Report No. 93-20 December 1993

OVERVIEW

THE AUDITOR
STATE OF HAWAII

Examination of Selected Aspects of Capital Projects Funds

Summary

Capital improvement projects (CIPs) of the State constitute one of its more significant and costly programs. In 1981, the Legislature appropriated about $419 million for the CIP program. Ten years later CIP appropriations had increased almost sixfold to more than $2.4 *billion*. CIPs are funded through sales of general obligation bonds and revenue bonds as well as moneys from special funds, the general fund, and federal funds.

Because of the growth and size of capital projects funds the Office of the Auditor and the certified public accounting firm of KPMG Peat Marwick conducted an examination of selected aspects of capital projects funds.

We found that the executive's budget requests for CIPS and the Legislature's appropriations do not result in a realistic spending program. This is because the CIPs that are funded cannot realistically be completed within the three-year time limit on appropriations set under the State Constitution. This in turn has weakened the Legislature's control over the CIP program. We found also that constitutional lapsing provisions have been circumvented because the definition of an encumbrance is unclear and encumbrance policies conflict. Other problems: agencies are avoiding lapsing requirements through inappropriate interagency contracts; encumbrances are not being monitored; and encumbrances for works of art are a particular concern.

We also found that continuing appropriations for projects receiving federal aid are unnecessary, and that agencies are still not transferring surplus appropriations to the project adjustment fund as required by the general appropriations acts.

Recommendations and Responses

We recommend that the Legislature consider requiring the executive branch to submit a realistic budget for a three-year CIP program. The Legislature should appropriate funds for capital improvement projects in increments based on the three-year spending schedule. We recommend that in-house personnel costs for CIPs be included in the operating budget. Currently agencies carry forward CIP appropriations by suspect encumbrance practices to protect future salary costs of civil service employees. We also recommend that the Legislature provide a statutory definition of an encumbrance.

We recommend that responsibilities of expending agencies be clearly defined so that they do not use interagency contracts to circumvent constitutional lapsing requirements. In addition, the Works of Art Special Fund should be repealed. We also recommend that the Legislature cease the practice of generally allowing appropriations needed for federal funding to be non-lapsing.

The Department of Accounting and General Services (DAGS) should monitor more strictly the encumbrance practices of expending agencies to make sure encumbrances are justified. The Department of Budget and Finance (B&F) should ensure that surplus appropriations are transferred to the project adjustment fund.

The Department of Accounting and General Services agrees that in-house personnel costs of CIP should be included in the operating budget instead of the CIP budget. It also agrees that a statutory definition of an encumbrance is necessary. Further, it has no objections to our recommendation that the Legislature cease allowing appropriations to be non-lapsing.

DAGS has reservations about some of our recommendations, particularly that the executive branch submit a realistic CIP budget based on a three-year spending cycle and that DAGS monitor the encumbrance practices of agencies. It also has reservations about our recommendation that it prepare an annual report on the activity of the project adjustment fund—it believes that it is more appropriate for B&F to prepare such a report. DAGS opposes the abolishment of interagency contracts—if they meet constitutional mandates and legal parameters outlined in an Attorney General opinion of 1988. DAGS did not address the problem of interagency contracts being entered into solely to avoid lapsing of appropriations. It also opposes our recommendation to repeal the Works of Art Special Fund because it believes the fund is needed to allow the State Foundation on Culture and the Arts to obtain meaningful art works. We stand by our recommendation that this fund be repealed and that works of art included in CIP appropriations be subject to the same lapsing provisions as other CIP appropriations.

The Department of Budget and Finance concurs with our recommendation that it should ensure that surplus appropriations are transferred to the project adjustment fund.

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