

HHT Committee

From: Monique Yamashita <Monique.Yamashita@khako.org>
Sent: Wednesday, August 16, 2017 3:46 PM
To: HHT Committee
Subject: RE: KHAKO Response: KHAKO Westside Shelter HHT-20
Attachments: 2015 Audit Report.pdf

Attention Councilmember Crivello:

In preparation for tomorrow's Committee meeting, please see that attached 2015 Financial Statement for KHAKO. The 2016 Financial Statement is in the final approval stage and should be available to the committee by the end of August 2016.

Sincerely,

Monique R. Yamashita, MSW | Chief Executive Officer
Ka Hale A Ke Ola Homeless Resource Centers, Inc.
670 Waiale Road
Wailuku, HI 96793
Ph: (808) 446-8133
www.khako.org

"Breaking the Cycle of Homelessness"

From: Monique Yamashita
Sent: Tuesday, August 15, 2017 4:32 PM
To: 'HHT.Committee@mauicounty.us' <HHT.Committee@mauicounty.us>
Subject: KHAKO Response: KHAKO Westside Shelter HHT-20

Attn: Councilmember Stacy Crivello, Chair

Monique R. Yamashita | Chief Executive Officer
Ka Hale A Ke Ola Homeless Resource Centers, Inc.
670 Waiale Road
Wailuku, HI 96793
Ph: (808) 446-8133
www.khako.org

"Breaking the Cycle of Homelessness"

KA HALE A KE OLA HOMELESS RESOURCE CENTERS, INC.

**FINANCIAL STATEMENTS AND SUPPLEMENTARY
INFORMATION WITH INDEPENDENT AUDITOR'S REPORTS**

Year Ended December 31, 2015



N&K CPAs, Inc.
ACCOUNTANTS|CONSULTANTS

AMERICAN SAVINGS BANK TOWER | 1001 BISHOP STREET, SUITE 1700 | HONOLULU, HAWAII 96813-3696
T (808) 524-2255 **F** (808) 523-2090 | nkcpa.com

KA HALE A KE OLA HOMELESS RESOURCE CENTERS, INC.

TABLE OF CONTENTS

	<u>Page</u>
PART I FINANCIAL SECTION	
Independent Auditor's Report	4 - 6
Financial Statements	
Statement of Financial Position	7
Statement of Activities	8
Statement of Cash Flows	9
Notes to Financial Statements	10 - 22
Supplementary Information	
Schedule of Contracts with the Homeless Programs Office, Department of Human Services of the State of Hawaii	24
Schedule of Contracts with the Benefit, Employment and Support Services Division Department of Human Services of the State of Hawaii	25
PART II REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS	
Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	27 - 28
PART III SCHEDULE OF FINDINGS AND RESPONSES	30
PART IV SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS	
Status Report	32

PART I
FINANCIAL SECTION

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Ka Hale A Ke Ola Homeless Resource Centers, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of Ka Hale A Ke Ola Homeless Resource Centers, Inc. (a nonprofit organization), which comprise the statement of financial position as of December 31, 2015, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Ka Hale A Ke Ola Homeless Resource Centers, Inc. as of December 31, 2015, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter Regarding Going Concern

The accompanying financial statements have been prepared assuming that Ka Hale A Ke Ola Homeless Resource Centers, Inc. will continue as a going concern. As discussed in Note L to the financial statements, Ka Hale A Ke Ola Homeless Resource Centers, Inc. has sustained net losses from operations over the years which have negatively impacted its financial position. At December 31, 2015, Ka Hale A Ke Ola Homeless Resource Centers, Inc.'s current liabilities exceeded its current assets by approximately \$5,539,800. As of December 31, 2015, this deficit in working capital resulted in the inability to make required debt service payments. These conditions raise substantial doubt about Ka Hale A Ke Ola Homeless Resource Centers, Inc.'s ability to continue as a going concern. Management's plans regarding those matters are also described in Note L. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

Other Matters

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedules of contracts with the Homeless Programs Office and with the Benefit, Employment and Support Services Division of the Department of Human Services of the State of Hawaii, as required by the State of Hawaii, are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required By *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 2, 2016, on our consideration of Ka Hale A Ke Ola Homeless Resource Centers, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Ka Hale A Ke Ola Homeless Resource Centers, Inc.'s internal control over financial reporting and compliance.

N&K CPAs, Inc.

Honolulu, Hawaii
September 2, 2016

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
STATEMENT OF FINANCIAL POSITION
December 31, 2015

ASSETS

CURRENT ASSETS

Cash and cash equivalents	\$ 409,506
Grants receivable	216,740
Tenants receivable, net of allowance for bad debts of \$366,712	34,448
Prepaid expenses	60,790
Total current assets	<u>721,484</u>

PROPERTY AND EQUIPMENT

Shelter facilities	39,928,595
Shelter furnishings	914,674
Office furniture and equipment	667,393
Vehicles	96,150
	<u>41,606,812</u>
Less accumulated depreciation and amortization	<u>22,514,764</u>
	<u>19,092,048</u>

OTHER ASSETS

Southside conditional contribution	1,540,000
Restricted cash and cash equivalents	748,033
Restricted certificates of deposit	244,011
Restricted investments	7,956
Tenant security deposits	182,351
	<u>2,722,351</u>
	<u>\$ 22,535,883</u>

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES

Construction loan payable	\$ 4,000,000
Current portion of note payable	157,069
Accounts payable	187,020
Accrued liabilities	185,246
Interest payable	1,684,079
Deferred grant revenue	47,845
Total current liabilities	<u>6,261,259</u>

NONCURRENT LIABILITIES

Deferred revenue - conditional contribution	1,540,000
Tenant security deposits	182,351
Note payable, less current maturities	2,842,931
	<u>4,565,282</u>
Total liabilities	<u>10,826,541</u>

NET ASSETS

Unrestricted	10,709,342
Permanently restricted	1,000,000
	<u>11,709,342</u>
	<u>\$ 22,535,883</u>

See accompanying notes to financial statements.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
STATEMENT OF ACTIVITIES
Year Ended December 31, 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUE AND OTHER SUPPORT				
Grants from governmental agencies	\$ 2,515,462	\$ --	\$ --	\$ 2,515,462
Program fees	625,830	--	--	625,830
General contributions	162,475	--	--	162,475
Interest and dividend income	2,718	--	--	2,718
Fundraising income	9,641	--	--	9,641
Rental income	2,420,108	--	--	2,420,108
Gain from extinguishment of debt	5,438,638	--	--	5,438,638
Other	<u>231,907</u>	<u>--</u>	<u>--</u>	<u>231,907</u>
Total revenue and other support	<u>11,406,779</u>	<u>--</u>	<u>--</u>	<u>11,406,779</u>
EXPENSES				
Program services				
Shelter operations	4,497,598	--	--	4,497,598
Education, training, and social services	<u>996,244</u>	<u>--</u>	<u>--</u>	<u>996,244</u>
	5,493,842	--	--	5,493,842
Supporting services				
Management and general	<u>926,386</u>	<u>--</u>	<u>--</u>	<u>926,386</u>
Total expenses	<u>6,420,228</u>	<u>--</u>	<u>--</u>	<u>6,420,228</u>
CHANGE IN NET ASSETS	4,986,551	--	--	4,986,551
NET ASSETS AT BEGINNING OF YEAR	<u>5,722,791</u>	<u>--</u>	<u>1,000,000</u>	<u>6,722,791</u>
NET ASSETS AT END OF YEAR	\$ <u>10,709,342</u>	\$ <u>--</u>	\$ <u>1,000,000</u>	\$ <u>11,709,342</u>

See accompanying notes to financial statements.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
STATEMENT OF CASH FLOWS
Year Ended December 31, 2015

INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS

Cash flows from operating activities

Change in net assets	\$ 4,986,551
Adjustments to reconcile change in net assets to net cash used by operating activities:	
Depreciation and amortization	1,653,358
Provision for doubtful accounts	42,838
Extinguishment of debt	(5,438,638)
(Increase) decrease in:	
Grants receivable	(67,873)
Tenants receivable	(41,767)
Tenant security deposits	(29,219)
Southside conditional contribution	(1,540,000)
Prepaid expenses	1,400
Other	(3,078)
Increase (decrease) in:	
Accounts payable	(66,423)
Accrued liabilities	33,141
Interest payable	396,718
Tenant security deposits	(23,788)
Deferred grant revenue	38,276
Total adjustments	<u>(5,045,055)</u>
Net cash used by operating activities	<u>(58,504)</u>

Cash flows from investing activities

Purchase of property and equipment	(202,576)
Payment for acquisition of Hale Makana O'Waiale	<u>(61,025)</u>
Net cash used in investing activities	<u>(263,601)</u>

Cash flows from financing activities

Principal payments on note payable	<u>(25,000)</u>
Net cash used by financing activities	<u>(25,000)</u>

NET DECREASE IN CASH AND CASH EQUIVALENTS (347,105)

Cash and cash equivalents at beginning of year 756,611

Cash and cash equivalents at end of year \$ 409,506

SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES

Gain from extinguishment of debt	\$ 5,438,638
Acquisition of Hale Makana O'Waiale property and equipment	\$ 16,327,600
Assumption of notes payable	\$ 8,463,638

See accompanying notes to financial statements.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE A - NATURE OF ACTIVITIES

Ka Hale A Ke Ola Homeless Resource Centers, Inc. (KHAKO) is a private, nonprofit community-based organization incorporated in the State of Hawaii. KHAKO was formed as Maui Catholic Charities in 1986, as an affiliate agency of the Catholic Charities of the Diocese of Honolulu. In November 1992, KHAKO was formed to become an independent organization to administer and maintain the Ka Hale A Ke Ola Resource Center. In 2004, KHAKO opened the Na Hale O Wainee Resource Center in Lahaina, Maui. KHAKO was previously known as Maui Economic Concerns of the Community, Inc., until it changed its name to Ka Hale A Ke Ola Homeless Resource Centers, Inc. in August 2010.

KHAKO was organized to serve the needs of low-income and homeless families on Maui by providing emergency, transitional, and affordable permanent housing, as well as providing educational, vocational training, and other supportive services to voice their concerns, to empower them to take responsibility for their own lives and to call on the community to assist in these actions.

Effective January 1, 2015, KHAKO acquired Hale Makana o' Waiale Rental Project (Project) which is a 200-unit multifamily apartment complex located in Wailuku, Hawaii, intended for rental to individuals or families with income below 50% of the County of Maui's median gross income levels.

KHAKO receives a substantial amount of its support from the County of Maui and the State of Hawaii. A significant reduction in the level of this support, if this were to occur, could have an adverse effect on KHAKO's programs and activities.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES

- (1) ***Basis of accounting and financial statement presentation*** - The financial statements of KHAKO have been prepared on the accrual basis of accounting consistent with accounting principles generally accepted in the United States of America. Net assets, public support and revenues and expenses are classified based upon the existence or absence of donor-imposed restrictions. Accordingly, net assets of KHAKO and changes therein are classified and reported as follows:

Unrestricted - Net assets which are free of donor-imposed restrictions; all revenues, expenses, gains and losses that are not changes in temporarily or permanently restricted net assets.

Temporarily Restricted - Net assets whose use by KHAKO is limited by donor-imposed stipulations that either expire by passage of time or that can be fulfilled by actions of KHAKO pursuant to those stipulations. KHAKO did not have any temporarily restricted net assets.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Permanently Restricted - Net assets whose use is limited by donor-imposed restrictions that neither expire with the passage of time nor can be fulfilled or otherwise removed by actions of KHAKO.

- (2) ***Use of estimates*** - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.
- (3) ***Cash and cash equivalents*** - KHAKO considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.
- (4) ***Tenants receivable*** - Tenants receivable consists of rent due from clients and are stated at the amount management expects to collect from outstanding balances. The carrying amount of tenants receivable is reduced by a valuation allowance that reflects management's best estimate of the amounts that will not be collected based upon prior experience and management's assessment of the credit worthiness of clients.

Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances determined to be uncollectible after management has used reasonable collection efforts are not written-off. Instead, these uncollectible accounts will continue to be accounted for, in the event delinquent tenants attempt to obtain services from KHAKO in the future. If this were to occur, they would be required to settle all past due accounts before receiving future services.

- (5) ***Investments*** - Investments in marketable securities are reported at fair value based on quoted market prices. Realized and unrealized gains and losses are recognized in the statement of activities. Investment income and gains restricted by a donor are reported as increases in unrestricted net assets if the restrictions are met in the reporting period in which the income and gains are recognized.
- (6) ***Property and equipment*** - Property and equipment acquisitions of \$500 or more with an estimated useful life over one year are recorded at cost. Donated assets are recorded at their estimated fair value at the date of the gift. Depreciation is calculated using the straight-line method based on the estimated useful lives of the assets, which range from 3 to 40 years.

Expenditures for maintenance, repairs, and minor renewals are charged to expense; expenditures for betterments are capitalized. Property retired or otherwise disposed of is removed from the appropriate asset and related accumulated depreciation accounts. Gains and losses on the sale of assets are reflected in current operations.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Long-lived assets held and used by KHAKO are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In the event that facts and circumstances indicate that the cost of any long-lived assets may be impaired, an evaluation of recoverability would be performed.

- (7) **Rental revenue** - The rental property is generally leased to tenants under one year non-cancelable operating leases. Rental income is recognized under the operating method as rentals become due. Other income includes fees for late payments, cleaning, damages and other charges and is recorded when earned.
- (8) **Recognition of government grant revenue** - Revenues on cost reimbursement contracts are recognized when allowable and reimbursable expenses are incurred, and upon meeting the legal and contractual requirements of the funding source. Revenues on fee-for-service contracts are recognized when the services required by the contractual agreements are satisfactorily performed. These revenues are generally considered exchange transactions, and are thereby recorded as revenues of the unrestricted net asset class. Funding received in advance of the applicable revenue recognition criteria is recorded as deferred grant revenue in the statement of financial position.
- (9) **Restricted and unrestricted revenue and support** - Contributions, revenues and support are recorded in the period earned as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

- (10) **Donated services and materials** - Donated services are recognized as contributions if the services (a) create or enhance nonfinancial assets or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased by KHAKO. Significant and essential donated services are performed by various volunteers to support KHAKO's programs and activities. These services have not been reflected in the financial statements as the criteria for recognition were not met.
- (11) **Functional allocation of expenses** - The costs of providing the various programs and other activities are summarized on a functional basis in the statement of activities. Accordingly, costs are allocated to the benefited programs and supporting services based on direct costs incurred and management's estimates of resources consumed by these functions.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (Continued)

- (12) **Income taxes** - KHAKO is recognized by the Internal Revenue Service as an exempt organization under Section 501(c)(3) of the Internal Revenue Code. KHAKO is not subject to income taxes in the U.S. federal jurisdiction and the State of Hawaii.
- (13) **Subsequent events** - Management has evaluated subsequent events through September 2, 2016, the date on which the financial statements were available to be issued. There were no other subsequent events that required adjustment of or disclosure in the financial statements.

NOTE C - HALE MAKANA O' WAIALE AFFORDABLE RENTAL PROJECT

KHAKO began construction of the Hale Makana O' Waiale Affordable Rental Project (Project) in 1996, and completed it in 1997. The total cost of constructing the Project was \$16,744,734; funded by loans from the County of Maui (County) totaling \$8,725,015; a loan from the Rental Housing Trust Fund Commission (RHTF) of the Housing and Community Development Corporation of Hawaii now known as Hawaii Housing Finance and Development Corporation (HHFDC) totaling \$3,000,000; grants from the County totaling \$1,769,065; and grants from the U.S. Department of Housing and Urban Development passed-through the County totaling \$3,250,654. Under the terms of the agreements between KHAKO and the funding agencies, KHAKO must use the constructed assets to provide affordable rental housing for low-income families for the life of the assets.

Effective December 18, 1997, the Hale Makana O' Waiale, a Hawaii Limited Partnership (Partnership) was formed to own and operate the Project as a qualified low-income housing project within the meaning of Section 42 of the Internal Revenue Code (IRC) of 1986 and Section 235-110 of the Hawaii Revised Statutes (HRS). To effectuate the purpose of the partnership, KHAKO assigned to the Partnership its interest in the land lease from the County related to the Project. Included in the assignment of the land lease were all interests of KHAKO in the buildings, improvements and privileges connected thereto. The assignment was effective December 30, 1997. The Partnership simultaneously entered into a Restrictive Covenant Agreement with the HHFDC to maintain the Project as a low-income housing project in accordance with the IRC for an additional 40 years beyond the minimum 15-year IRC compliance period for a total of 55 years. During this term, the Partnership must lease 100% of the units in the Project to individuals or families whose income is 50% or less of the area median gross income as determined in accordance with Section 42 of the IRC.

As a result of the assignment of the land lease and related buildings and improvements to the Partnership, the fixed assets related to the Project totaling \$16,744,734, and the loans secured by the Project totaling \$11,725,015, were transferred from KHAKO to the Partnership as of December 31, 1997. The value of the newly constructed assets of the Project less the related loans were recorded by the Partnership as in-kind capital contribution from KHAKO of \$43,489 and a note payable to KHAKO of \$4,976,230.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE C - HALE MAKANA O' WAIALE AFFORDABLE RENTAL PROJECT (Continued)

On January 30, 1998, KHAKO, as the operating general partner, entered into a limited partnership agreement with the Hawaii Investors' Administrative Partner, Inc. (HIAPI), as the administrative general partner, and the Hawaii Affordable Housing Fund I (HAHF), as the sole limited partner of the Partnership. As part of the terms of the limited partnership agreement, the HAHF and HIAPI made capital contributions to the Partnership totaling \$4,301,123 and \$4,249, respectively. These capital contributions were used to repay various loans due to the County and establish operating reserves.

The limited partnership agreement stipulates that on or after the 15-year IRC compliance period, the limited partners have the option to require KHAKO to purchase the limited partners' interest in the Partnership. The option price shall be equal to the principal amount of outstanding indebtedness secured by the Project; the limited partners' federal and state taxes due upon such purchase; and the amount of any unpaid shortfall in low-income housing tax credits actually generated by the Partnership compared to the tax credits projected at the inception of the limited partnership.

During 2003, HAHF sold 63.82% of its interest in the Partnership to SunAmerica Housing Fund 1117 (SHF), the Investment Partnership. The remaining 36.18% interest was assigned to Bank of Hawaii (BOH), the Class A Limited Partner, in complete redemption and liquidation of BOH's interest in HAHF. These transactions occurred between HAHF, SHF, and BOH and were not Partnership transactions.

As a result of the sale by HAHF, effective July 1, 2003, a first amendment to the original limited partnership agreement changed the partners of the Partnership. Concurrently with the execution of the first amendment, HIAPI withdrew from the Partnership and the Hawaii Investors for Affordable Housing, Inc. (HIAHI) was admitted as the Special Limited Partner.

As of January 1, 2011, BOH assigned all of its interest in the Partnership, exclusive of certain retained rights, to SHF. Concurrently with this transaction, a second amendment to the limited partnership agreement was executed on January 1, 2011, and BOH withdrew from the Partnership. As a result of this transaction, as of January 1, 2011, profits, losses and the distribution of net cash flows will be allocated 1.0%, 0.01% and 98.99% to the Operating General Partner, Special Limited Partner and the Investment Partnership, respectively.

Effective January 1, 2015, the Special Limited Partner and the Investment Partnership exited the Partnership and required KHAKO to purchase the limited partners' interest in the Partnership in the amount of \$61,025. As such, KHAKO acquired the Project and continues

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE C - HALE MAKANA O' WAIALE AFFORDABLE RENTAL PROJECT (Continued)

to operate the rental project as a qualified low-income housing project within the meaning of Section 42 of the Internal Revenue Code and Section 235-110 of the Hawaii Revised Statutes. With KHAKO's acquisition of the project, the following are the assets acquired and the liabilities assumed:

Cash	\$	35,371
Receivables	\$	20,066
Prepaid expenses	\$	26,510
Property and equipment	\$	16,327,600
Other assets	\$	317,692
Accounts payable and accrued liabilities	\$	319,889
Notes payable	\$	8,463,638

NOTE D - CONCENTRATION OF CREDIT RISK

KHAKO maintains its cash accounts and restricted accounts in a commercial bank and a financial services company. Cash and cash equivalents are insured up to \$250,000 per account holder by the Federal Deposit Insurance Corporation (FDIC). Cash, cash equivalents and investments held by the financial services company are insured up to \$500,000 (with a limit of \$250,000 for cash) by the Securities Investor Protection Corporation (SIPC). In assessing its concentration of credit risk related to cash, cash equivalents, and investments, KHAKO places its cash, cash equivalents, and investments in financial institutions, which may at times exceed FDIC and SIPC insurance limits.

KHAKO has a repurchase agreement with a bank. At the end of each business day, KHAKO enters into a transaction in which the bank agrees to transfer to KHAKO government or agency securities against the transfer of funds by KHAKO, with a simultaneous agreement by KHAKO to transfer to the bank such securities the following morning against the transfer of funds by the bank. Securities transferred to KHAKO are in a book entry account at a Federal Reserve Bank and/or Federal Home Loan Bank. At December 31, 2015, funds in these accounts totaling \$1,545,000 are included in restricted cash and cash equivalents on the statement of financial position. This amount is not insured by the FDIC or the SIPC.

NOTE E - LONG-TERM OBLIGATIONS

Under the terms of the agreements between KHAKO and the funding agencies, KHAKO must use the constructed assets to provide affordable rental housing for low-income families for the life of the assets. If KHAKO uses the constructed assets for other than its intended purpose, KHAKO must either pay the funding agencies the current fair value of the assets, or transfer control and title of the assets to the funding agencies.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE E - LONG-TERM OBLIGATIONS (Continued)

The long-term obligations at December 31, 2015, consist of the following:

	<u>Amount</u>
Note payable to Rental Housing Trust Fund Commission maturing on June 25, 2026. Interest at 3% is compounded annually beginning June 26, 2016. No principal and interest payments are required while loans payable to the County of Maui are outstanding or until June 25, 2016, whichever is earlier. Thereafter, monthly payments including interest at 3% shall be due over a ten-year period ending no later than June 25, 2026.	\$ 3,000,000
Construction loan from the County of Maui maturing on June 30, 2030. No principal and interest are required through May 2006. Annual interest only payments were due in June 2006 and June 2007. Thereafter, annual payments of approximately \$283,000, including interest at variable interest rates shall be due over a twenty-three year period ending on June 30, 2030.	<u>4,000,000</u> 7,000,000
Less current maturities	<u>4,157,069</u> \$ <u>2,842,931</u>

The aggregate maturities of the long-term obligation for future years are as follows:

<u>Year</u>	<u>Amount</u>
2016	\$ 4,157,069
2017	263,000
2018	270,000
2019	279,000
2020	287,000
Thereafter	<u>1,743,931</u> \$ <u>7,000,000</u>

KHAKO has not made required debt service payments on the construction loan. This constitutes an event of default under the terms and conditions of the loan agreement that could result in the outstanding loan becoming callable at the discretion of the County. The loan is secured by the real property and improvements funded by the proceeds

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE E - LONG-TERM OBLIGATIONS (Continued)

of the loan. At December 31, 2015, the total loan payable was \$4,000,000. Interest expense for the year ended December 31, 2015, totaled \$139,990. Accordingly, the entire outstanding loan balance has been classified as a current liability in the statement of financial position at December 31, 2015.

On August 25, 2015, the note payable to the County of Maui totaling \$5,438,638, which consisted of \$4,055,000 in principal and \$1,408,638 in interest less \$25,000 payment accompanying the proposed repayment plan, was forgiven via Resolution No. 15-103. Despite the proposal to repay, the County decided to forgive the entire outstanding debt related to the construction of the Project.

NOTE F - PERMANENTLY RESTRICTED NET ASSETS

Under the terms of a \$1.5 million grant received from a private foundation to build the Ka Hale A Ke Ola Homeless Resource Center (Center) in 1992, KHAKO must maintain a \$1,000,000 endowment in perpetuity and income from endowment earnings must be used solely for the maintenance and upkeep of the Center. Endowment assets are comprised of cash, cash equivalents, and investments.

Interpretation of Relevant Law

The board of directors of KHAKO has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, KHAKO classifies as permanently restricted net assets, (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by KHAKO in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, KHAKO considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- (1) The duration and preservation of the fund
- (2) The purposes of KHAKO and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE F - PERMANENTLY RESTRICTED NET ASSETS (Continued)

- (5) The expected total return from income and the appreciation of investments
- (6) The investment policies of KHAKEO
- (7) Other resources of KHAKEO

Endowment net asset composition by fund type as of December 31, 2015, was as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-designated endowment funds	\$ <u> --</u>	\$ <u> --</u>	\$ <u>1,000,000</u>	\$ <u>1,000,000</u>

Changes in endowment net assets for the year ended December 31, 2015 were as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ <u> --</u>	\$ <u> --</u>	\$ <u>1,000,000</u>	\$ <u>1,000,000</u>
Investment return:				
Investment income	<u> --</u>	<u> 366</u>	<u> --</u>	<u> 366</u>
Total investment return	<u> --</u>	<u> 366</u>	<u> --</u>	<u> 366</u>
Appropriation of endowment assets for expenditure	<u> --</u>	<u> (366)</u>	<u> --</u>	<u> (366)</u>
Endowment net assets, end of year	\$ <u> --</u>	\$ <u> --</u>	\$ <u>1,000,000</u>	\$ <u>1,000,000</u>

Return Objectives and Risk Parameters

KHAKEO has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the historic dollar value of the original endowment assets. Endowment assets include those assets of donor-restricted funds that KHAKEO must hold in perpetuity or for a donor-specified period(s). KHAKEO seeks low volatility of returns while assuming a low level of investment risk.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE F - PERMANENTLY RESTRICTED NET ASSETS (Continued)

Strategies Employed for Achieving Objectives

KHAKO emphasizes short-term investments that are insured by the U.S. government to achieve its objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

KHAKO has a policy of expending only the accumulated earnings on the endowment fund principal for the maintenance and upkeep of the Center, as required by donor stipulations. Earnings in excess of the original endowment amount are considered to be appropriated for this purpose when earned.

NOTE G - RESTRICTED RESOURCES

As of December 31, 2015, KHAKO received restricted cash totaling \$1,540,000 in connection with contributions that are conditioned upon the future development of a resource center in South Maui upon land to be designated. Revenue recognition will be deferred until the conditions on which they depend are substantially met. Accordingly, cash received in advance of revenue recognition is presented as deferred revenue on the statement of financial position.

As discussed in Note F, KHAKO also maintains an endowment in perpetuity. The endowment is made up of a combination of cash, cash equivalents and short-term investments. At December 31, 2015, restricted resources are summarized as follows:

	Permanently Restricted	Conditional Restricted	Tenant Security Deposits	Total Restricted
Cash and cash equivalents	\$ 748,033	\$ 1,540,000	\$ 27,051	\$ 2,315,084
Certificates of deposit	244,011	--	--	244,011
Equity securities	<u>7,956</u>	<u>--</u>	<u>--</u>	<u>7,956</u>
	<u>\$ 1,000,000</u>	<u>\$ 1,540,000</u>	<u>\$ 27,051</u>	<u>\$ 2,567,051</u>

NOTE H - LEASE COMMITMENTS

KHAKO entered into a ground lease with the County on May 22, 1992. Under the terms of the lease, KHAKO is entitled to have and hold the property for 55 years at an annual rent of \$1 provided that KHAKO uses the property to provide shelter for homeless persons, and other programs which directly benefit the people of Maui, especially low-income persons and families and for related administrative and support facilities.

On October 23, 1995, KHAKO entered into an agreement with the County to lease land adjacent to the property described in the above lease agreement. Under the terms of this lease, KHAKO is entitled to have and hold the property for 55 years at an annual rent of \$1

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE H - LEASE COMMITMENTS (Continued)

provided that KHAKO uses the property for the construction and operation of housing units for low income residents of Maui, and other programs which directly benefit the people of Maui, especially low income persons and families and for related administrative and support facilities.

On December 30, 1997, KHAKO assigned the lease dated October 23, 1995, together with all buildings, improvements and privileges to the Partnership with the prior consent of the County. Effective January 1, 2015, the Partnership was dissolved.

On November 6, 2001, KHAKO entered into an agreement with the County to lease land located in Lahaina, Hawaii. Under the terms of the lease, KHAKO is entitled to have and hold the property for 55 years at an annual rent of \$1 provided that KHAKO uses the property to provide shelter for homeless persons, and other programs which directly benefit the people of Maui, especially low-income persons and families and for related administrative and support facilities.

NOTE I - PENSION PLAN

KHAKO has a defined contribution pension plan which covers all full-time employees who are 21 years of age with at least one year of service. Participating employees may make voluntary deferral contributions to the plan up to the maximum amounts permitted by the Internal Revenue Service. KHAKO makes contributions on behalf of employees equal to 3% of their compensation. In addition, KHAKO makes an additional contribution on behalf of participating employees equal to 50% of the first 6% of their salary deferral contributions. Contributions by KHAKO on behalf of each employee are subject to limits prescribed by the Internal Revenue Service and are fully vested to the employee after three years of service. Voluntary employee salary deferral contributions to the plan are always fully vested to the employee. During the year ended December 31, 2015, KHAKO's contribution to the plan amounted to approximately \$55,700.

NOTE J - FAIR VALUE MEASUREMENTS

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described below:

- Level 1** Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.
- Level 2** Inputs to the valuation methodology include:
 - Quoted prices for similar assets or liabilities in active markets;

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE J - FAIR VALUE MEASUREMENTS (Continued)

- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The following is a description of the valuation methodologies used for assets at fair value. There have been no changes in the methodologies used at December 31, 2015.

Stocks are classified within Level 1 of the hierarchy because they are valued using quoted market prices of shares held by KHAKO at year end.

The following table sets forth by level, within the fair value hierarchy, KHAKO's assets at fair value as of December 31, 2015:

Assets at Fair Value as of December 31, 2015				
	Level 1	Level 2	Level 3	Total
Equity securities	\$ <u>7,956</u>	\$ <u>--</u>	\$ <u>--</u>	\$ <u>7,956</u>
	\$ <u>7,956</u>	\$ <u>--</u>	\$ <u>--</u>	\$ <u>7,956</u>

NOTE K – CONTRACT COMMITMENTS

In August 2011, KHAKO entered into an agreement with Sunetric Capital LLC to purchase electricity at 25% less than the Electrical Utility Rate Schedule then in effect (for the Project) which started in July 2012 and expires in 2032. Electricity cost paid to Sunetric Capital LLC totaled approximately \$191,800 for the year ended December 31, 2015.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015

NOTE K – CONTRACT COMMITMENTS (Continued)

In August 2011, KHAKE entered into an agreement with Kala Capital LLC to purchase electricity at 25% less than the Electrical Utility Rate Schedule then in effect (for Westside) which started in March 2013 and expires in 2033. Electricity cost paid to Kala Capital LLC totaled approximately \$123,200 for the year ended December 31, 2015.

In June 2013, KHAKE entered into an agreement with SPS Solar VII LLC to purchase electricity at 25% less than the Electrical Utility Rate Schedule then in effect (for Central) which started in January 2015 and expires in 2035. For the period from the Commercial Operation Date and for twenty-eight (28) months, the Energy Price will not be discounted. Electricity cost paid to SPS Solar VII LLC totaled approximately \$86,500 for the year ended December 31, 2015.

NOTE L - GOING CONCERN UNCERTAINTY

KHAKE's financial statements have been presented on the basis that it is a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. KHAKE has, however, sustained net losses from operations in recent years which have negatively impacted its financial position as follows:

- Current liabilities exceeded its current assets by approximately \$5,539,800.
- KHAKE has been unable to make required debt service payments to the County of Maui, which is a violation of the terms of the loan agreement.

These conditions have created uncertainty as to KHAKE's ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability or classification of recorded asset or liability amounts that might be necessary should KHAKE be unable to continue as a going concern.

KHAKE's continued existence as a going concern is dependent upon its ability to generate sufficient cash flows to meet its obligations as they become due and resolve the violation of loan covenant described above. Management has been working with the State of Hawaii and the County of Maui to see if modifications can be made to the terms and conditions of existing loan agreements that might strengthen KHAKE's financial position and improve its long-term outlook.

SUPPLEMENTARY INFORMATION

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
SCHEDULE OF CONTRACTS WITH THE HOMELESS PROGRAMS OFFICE
DEPARTMENT OF HUMAN SERVICES OF THE STATE OF HAWAII
Year Ended December 31, 2015

	<u>Federal Funds</u>	<u>State Funds</u>	<u>Total</u>
Contract Number HPO-1012-SA01			
Contract amount	\$ <u> --</u>	\$ <u>1,500,348</u>	\$ <u>1,500,348</u>
Contract expenses - prior periods	\$ <u> --</u>	\$ <u>625,145</u>	\$ <u>625,145</u>
Contract expenses - current period	<u> --</u>	<u>875,203</u>	<u>875,203</u>
Total contract expenses	\$ <u> --</u>	\$ <u>1,500,348</u>	\$ <u>1,500,348</u>
Contract Number HPO-1012-SA02			
Contract amount	\$ <u> --</u>	\$ <u>1,500,348</u>	\$ <u>1,500,348</u>
Contract expenses - prior periods	\$ <u> --</u>	\$ <u> --</u>	\$ <u> --</u>
Contract expenses - current period	<u> --</u>	<u>625,145</u>	<u>625,145</u>
Total contract expenses	\$ <u> --</u>	\$ <u>625,145</u>	\$ <u>625,145</u>
Contract Number HPO-2085			
Contract amount	\$ <u>57,347</u>	\$ <u> --</u>	\$ <u>57,347</u>
Contract expenses - prior periods	\$ <u>8,300</u>	\$ <u> --</u>	\$ <u>8,300</u>
Contract expenses - current period	<u>1,638</u>	<u> --</u>	<u>1,638</u>
Total contract expenses	\$ <u>9,938</u>	\$ <u> --</u>	\$ <u>9,938</u>
Contract Number HPO-2089			
Contract amount	\$ <u>25,000</u>	\$ <u> --</u>	\$ <u>25,000</u>
Contract expenses - prior periods	\$ <u>12,500</u>	\$ <u> --</u>	\$ <u>12,500</u>
Contract expenses - current period	<u>12,500</u>	<u> --</u>	<u>12,500</u>
Total contract expenses	\$ <u>25,000</u>	\$ <u> --</u>	\$ <u>25,000</u>
Contract Number HPO-3009			
Contract amount	\$ <u>20,956</u>	\$ <u> --</u>	\$ <u>20,956</u>
Contract expenses - prior periods	\$ <u> --</u>	\$ <u> --</u>	\$ <u> --</u>
Contract expenses - current period	<u>10,478</u>	<u> --</u>	<u>10,478</u>
Total contract expenses	\$ <u>10,478</u>	\$ <u> --</u>	\$ <u>10,478</u>

The schedule of contracts with the Homeless Programs Office funded by the Department of Human Services of the State of Hawaii is presented on the accrual basis of accounting. Because the schedule presents only a selected portion of the operations of Ka Hale A Ke Ola Homeless Resource Centers, Inc., it is not intended to, and does not present the financial position, changes in net assets, or cash flows of Ka Hale A Ke Ola Homeless Resource Centers, Inc.

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
SCHEDULE OF CONTRACTS WITH THE BENEFIT, EMPLOYMENT AND
SUPPORT SERVICES DIVISION
DEPARTMENT OF HUMAN SERVICES OF THE STATE OF HAWAII
Year Ended December 31, 2015

	<u>Federal Funds</u>	<u>State Funds</u>	<u>Total</u>
Contract Number ETPO-2156			
Contract amount	\$ <u>100,000</u>	\$ <u>--</u>	\$ <u>100,000</u>
Contract expenses - prior periods	\$ --	\$ --	\$ --
Contract expenses - current period	<u>43,634</u>	<u>--</u>	<u>43,634</u>
Total contract expenses	\$ <u>43,634</u>	\$ <u>--</u>	\$ <u>43,634</u>

The schedule of contracts with the Benefit, Employment & Support Services Division funded by the Department of Human Services of the State of Hawaii is presented on the accrual basis of accounting. Because the schedule presents only a selected portion of the operations of Ka Hale A Ke Ola Homeless Resource Centers, Inc., it is not intended to, and does not present the financial position, changes in net assets, or cash flows of Ka Hale A Ke Ola Homeless Resource Centers, Inc.

PART II

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

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

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Ka Hale A Ke Ola Homeless Resource Centers, Inc.

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Ka Hale A Ke Ola Homeless Resource Centers, Inc. (KHAKO), which comprise the statement of financial position as of December 31, 2015, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated September 2, 2016.

Internal Control Over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the KHAKO's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and responses as item 2015-001.

KHAKO's Response to Findings

KHAKO's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. KHAKO's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

N & K CPAs, Inc.

Honolulu, Hawaii
September 2, 2016

PART III
SCHEDULE OF FINDINGS AND RESPONSES

Ka Hale A Ke Ola Homeless Resources Centers, Inc.
SCHEDULE OF FINDINGS AND RESPONSES
Year Ended December 31, 2015

<u>Ref. No.</u>	<u>Internal Control and Compliance Findings</u>
2015-001	<p>Noncompliance with Terms and Conditions of Loan Agreement</p> <p>Criteria: Under the terms and conditions of the loan agreement with the County of Maui, dated April 30, 2003, KHAKO was required to make annual interest only payments commencing in June 2006 and June 2007. Thereafter, annual payments of approximately \$283,000 shall be due over a twenty-three year period ending on June 30, 2030.</p> <p>Condition: KHAKO has not made any of the required debt service payments on this loan as of December 31, 2015, which consisted of approximately \$1,005,000 in principal and \$1,684,000 in interest.</p> <p>Cause: As discussed in Note L to the financial statements, KHAKO has experienced financial difficulties over the past few years that have had an adverse effect on its working capital, in particular, cash flows available to make the required debt service payments.</p> <p>Effect: Failure to make required debt service payments in accordance with the terms and conditions of the loan agreement with the County of Maui, dated April 30, 2003, constitutes an event of default that could result in the outstanding loan becoming callable at the discretion of the County of Maui. Accordingly, the entire outstanding loan balance of \$4,000,000 is required to be classified as a current liability in the statement of financial position at December 31, 2015. Furthermore, as discussed in Note L, the failure to make required debt service payments is one of the principal conditions giving rise to the assessment of substantial doubt about KHAKO's ability to continue as a going concern.</p> <p>Recommendation: As discussed in Note L, management is aware of the situation and should continue to work with the County of Maui to negotiate a modification to the terms and conditions of the loan agreement that could provide KHAKO with some financial relief that would enable KHAKO to strengthen its financial position and improve its long-term outlook.</p> <p>Management's Response: Monique Yamashita, CEO, is the contact person responsible for the corrective action. Management plans to continue to implement cost cutting measures in order to improve KHAKO's cash flows from operating activities. Management also plans to continue to work with the County of Maui to negotiate a modification to the loan agreement that could improve KHAKO's ability to meet its current and future obligations. This will be an ongoing process.</p>

PART IV
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Ka Hale A Ke Ola Homeless Resource Centers, Inc.
STATUS REPORT
Year Ended December 31, 2015

This section contains the current status of our prior audit recommendation. The recommendation is referenced to the page of the previous audit report for the year ended December 31, 2014, dated September 15, 2015.

SECTION II - FINANCIAL STATEMENT FINDINGS

<u>Recommendation</u>	<u>Status</u>
<p>2014-001 Noncompliance with Terms and Conditions of Loan Agreement (page 28)</p> <p>Management is aware of the situation and should continue to work with the County of Maui to negotiate a modification to the terms and conditions of the loan agreement that could provide KHAKE with some financial relief that would enable KHAKE to strengthen its financial position and improve its long-term outlook.</p>	<p>Management continues to work with the County of Maui to resolve the underlying conditions that has resulted in this instance of noncompliance. Refer to management's response to finding 2015-001 on page 30.</p>