

Condition: The department does not maintain adequate records of projects in progress and, therefore, no reconciliation to FAMIS as contracts progress.

Effect: The failure to adequately maintain adequate records and to reconcile projects costs to FAMIS increases the risk that errors could occur and not be detected in a timely manner.

Recommendation: Management needs to ensure that costs associated with projects in progress are controlled with the use of a subsidiary accounting record, by project, updated monthly, reconciled to FAMIS, and reviewed by supervisory personnel.

Response: The Division will follow internal procedures established to record capital improvement projects as fixed assets in the State's inventory system. These procedures require an activity/project code be established in FAMIS for each project. This will allow the division to track expenditures by project, reconcile monthly to FAMIS reports, record the fixed asset on the State's inventory system when project completed, and provide data on construction projects in progress for financial reporting purposes.

07-2 Internal records are not reconciled to FAMIS on a monthly basis.

Criteria: Subsidiary records supporting the FAMIS system account balances need to be reconciled on a periodic basis to insure that both the details of the subsidiary records and the FAMIS balances are accurate and reliable.

Condition: The department does not reconcile loan division master lists to FAMIS reports on a monthly basis. This condition was cited in the prior year audit.

DEPARTMENT OF AGRICULTURE
STATE OF HAWAII
Schedule of Findings and Questioned Costs
Year Ended June 30, 2007

Effect: Increases risk that errors or other discrepancies could occur and not be detected in a timely manner.

Recommendation: Establish policy to require monthly reconciliation of the loan master lists to the corresponding items in FAMIS. A simple reconciliation reflecting the master list balance, reconciling items (differences) to FAMIS balances, and the actual FAMIS balance should be documented each month, similar to reconciling a checkbook cash balance to a bank statement balance. The division should monitor and review the reconciliations to ensure monthly reconciliations are properly conducted according to the policy.

Response: As recommended in the prior year's audit, the Division established a written policy requiring monthly reconciliation of the loan master lists to FAMIS balances. However, actual monthly reconciliation of the loan master lists to FAMIS balances were not performed because the Division was trying to determine if the difference amount between the loan master list balance and FAMIS balance was consistent. During the period from July 2007 through March 2008, a period of nine (9) months, the difference amount has remained steady. The Division will utilize this difference amount to perform monthly reconciliations between the loan master lists and the FAMIS reports.

C. FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

None