

AUDIT REPORT NO. 69-9  
JUNE 1969

# FINANCIAL AUDIT OF THE KAUAI VETERANS MEMORIAL HOSPITAL

FOR THE FISCAL YEAR ENDED JUNE 30, 1968

A REPORT TO THE GOVERNOR AND THE  
LEGISLATURE OF THE STATE OF HAWAII



SUBMITTED BY THE LEGISLATIVE AUDITOR OF THE STATE OF HAWAII

## **THE OFFICE OF THE LEGISLATIVE AUDITOR**

The office of the legislative auditor is a public agency attached to the Hawaii State legislature. It is established by Article VI, Section 8, of the Constitution of the State of Hawaii. The expenses of the office are financed through appropriations made by the legislature.

The primary function of this office is to strengthen the legislature's capabilities in making rational decisions with respect to authorizing public programs, setting program levels, and establishing fiscal policies and in conducting an effective review and appraisal of the performance of public agencies.

The office of the legislative auditor endeavors to fulfill this responsibility by carrying on the following activities.

1. Conducting examinations and tests of state agencies' planning, programming, and budgeting processes to determine the quality of these processes and thus the pertinence of the actions requested of the legislature by these agencies.
2. Conducting examinations and tests of state agencies' implementation processes to determine whether the laws, policies, and programs of the State are being carried out in an effective, efficient and economical manner.
3. Conducting systematic and periodic examinations of all financial statements prepared by and for all state and county agencies to attest to their substantial accuracy and reliability.
4. Conducting tests of all internal control systems of state and local agencies to ensure that such systems are properly designed to safeguard the agencies' assets against loss from waste, fraud, error, etc.; to ensure the legality, accuracy and reliability of the agencies' financial transaction records and statements; to promote efficient operations; and to encourage adherence to prescribed management policies.
5. Conducting special studies and investigations as may be directed by the legislature.

Hawaii's laws provide the legislative auditor with broad powers to examine and inspect all books, records, statements, documents and all financial affairs of every state and local agency. However, the office exercises no control functions and is restricted to reviewing, evaluating, and reporting its findings and recommendations to the legislature and the governor. The independent, objective, and impartial manner in which the legislative auditor is required to conduct his examinations provides the basis for placing reliance on his findings and recommendations.



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## FOREWORD

This is a report on our examination of the financial books and accounts of the Kauai Veterans Memorial Hospital and the transactions noted therein for the fiscal year ended June 30, 1968. The purpose of our examination was to determine the propriety of the hospital's financial transactions, the accuracy and reliability of its financial records, and the adequacy of the hospital's controls to safeguard its assets against loss, waste, fraud and extravagance. We made no assessment of the effectiveness of the hospital or the efficiency with which it has carried out its programs, except as they bear directly on the fiscal transactions under examination.

It is our practice to request each of the agencies affected by our examination to submit in writing its comments on our findings and recommendations and to indicate what action it has taken or intends to take. The responses received from those agencies are appended as Part IV of this report.

We wish to express our deep appreciation to the management and staff of the Kauai Veterans Memorial Hospital and the State department of health for their excellent cooperation and assistance.

Clinton T. Tanimura  
Legislative Auditor

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**PART I**  
**INTRODUCTION TO THE AUDIT OF THE**  
**KAUAI VETERANS MEMORIAL HOSPITAL**

**Chapter 1**

**INTRODUCTION**

This is a report on our post-audit of the financial transactions, books and accounts of the Kauai Veterans Memorial Hospital. The audit was conducted pursuant to section 23-4, Hawaii Revised Statutes, which requires the office of the auditor to conduct post-audits of all transactions and of all books and accounts kept by departments, offices and agencies which are supported by or handle State or public funds.

**Purpose of Audit**

The audit was conducted to examine the propriety of the hospital's financial transactions, the accuracy and reliability of its financial records, and the adequacy of its controls to safeguard its assets against loss, waste, fraud and extravagance.

**Scope of Audit**

The audit examined the hospital's financial records for, and the transactions had during the fiscal year July 1, 1967 to June 30, 1968. It was

made in accordance with generally accepted auditing standards as adopted by the American Institute of Certified Public Accountants and as set forth in the *Manual of Guides of the Office of the Legislative Auditor*. It included tests of the accounting records and the use of such auditing procedures as we considered necessary.

**Organization of the Report**

This report is organized into three parts. Part I (chapter 1) consists of this introduction.

Part II (chapters 2 through 4) contains our opinions, findings and recommendations regarding the hospital's system of internal control, its financial statements, and its transactions.

Part III contains a summary of the findings and recommendations.

**Some Background**

The Kauai Veterans Memorial Hospital is a government-operated, short-term care hospital located at Waimea in the county of Kauai. Act

73, SLH 1951, authorized its establishment. The hospital officially opened to the public in February 1957. It is a general hospital, providing all major categories of medical care and services, including 24-hour emergency room and ambulance services. It serves primarily the population of West Kauai and the island of Niihau.

The present facility has a capacity of 37 beds—28 beds are allocated to medical-surgical and 9 beds to obstetrics. In fiscal year 1967-1968, the hospital had approximately 47 employees; it admitted 1549 patients; it had an average daily census of 32.8 patients.

Exhibit I at the end of this chapter summarizes the statistical data of the hospital for the years ended June 30, 1967 and June 30, 1968.

#### **Recent Legislation on Hospital Administration**

In the past four years, the State legislature enacted several pieces of legislation affecting the administration of public hospitals, including the Kauai Veterans Memorial Hospital. Act 97, SLH 1965, transferred the functions of planning, construction, improvement, maintenance and operation of all public hospitals and other public health and medical facilities from the counties to the State, effective July 1, 1965. However, to provide an uninterrupted continuation of

services, the act authorized the State to contract with the counties for the counties to perform the above functions, with certain restrictions, during the period July 1, 1965 to June 30, 1966.

Act 14, SLH 1966, authorized the governor to re-enter into the contracts described in the preceding paragraph with the various counties for the period July 1, 1966 to June 30, 1967.

Finally, Act 203, SLH 1967, affirmed that all matters pertaining to the operation and maintenance of county hospitals and related public health and medical facilities are State responsibilities, but provided that "each county shall, on behalf of the State, operate and maintain" such hospitals and facilities, with all costs to be paid for by the State. This act also provided for the establishment of a county hospital advisory council in each county to serve without compensation and to advise the director of health of the State on matters concerning the planning, construction, improvement, maintenance and operation of the public hospitals and other public health and medical facilities in the county.<sup>1</sup>

<sup>1</sup> At the 1969 session, the legislature completed the State "take-over" of all public hospital and health facilities operations by enacting H.B. No. 740, H.D. 1, S.D. 1. This bill, upon the governor's approval, requires that effective January 1, 1970, all functions pertaining to the operation and maintenance of all public hospitals and all other public health and medical facilities (which are currently being performed by the various counties in behalf of the State under Act 203, SLH 1967), together with all personnel, personal property and real property employed therein, be completely transferred from the counties to the State.

Pursuant to Act 203, a county hospital advisory council was organized in the county of Kauai in February 1968. In addition, the county of Kauai by its resolution no. 83, dated December 6, 1967, created a county advisory committee on hospital management to advise the county council on all aspects of hospital management and operations in the county of Kauai.<sup>2</sup>

### Funding

The day-to-day operations of the Kauai Veterans Memorial Hospital are funded primarily by money received as a result of services rendered to patients. However, these hospital receipts are not always sufficient to finance the entire cost of operating and maintaining the hospital. Therefore, funds from the State general fund are appropriated annually by the legislature to the hospital as a supplement to hospital receipts.

<sup>2</sup>For a general discussion on the various county hospital advisory councils and boards, see our reports to the State legislature entitled, *Status Report on the Implementation of Act 203, Session Laws of Hawaii 1967*, dated February 1968, and *Second Annual Status Report on the Implementation of Act 203, Session Laws of Hawaii 1967*, dated February 1969.

**EXHIBIT I**  
**STATISTICAL DATA**  
Years Ended June 30, 1967 and 1968

	1967	1968
Number of beds . . . . .	37	37
Number of bassinets . . . . .	10	10
Number of incubators . . . . .	2	2
Average number of employees . . .	46	47
Nursing personnel:		
Registered nurses <sup>a</sup> . . . . .	8	9
Practical nurses . . . . .	13	13
Nurses aid . . . . .	2	2
Meals served . . . . .	24,083	31,837
Pounds laundered . . . . .	106,422	132,566
Out-patient visits . . . . .	2,876	3,826
Patients admitted . . . . .	1,414	1,549
Newborn babies delivered . . .	214	182
Patient-days of care—adult . . . .	8,667	11,420
Patient-days of care—newborn . . .	850	569
Average length of stay-days <sup>b</sup> . . .	5.9	8.7
Daily average number of patients, including newborns	26.0	32.8
Number of operations . . . . .	423	465
Number of X-ray procedures . . .	1,228	1,567
Number of laboratory tests . . .	8,299	10,904
Total physical therapy treatments	73	18

<sup>a</sup>Includes nurses in administration.

<sup>b</sup>Adults and pediatrics.

Source: Data compiled by Kauai Veterans Memorial Hospital from its records and reports.

**PART II**  
**FINDINGS AND RECOMMENDATIONS ON INTERNAL CONTROL,**  
**FUND MANAGEMENT AND OPERATION, AND OPINION ON FINANCIAL STATEMENTS**

**Chapter 2**

**INTERNAL CONTROL**

This chapter contains our findings and recommendations regarding the Kauai Veterans Memorial Hospital's internal control system. Our findings and recommendations with respect to specific transactions, statements and funds are noted in subsequent chapters.

The term, "system of internal control," means the plan of organization and all of the methods and measures adopted within the hospital to check the accuracy and reliability of its accounting data, to promote operational efficiency, and to encourage adherence to prescribed laws, policies, and rules and regulations of the State of Hawaii, the State department of health, the county of Kauai, and the Kauai Veterans Memorial Hospital. A sound system of internal control includes two basic elements. The first is a system of authorizations and recording procedures to provide adequate and reasonable accounting control over assets, liabilities, revenues and expenditures in

accordance with generally accepted accounting principles and with the laws, policies, and rules and regulations of the State, the department of health, the county, and the hospital. The second is an appropriate segregation of duties assigned in a manner that no one individual controls all phases of a transaction without the interrelated function of a "cross-check" by some other individual.

**General Control**

Where there are a limited number of personnel, the possibility of setting up an ideal system of internal control is severely curtailed. Such limitation exists at the hospital. Specifically, this situation is present in the areas of cash, accounts receivable, and inventory controls. Because of the small staff available, an appropriate segregation of duties in these areas for control purposes is impractical. Therefore, at the Kauai Veterans Memorial Hospital, constant surveillance on the part of management is the principal and only practical means of safeguarding the assets under its control.

## Compliance with Perquisite Policies

Our audit revealed that the hospital has not complied with certain policies and procedures relating to perquisites.<sup>1</sup>

Prior to April 2, 1968, perquisites were governed by county policies and procedures. However, on April 2, 1968, the State department of health, with the approval of the governor, issued certain policies and instructions to be followed by all public hospitals. Included among the instructions was one stating that "all hospitals will follow the department of health perquisite policy." The State department of health's policy on perquisites requires all executive officers of divisions to submit to the director of health reports on all employees to whom perquisites are granted.

Employees of the hospital receive certain perquisites such as hospitalization in private room at ward room rates and purchase of drugs at cost. However, the hospital has not submitted to the director of health any report on these employees receiving perquisites.

*We recommend that the hospital adhere to the State policy and immediately submit the*

<sup>1</sup>The State department of health, in its *Policies and Procedures on Perquisites*, dated October 27, 1964, defines perquisites as, "Those things furnished or services rendered to an employee by the State government which have value to the employee by reducing his personal expenses."

*required perquisite reports to the director of health. A review of the perquisites will give the director a chance to determine whether the perquisites are properly allowable under the State policy.*

## Inventory Control

At the time of our audit, the hospital was not maintaining an inventory of drugs and supplies under a perpetual inventory system. Under this system, a running count of inventory items on hand is maintained. As inventory items are added or withdrawn, entries are made and the total on hand is calculated and recorded. Perpetual inventory records serve as the primary control over inventory goods.

As of the writing of this report, the hospital is in the process of placing all drug items on a perpetual inventory system. The hospital expects to have this perpetual inventory system for drugs fully implemented at the beginning of fiscal year 1969-70.

*We concur with the hospital's present course of placing all drugs on a perpetual inventory system, especially in view of the fact that drugs constitute a major portion of its inventory. We recommend, however, that the hospital consider placing other major items contained in the inventory of goods on a perpetual inventory system.*

## Depositing of Cash Receipts

The hospital deposits its cash receipts, not on a daily basis, but on the average of twice a week. There appears to be no justifiable reason for this practice. Daily deposits would minimize the amount of funds kept on hand at all times, thereby reducing the risk of theft or misappropriation and temptation for employees to borrow from the funds "temporarily." *We recommend that the hospital adopt the practice of making daily deposits of cash receipts.*

## Chapter 3

### SPECIAL FUND

The operation and maintenance of the Kauai Veterans Memorial Hospital are financed through a special fund.<sup>1</sup> The fund derives its resources primarily from charges made to patients for services rendered. As a supplement, the State legislature appropriates for each fiscal year a sum equal to the excess of estimated expenditures over estimated hospital receipts (the amount of the appropriation is reduced,

<sup>1</sup>See section 147-21, RLH 1955. This section was superseded by Act 97, SLH 1965, Act 14, SLH 1966, and Act 203, SLH 1967, and is therefore omitted in the newly issued Hawaii Revised Statutes. The use of the special fund, however, has continued since Act 97.

however, to the extent that the actual excess is less than the estimate<sup>2</sup>). However, if it appears that the actual requirement will exceed the estimated expenditures, and that the actual hospital receipts will exceed the estimated receipts, the hospital may, with the prior approval of the State department of budget and finance, utilize any such excess receipts to pay for such additional requirement.

This chapter displays the special fund financial statements. It contains a discussion of the major items and figures noted therein. The statements are displayed on both the *accrual* and the *modified cash* bases of accounting. The differences between the two methods of accounting are explained in greater detail in the remaining portions of this chapter. Briefly, however, the financial statements of the *modified cash* basis reflect the actual cash transactions had by the hospital during the fiscal year—that is, the cash actually received, the cash actually paid out, the legal obligations to pay cash assumed, and the cash amounts encumbered or set aside for future payment—and the cash position of the hospital at the end of the fiscal year—that is, the amount of cash on hand. The modified cash basis of accounting reflects the "pay as you go" concept, and it is used by the State for funding and budgeting purposes.

<sup>2</sup>Provided, that this requirement of a reduction in the appropriated amount does not apply if the excess receipt is to be expended for a purpose or purposes approved by the governor or the director of the State department of budget and finance. (See general appropriation acts of 1961, *et seq*; for example, section 15, Act 54, SLH 1967.)

On the other hand, the financial statements on the accrual basis of accounting reflect the special fund's total proprietary rights.<sup>3</sup> They display the rights acquired and the rights given away by the hospital during the fiscal year—that is, the dollar value of the rights to payments for services rendered which accrued (although not necessarily paid), and the legal obligations to pay cash assumed—and the total proprietary position of the hospital at the end of the fiscal year—that is, the amount of property, including cash and the rights to cash.

### Opinion on Financial Statements

In our opinion, the financial statements of the special fund presented on the *accrual* basis of accounting fairly present the assets and liabilities of the fund at June 30, 1968 and the results of the hospital's operations for the year July 1, 1967 to June 30, 1968.

As to the figures presented on the *modified cash* basis of accounting, it is our opinion that the financial statements fairly present the cash balance, liabilities, and commitments of the fund at June 30, 1968 and the results of revenues collected and expenditures made and obligated on account of the fund for the fiscal year July 1, 1967 to June 30, 1968.

<sup>3</sup>Except that *fixed assets* such as land and buildings (if purchased with special fund monies) are not reflected even on the accrual basis. The hospital, as in the case of other governmental agencies, accounts for fixed assets separately. Our comments regarding the hospital's fixed assets are noted later in this chapter.

### Balance Sheet

The balance sheet of the Kauai Veterans Memorial Hospital as of June 30, 1968 is shown in Table I.

As noted in the balance sheet, the accrual basis and the modified cash basis produce different results. This difference is attributable to the following. The accrual basis discloses as assets *all* items owned by the special fund; the modified cash basis includes only cash. The modified cash basis does not include "accounts receivable" as assets because accounts receivable are not cash, although presumably they will be converted to cash in the future. The modified cash basis also excludes "inventory" from assets because expenditures when made or obligated for inventorial items are monies out of pocket; they are thus treated as *expense* when made or obligated. Under the accrual basis, these expenditures are not treated as expense, and the items bought are considered "assets" until they are used.

Liabilities under both methods of accounting are similar. Encumbrances<sup>4</sup> however, are included under the modified cash basis, but not under the accrual basis. The reason for this is that government views encumbrances as firm commitments to expend cash, although the hospital is not obligated to anyone to do so.

<sup>4</sup>*Encumbrances* are obligations in the form of purchase orders, contracts, or commitments which are chargeable to the year in which they are budgeted. These obligations cease to be encumbrances when they are paid or become actually due and payable.

**TABLE I  
BALANCE SHEET  
SPECIAL FUND  
June 30, 1968**

	Accrual	Modified Cash
<b>ASSETS</b>		
Cash:		
In treasury, County of Kauai . . .	\$150,145	\$150,145
On hand . . . . .	150	150
Total cash . . . . .	\$150,295	\$150,295
Accounts receivable (less allowance of \$5,271 for doubtful accounts)	91,884	-
Inventory of drugs and supplies, at cost . . . . .	29,306	-
Total assets . . . . .	\$271,485	\$150,295
<b>LIABILITIES, RESERVE, AND FUND BALANCE</b>		
Liabilities:		
Accounts payable . . . . .	\$ 14,252	\$ 14,252
Unrequired balance of appropriation (Section 1, Act 54, SLH 1967) due to State general fund . . . . .	94,536	94,536
Total liabilities . . . . .	\$108,788	\$108,788
Reserve for encumbrances . . . . .	-	25,129
Fund balance:		
Balance, July 1, 1967 . . . . .	134,992	150
Add:		
Transfer of funds from Maui Memorial Hospital . . . . .	688	688
Reimbursement of expenses incurred in fiscal year 1966-1967 . . . . .	9,806	9,806
Excess of revenue over expenditures (Table II) . . . . .	17,211	5,734
Balance, June 30, 1968 . . . . .	\$162,697	\$ 16,378
Total liabilities, reserve and fund balance . . . . .	\$271,485	\$150,295

A discussion on the various items on the balance sheet follows.

**Assets. 1. Cash.** On June 30, 1968, the cash in the special fund totaled \$150,295, including \$150,145 held in the county of Kauai treasury and \$150 on hand. The sum of \$150,145 held in the county of Kauai treasury includes \$94,536, the balance of the State appropriation not required and unused by the hospital and thus due the State general fund (explained later in the section on liabilities). The cash on hand represents petty cash and change funds in the business office (\$125) and nurse's station (\$25). These funds are used to give change when payments for services are received and for minor expenses such as postage and freight.

**2. Accounts receivable.** The accounting records of the Kauai Veterans Memorial Hospital show, on the accrual basis, accounts receivable of \$97,155. This sum represents the uncollected balance of hospital revenue at June 30, 1968. The following is a summary of these accounts receivable.

Patients . . . . .	\$43,528
Plantations . . . . .	12,362
HMSA . . . . .	10,310
Medicare . . . . .	19,194
Medicaid . . . . .	10,106
Contractual Reimbursements . . . . .	1,655
	\$97,155

Patient receivables (\$43,528) are monies due from individual patients for services rendered by the hospital. Plantation receivables (\$12,362) and HMSA receivables (\$10,310) are amounts collectible from the plantations and HMSA for hospital services provided the members of their health benefit plans. Medicare<sup>5</sup> receivables (\$19,194) and medicaid<sup>6</sup> receivables (\$10,106) are amounts that the hospital is entitled to receive as provisional payments for services rendered to medicare and medicaid patients during the fiscal year. Contractual reimbursements (\$1,255 from medicaid and \$400 from medicare) are claims for the difference between the reasonable cost of providing services to medicare and medicaid patients during the fiscal year and the amount of provisional payments received and receivable by the hospital for these services. These claims are subject to audits by representatives of medicare and medicaid.

Of the total accounts receivable, the hospital has estimated that approximately \$5,271 will be uncollectible. This uncollectible amount is recorded by a bookkeeping entry on the books of the hospital as "allowance for doubtful accounts." Excluding this allowance, the net accounts receivable on June 30, 1968 was \$91,884.

<sup>5</sup>Medicare is a federal health insurance program for the aged authorized under the Social Security Act.

<sup>6</sup>Medicaid is a federal grant-in-aid program under the Social Security Act which provides funds on a matching basis with the states to persons eligible to receive public assistance for medical care.

In addition to the above accounts receivable, the accounting records of the hospital show that an additional \$21,210 was due the hospital on June 30, 1968. However, this amount is not reflected in the hospital's financial statement (Table I) because it consists of accounts which the hospital, with the concurrence of the county attorney, considers to be uncollectible and worthless. These worthless accounts include both pre-Act 97 county accounts receivable and post-Act 97 State accounts receivable.

Despite the uncollectibility and worthlessness of these accounts, they have continuously remained on the books of the hospital. It would appear that old accounts, which are clearly uncollectible, should be deleted from the records. With respect to State receivables, such deletion is possible under section 40-82, HRS. This section provides that any State agency may delete from its records any account which has been delinquent for more than two years and which the attorney general has determined to be uncollectible because the debtor cannot be located, the debtor is unknown or cannot be identified, the debtor has filed bankruptcy, or the account is uneconomical or impractical to collect. The hospital, however, has not availed itself of this statutory provision and has made no reference to the attorney general for his determination on the collectibility of accounts outstanding for more than two years.

With respect to county receivables, there is apparently no statutory authority that permits the removal of clearly uncollectible accounts from the records. *We recommend that with*

respect to State accounts receivable, the hospital refer all such accounts as it deems uncollectible to the State attorney general for his determination as to their collectibility, and that with respect to county accounts receivable the State legislature enact legislation similar to section 40-82, HRS, to permit the deletion of those county accounts which are clearly uncollectible from the records of the hospital.<sup>7</sup>

3. *Inventories of drugs and supplies.* Inventories on hand, totaling \$29,306 at June 30, 1968, are valued at cost and include a wide variety of items such as drugs and pharmaceuticals, groceries, hospital and office supplies, and linen.

**Liabilities, reserve and fund balance.** 1. *Accounts payable.* Accounts payable of \$14,252 represents the legal obligations of the hospital that remained unpaid as of June 30, 1968.

2. *Unrequired balance of appropriation due the State general fund.* The unrequired balance of appropriation due the State general fund of \$94,536 is the full amount of the State general fund appropriation, authorized by section 1, Act 54, SLH 1967, to the hospital for the fiscal year 1967-1968. It appears as *due* the general fund

<sup>7</sup>The passage of House Bill No. 740, H.D. 1, S.D. 1, 1969 legislative session, conceivably will require the transfer of these county accounts receivable to the State as "personal property" used in the operation and maintenance of the hospital. If such be the case, these county accounts receivable will become State property and be subject to section 40-82, HRS.

because no part of the appropriated amount was required in the operation and maintenance of the hospital during the fiscal year; the amount of hospital receipts in the fiscal year was more than sufficient to finance the total requirements of the hospital. (See chapter 4 for additional discussion on this matter.)

3. *Reserve for encumbrances.* The reserve for encumbrances of \$25,129 represents the total estimated cost of equipment, material and supplies committed to be purchased, but not received or paid for as of June 30, 1968.

4. *Fund balance.* The fund balance at June 30, 1968 showed an increase over that existing on June 30, 1967. The increase resulted from (a) a transfer of funds from the Maui Memorial Hospital (\$688),<sup>8</sup> (b) reimbursements of expenses incurred in fiscal year 1966-1967 (\$9,806), and (c) excess of revenue over expenditures in fiscal year 1967-68 (\$17,211 under the accrual method and \$5,734 under the modified cash method).

<sup>8</sup>The Maui Memorial Hospital ended the 1965-1966 fiscal year with a surplus of \$35,960. The governor recommended that this surplus be used to purchase equipment for all Act 97 hospitals and that the allocation of this surplus among the hospitals be based on a review of equipment requirements and priorities by a committee created by the State department of health. An equipment review committee was formed in early 1967. By October 1967, this committee agreed on certain allocations of the surplus funds among the Act 97 hospitals. The Kauai Veterans Memorial Hospital's allocation amounted to \$688. The use of excess receipts of special fund hospitals for any purpose approved by the governor or the State director of budget and finance has traditionally been authorized by the legislature in the general appropriation acts enacted since 1961. See footnote 2, chapter 3, *supra*.

There is a difference of \$146,319 in the fund balance between the accrual method of accounting (\$162,697) and the modified cash method (\$16,378), because the modified cash method does not recognize certain balance sheet items which are recognized in the accrual method. The following reconciliation describes these items.

Fund balance, accrual basis . . . . .		\$162,697	
Less:			
Items not recognized as assets under the modified cash basis of accounting:			
Accounts receivable . . . . .	\$91,884		
Inventories, at cost . . . . .	29,306		
Encumbered items not recognized as liabilities under the accrual basis of accounting . . . . .	25,129		
		<u>146,319</u>	
Fund balance, modified cash basis . . . . .			<u>\$ 16,378</u>

In essence, as noted on the balance sheet, the accrual - based fund balance of \$162,697 represents all assets (cash, receivables, and inventory) owned, and all legal obligations outstanding on June 30, 1968; and the modified cash-based fund balance of \$16,378 represents the excess liquid assets (cash minus all legal obligations and commitments to purchase).

The liquid (cash) excess of \$16,378 consists of \$150 in petty cash funds established many

years ago (the purposes of the petty cash funds were described earlier in this chapter) and \$16,228 in surplus funds. As surplus, the \$16,228 is in the hospital's special fund, but the State department of health has restricted the hospital from using the surplus unless prior authorization is granted by the State department and other concerned agencies.<sup>9</sup>

### Statement of Revenue and Expenditures

The statement of revenue and expenditures of the Kauai Veterans Memorial Hospital for the year ended June 30, 1968 is displayed in Table II.

As in the case of the balance sheet, the statement of revenue and expenditures is displayed on both the accrual and modified cash bases of accounting. The transactions represented by the figures noted for each category under the accrual basis are not necessarily the same as those transactions represented by the figures under the modified cash basis. This is because:

<sup>9</sup>As noted earlier, none of the legislatively appropriated sum was required by the hospital in fiscal year 1967-68. The question, of course, is to what use might the \$16,228 surplus be put.

**TABLE II**  
**STATEMENT OF REVENUE AND EXPENDITURES**  
**SPECIAL FUND**  
**Year Ended June 30, 1968**

	Actual Amount		Budget	Modified Cash Over [Under] Budget
	Accrual	Modified Cash		
Revenue:				
Net patient services (Schedule I) .....	\$479,483			
Other revenue .....	<u>3,226</u>			
Total revenue .....	<u>\$482,709</u>	<u>\$491,330</u>	<u>\$339,813</u>	<u>\$151,517</u>
Expenditures:				
Personal services .....	302,868	302,868	293,284	9,584
Other current expenditures (Schedule II) .....	144,725	153,134	114,945	38,189
Equipment .....	<u>17,905</u>	<u>29,594</u>	<u>26,120</u>	<u>3,474</u>
Total expenditures ....	<u>\$465,498</u>	<u>\$485,596</u>	<u>\$434,349</u>	<u>\$ 51,247</u>
Excess of revenue over expenditures (expenditures over revenue) (Table I) ....	<u>\$ 17,211</u>	<u>\$ 5,734</u>	<u>[\$ 94,536]</u>	<u>[\$100,270]</u>

The statement on the *accrual* basis includes, in "revenue," all amounts which were *earned* and thus *accrued* to the hospital during the fiscal year. Some of these may or may not have been paid during the fiscal year. The statement on the *modified cash* basis includes, in "revenue," only those amounts which the hospital *actually collected* during the fiscal year. The receipts may have been for accounts which accrued in prior fiscal years.

The statement on the accrual basis includes, in "expenditures," all amounts which were *incurred*<sup>10</sup>— that is, became *legally payable*—by the hospital during the fiscal year. The statement on the *modified cash* basis includes in "expenditures," all amounts which not only became legally payable during the fiscal year, but also all amounts which the hospital set aside or committed or *encumbered* to be used in the future for specific purposes.

<sup>10</sup>Under the accrual method of accounting, supplies and inventorial items for which expenditures are incurred are recorded and carried as assets until such time as the items are utilized in the operations of the hospital. Only as the items are used are the expenditures recognized as expense or cost of operations. Under the modified cash basis, all expenditures are considered as expense or cost when made, regardless of when the items for which the expenditures were made are used.

On the accrual basis, the statement enables the hospital to determine how much revenue was generated as a result of the costs incurred during the fiscal year. On the modified cash basis, the statement enables one to compare the cash transactions had and obligations made by the hospital during the fiscal year with those anticipated in the budget. The modified cash basis is used by the State for budgeting and funding purposes. Thus, any comparison between what actually happened and what was budgeted must be confined to the amounts shown under the modified cash basis.

Specific variances between the accrual method and the modified cash basis of accounting for the hospital's revenue and expenditures and the variances between what actually took place under the modified cash basis and the budget are as follows.

**Revenue. 1. Net patient services revenue.** Net patient services revenue (\$479,483) is the income earned by the hospital for various services rendered to patients during the fiscal year. A breakdown of these various services is detailed on Schedule I of Table II.

**2. Other revenue.** Other revenue represents income generated primarily from charges for the use of hospital facilities by, and miscellaneous services rendered to, various non-patients. In fiscal year 1967-1968, other revenue from charges to non-patients totaled \$3,226 under the accrual basis.

**SCHEDULE I OF TABLE II**  
**Schedule of Patient Services Revenue**  
**Year Ended June 30, 1968**

		<b>Accrual Basis</b>
Daily Patient Services		
Room service . . . . .	\$294,402	
Newborn nursery . . . . .	<u>7,985</u>	\$302,387
Other Nursing Services		
Operating room . . . . .	\$ 23,217	
Delivery room . . . . .	7,695	
Central supply . . . . .	14,869	
Emergency service . . . . .	<u>10,272</u>	56,053
Clinical Services		
Laboratory . . . . .	\$ 47,241	
Blood bank . . . . .	5,334	
Radiology . . . . .	20,142	
Pharmacy . . . . .	26,308	
Anesthesiology . . . . .	7,621	
Inhalation therapy . . . . .	8,593	
Physical therapy . . . . .	399	
Electrocardiogram . . . . .	2,928	
Ambulance . . . . .	<u>1,490</u>	<u>120,056</u>
Total patient service revenue . . . . .		\$478,496
Add: Adjustments to revenue . . . . .		<u>987</u>
Net patient services revenue . . . . .		<u>\$479,483</u>

3. *Total revenue.* Total revenue for the year ended June 30, 1968 was \$482,709 under the accrual basis and \$491,330 under the modified cash basis. The difference in the two figures is because the transactions reflected in the \$482,709 are not the same as those transactions reflected in the \$491,330. The accrual-based \$482,709 represents the total revenue earned as a result of services provided during the fiscal year and gave rise to a right in the hospital to collect receipts; the modified cash-based \$491,330 represents payments made to the

hospital during the fiscal year regardless of when the services were provided (some of the services may have been provided in prior fiscal years).

The modified cash-based "total revenue" of \$491,330 (the amount actually collected during the fiscal year) is \$151,517 more than the \$339,813 budgeted for the year. This increase resulted primarily because the actual, daily, patient census (32.8) was 31 percent more than anticipated (25.0).

### Expenditures

Expenditures for personal services, other current expenditures, and equipment totaled \$465,498 on the accrual basis and \$485,596 on the modified cash basis. A detailed listing of other current expenditures (accrual basis) is presented in Schedule II of Table II.

Included in the accrual-based \$465,498, but not in the modified cash-based \$485,596, are the prior year's *encumbrances* which became *legal obligations* payable by the hospital during fiscal year 1967-1968. These encumbrances were included as expenditures on the modified cash basis (but not on the accrual basis) in the prior year's statement of revenue and expenditures, and thus do not appear again as expenditures on the modified cash basis in fiscal year 1967-68's statement. Despite the inclusion of these prior year's encumbrances, the total expenditures on the accrual basis were \$20,098 less than the total expenditures on the modified cash basis in fiscal year 1967-68. This is because the modified

cash-based \$485,596 for fiscal year 1967-68 includes new encumbrances, the total of which far exceeds the amount of the prior year's encumbrances.

**SCHEDULE II OF TABLE II**  
**Schedule of Other Current Expenditures**  
**Year Ended June 30, 1968**

		Accrual Basis
<b>Nursing Services</b>		
Central supply .....	\$13,164	
Operating room .....	4,611	
Medical and surgical .....	3,155	
Others .....	<u>470</u>	\$ 21,400
<b>Clinical Services</b>		
Laboratory .....	\$24,788	
Pharmacy .....	19,320	
Radiology .....	10,472	
Blood bank .....	4,451	
Inhalation therapy .....	2,895	
Anesthesiology .....	1,764	
Electrocardiogram .....	1,406	
Medical records .....	1,128	
Others .....	<u>577</u>	66,801
<b>House Services</b>		
Dietary .....	\$17,784	
Plant utilities .....	13,300	
Laundry and linen .....	4,925	
Housekeeping .....	2,752	
Building and grounds .....	1,386	
Automotive .....	<u>556</u>	40,703
<b>General and Administrative</b>		
Employee benefits .....	\$ 5,895	
Administration .....	4,657	
Telephone and intercom ..	3,142	
Insurance .....	<u>2,127</u>	15,821
Total other current expenditures . . . .		<u>\$144,725</u>

The modified cash-based \$485,596 exceeds the budgeted amount of \$434,349 by \$51,247. This excess in expenditures was financed entirely by increased hospital receipts, internal

“savings,” and funds transferred from the Maui Memorial Hospital. A discussion of the major variances between actual and budgeted expenditures follows.

1. *Personal services.* Salaries of approximately 47 employees, totaling \$302,868, consumed approximately 62 percent of the hospital's total expenditures. The \$302,868 that was expended for personal services exceeded the budgeted amount of \$293,284 by \$9,584. This excess resulted primarily from salary increases prompted by a reclassification of the nursing and hospital support positions. The reclassification occurred as a part of the revision of the statewide classification system presently being conducted by the State department of personnel services (DPS). The DPS announced the commencement of its study of the nursing and hospital support positions in November 1966 and completed it in July 1967. The actions taken were made retroactive to December 1, 1966.<sup>11</sup> Consequently, the fiscal impact of the reclassification actions was beyond the control of the hospital.

<sup>11</sup>The action taken by the DPS on this matter was apparently made without prior consideration of the State's ability to finance the increased cost of salaries. This is made evident in a memorandum dated September 1967 (which was after the reclassification was completed) from the State director of finance to the State director of the department of health in which he stated (in part), “While the means of financing this additional cost has not been fully ascertained, it is our hope that through the use of excess receipts, deferment of non-essential purchases of equipment, and transfers, the greater part or all of the costs can be met.” This kind of reclassification action taken by the DPS without involving the State director of finance to ascertain the cost implications of the intended action is reviewed in our audit report no. 69-4, entitled *General Audit of the Department of Personnel Services*, dated February 1969. See particularly part II, chapters 2 and 3 of that report.

2. *Other current expenditures.* Expenditures for other current services were primarily for materials and supplies used in the operation and maintenance of the hospital. Actual expenditures of \$153,134 exceeded the budgeted amount of \$114,945 by \$38,189. This excess resulted primarily because the actual daily, patient census (32.8) was 31 percent more than that estimated in the budget (25.0).

3. *Equipment.* Equipment expenditures of \$29,594 exceeded the budgeted amount of \$26,120 by \$3,474. The reasons for the increase in equipment purchases follow.

a. New equipment purchase, per allocation of the Maui Memorial Hospital's surplus by State department of health's equipment review committee . . . . .	\$ 688 <sup>12</sup>
b. Excess of actual cost of new ambulance (\$11,443) over budget estimate (\$10,000) . .	1,443
c. Additional equipment requirements to service a higher daily, patient population . .	<u>1,343</u>
Total . . . . .	<u>\$ 3,474</u>

**Excess of total revenue over expenditures.** In fiscal year 1967-1968, the operation and maintenance of the Kauai Veterans Memorial Hospital resulted in an excess of revenue over expenditures of \$17,211 on the *accrual* basis

<sup>12</sup>See footnote 8, *supra*, this chapter.

and \$5,734 on the *modified cash* basis. Thus, no part of the appropriated amount was required by the hospital. There are certain expenditures which were made by other State and county agencies on behalf of the hospital that are not reflected in the financial statements presented in this chapter. If these expenditures, totaling \$47,525, are considered, the hospital in fact sustained an operating loss of \$30,314, rather than a gain of \$17,211. These other expenditures and the agencies making them are as follows:

a. Fringe benefits for hospital employees (including the State's portion of FICA taxes and retirement system contributions) expended by the State department of budget and finance . . . . .	\$30,250
b. County administrative cost (i.e. the cost of staff services provided by the county of Kauai to the hospital) expended by the State department of budget and finance . . .	17,000
c. Interest on bonds issued by the county of Kauai to finance the construction of the hospital building, expended by the county of Kauai . . . . .	<u>275</u>
	<u>\$47,525</u>

The above expenditures are not included in the hospital's financial statements because they were not made from the Kauai Veterans Memorial Hospital's special fund. Monies for these items were appropriated and allotted to the State department of budget and finance and the county of Kauai. The hospital had no control over and no responsibility for these expenditures.

## Inventory of Property

A summary inventory of the items under the control and responsibility of the hospital at June 30, 1968 is as follows.

Land .....		\$ 21,146	
Land Improvements .....		27,362	
Building .....		393,273	
Fixed Equipment .....		72,161	
Automobiles .....		6,731	
Major Movable Equipment .....		133,645	
Minor Equipment .....		<u>15,614</u>	
			\$669,932
Less depreciation accumulated:			
Prior to July 1, 1967 .....	\$216,841		
During the year ended			
June 30, 1968 .....	<u>22,154</u>		<u>238,995</u>
Total Property (Net) .....			<u>\$430,937</u>

All property is valued at cost, except for donated items which are valued at market value estimated at the time of donation. Governmental units do not ordinarily record depreciation; the cost of acquiring property, once paid for, is considered sunk, and is not thereafter recognized in funding and budgeting. However, effective July 1, 1966, the hospital adopted the practice of recording depreciation of property. It did so because depreciation is an allowable expense in computing costs reimbursable by the federal government under the medicare and medicaid programs.

## Chapter 4

### SELECTED PROBLEMS

This chapter comments on certain operational practices of the Kauai Veterans Memorial Hospital. Some of the issues noted here are similar to those we found at the Kula Sanatorium and the Hilo Hospital when we conducted audits of those institutions. Our recommendations in these cases are generally similar to those we made in our reports on the audits of the Kula Sanatorium<sup>1</sup> and the Hilo Hospital.<sup>2</sup>

#### Return of Unrequired Balance of Appropriation to the State General Fund

As discussed in chapter 3, in fiscal year 1967-68, the hospital did not require the use of any part of the legislatively appropriated sum of \$94,536. This sum, therefore, was, on June 30, 1968, refundable to the State general fund. The return of this sum, however, was unduly delayed. It was not until April 1969, nine months after the close of the fiscal year, that the

<sup>1</sup>Legislative Auditor, *Management Audit of Kula Sanatorium: A Report to the Governor and the Legislature of the State of Hawaii*, report no. 67-2, February 1967.

<sup>2</sup>Legislative Auditor, *Financial Audit of the Hilo Hospital: A Report to the Governor and the Legislature of the State of Hawaii*, report no. 68-8, April 1968.

money was returned to the State general fund. *We recommend that the hospital take such necessary measure as to insure the expeditious return of all future unrequired appropriation balance.*

### Vending Machine

There is a vending machine in the hospital building. Revenue from this machine is used by the hospital's employee association. This situation is not unique to the Kauai Veterans Memorial Hospital. Other public institutions and agencies throughout the State do from time to time install vending machines in public buildings and utilize the revenue for the benefit of employees or, in some cases, patients.<sup>3</sup> Revenue generated from the use of space in public buildings (such as vending machines in public hospitals) is public funds.

We do not question the benefits derived from the use of vending machine revenue for employees' activities, but there is neither a statute nor governmental policy which permits such non-operational use of what otherwise is public funds. *Until some statutory authority is found and governmental policy formulated to*

<sup>3</sup>Legislative Auditor, *Management Audit of Kula Sanatorium*, pp. 82-83, and *Financial Audit of the Hilo Hospital*, p. 22.

*permit earmarking of the income for use by employees, we recommend that all revenue from the vending machine be treated and deposited as hospital revenue and included in the hospital's revenue estimates for budget purposes.*

In August 1968, the State department of health requested the State attorney general for an opinion on the legality of using vending machine revenue for employee and patient purposes. The attorney general has not as yet rendered such opinion.

### Free Coffee for Employees

At the time of our audit, the hospital had a long established practice of providing free coffee in the morning and afternoon to hospital employees. There was no justifiable reason for this gratuity. It constituted an unwarranted preferential treatment of the Kauai Veterans Memorial Hospital employees over other governmental employees.<sup>4</sup> We recommended to the hospital that this practice be discontinued immediately. We are pleased to report that prior to the writing of this report, the hospital adopted this recommendation. Hospital employees are now required to pay for coffee.

<sup>4</sup>Legislative Auditor, *Financial Audit of the Hilo Hospital*, p. 23.

## Fidelity Bond

The hospital purchases fidelity bonds to insure itself of performance by hospital employees holding positions of trust. We believe this is an unnecessary expenditure of funds. Identical insurance coverage can be afforded the hospital at less cost by merely including the hospital's employees along with all State employees holding positions of trust under the State's *blanket* comprehensive crime policy

which is administered by the State department of accounting and general services. We understand that the employees of some of the other Act 97 hospitals are insured under the State's policy. *We recommend that the hospital discontinue purchasing its own fidelity bond and, together with the State department of health, make necessary arrangements with the State department of accounting and general services to include the hospital employees within the State's comprehensive crime policy.*

## PART III SUMMARY

Section 23-4, Hawaii Revised Statutes, requires the office of the auditor to conduct post-audits of all transactions and of all books and accounts kept by State departments and its political subdivisions. Pursuant to this requirement, this office examined the books and accounts of the Kauai Veterans Memorial Hospital and the transactions noted therein for the fiscal period July 1, 1967 to June 30, 1968.

The audit was conducted to determine the propriety of the hospital's financial transactions, the accuracy and reliability of its financial records, and the adequacy of the hospital's controls to safeguard its assets against loss, waste, fraud and extravagance.

The examination covered the hospital's special fund and the property which the hospital is authorized to receive, manage and invest. Our major findings and recommendations with respect to internal control, the special fund, and certain practices of the hospital are summarized below.

### Internal Control

A system of internal control is required to insure the accuracy and reliability of financial data, to promote operational efficiency, and to

assure adherence to laws, policies, rules and regulations. Included in any system of internal control is the principle of "cross-check"—that is, the separation of duties such that no one individual handles all phases of a transaction.

**1. General control.** The smallness in size of the hospital staff precludes an appropriate separation of duties for control purposes in the area of cash, accounts receivable and inventory controls. Under such circumstances, constant surveillance on the part of the hospital's management is the principal and only feasible means of safeguarding the assets under its control.

**2. Compliance with perquisite policies.** The State department of health's policy on perquisites which is applicable to the hospital requires all executive officers of divisions to submit reports on all employees to whom perquisites have been authorized. Although employees of the hospital receive certain perquisites, no reports on employee perquisites have been submitted by the hospital to the director of health. *We recommend that the hospital adhere to the State policy and immediately submit the required reports to the director of health.* A review of the perquisites will give the director a chance to determine whether the perquisites are properly allowable under State policies.

3. **Inventory control.** At the time of our audit, the hospital was not maintaining an inventory of drugs and supplies under a perpetual inventory system. As of the writing of this report, the hospital is in the process of placing all drug items on a perpetual inventory system. The hospital expects the system to be fully implemented at the beginning of fiscal year 1969-1970. *We concur with the hospital's present course of action and recommend that it consider placing other major items contained in the inventory of goods on a perpetual inventory system.*

4. **Depositing of cash receipts.** The hospital generally deposits cash receipts twice a week rather than on a daily basis. There appears to be no justifiable reason for this practice. Daily deposits minimize the amount of funds kept on hand, thus reducing the risk of losing cash by theft or misappropriation. *We recommend that the hospital immediately adopt the practice of depositing all cash receipts on a daily basis.*

### Special Fund

The Kauai Veterans Memorial Hospital and all of its programs are funded by a special fund. The special fund receives its resources from charges to patients for services rendered. To the extent that actual hospital receipts in a fiscal year are insufficient to pay for all operating costs, the special fund is supplemented by State

appropriation. The financial statements of the special fund show both the cash position and transactions of the hospital under the modified cash basis of accounting, and its proprietary position and rights under the accrual basis of accounting.

1. **Opinion on financial statements.** In our opinion, the financial statements of the special fund presented on the *accrual* basis of accounting fairly present the assets and liabilities of the fund at June 30, 1968 and the results of the hospital's operations for the fiscal year July 1, 1967 to June 30, 1968. With respect to the figures presented on the *modified cash* basis, in our opinion, the financial statements fairly present the cash balance, liabilities and commitments of the fund at June 30, 1968 and the results of revenue collected and expenditures made and obligated on account of the fund for the fiscal year July 1, 1967 to June 30, 1968.

2. **Balance sheet.** On the accrual basis, the hospital had assets totaling \$271,485 and liabilities of \$108,788, for a fund balance of \$162,697. On the modified cash basis, it had assets of \$150,295, liabilities of \$108,788 and encumbrances of \$25,129, for a fund balance of \$16,378. The difference of \$146,319 in the fund balances between the two methods of accounting is due to the inclusion of non-liquid assets (accounts receivable and inventories) totaling \$121,190 and the exclusion of encumbrances totaling \$25,129 on the accrual basis.

In addition to the accounts receivable (accrual basis) reflected in the hospital's financial statements, additional accounts which the hospital considers uncollectible (\$21,210) are maintained in the accounting records. Some of the uncollectible accounts are county receivables (pre-Act 97) and others are State receivables (post-Act 97). With respect to county receivables, there is currently no legal means of deleting uncollectible accounts from the hospital's records. With respect to State receivables, section 40-82, HRS, provides for the deletion of uncollectible accounts with the approval of the State attorney general; however, the hospital has not availed itself of this statutory provision. *We recommend that with respect to State accounts receivable, the hospital refer all such accounts as it deems uncollectible to the State attorney general for his determination as to their collectibility, and that with respect to county accounts receivable, the State legislature enact legislation similar to section 40-82, HRS, to permit the deletion of those county accounts which are clearly uncollectible from the records of the hospital.*

**3. Revenue and expenditures.** *a.* During the fiscal year, hospital revenue totaled \$482,709 on the accrual basis and \$491,330 on the modified cash basis. The difference in the two figures is that transactions under the accrual basis reflect the hospital's right to collect receipts, whereas, transactions under the modified cash basis represent cash actually collected. The modified cash-based \$491,330 was \$151,517 over the

budgeted amount of \$339,813. Actual collection exceeded the amount anticipated in the budget because the actual daily, patient census was 31 percent more than the budgeted census.

*b.* Expenditures during the fiscal year totaled \$465,498 on the accrual basis and \$485,596 on the modified cash basis. The accrual-based figure includes and the modified cash-based figure excludes prior year's encumbrances which became legally due and payable in fiscal year 1967-1968, and the accrual-based figure excludes and the modified cash-based figure includes encumbrances made during the fiscal year. The net difference between the two figures is \$20,098. The modified cash-based \$51,247 is more than the amount budgeted for the fiscal year. The increase in actual expenditures over the amount budgeted was due to (1) the nursing and support position reclassification actions taken by the State department of personnel services, and (2) a 31 percent increase in daily, patient census over budget estimates.

*c.* In fiscal year 1967-1968, the operation and maintenance of the hospital resulted in an excess of revenue over expenditures of \$17,211 under the accrual basis and \$5,734 under the modified cash basis. Since revenue exceeded expenditures, no part of the \$94,536 appropriated to the hospital by the State legislature was required by the hospital.

## Selected Problems

Certain operational practices of the Kauai Veterans Memorial Hospital deserve comment. Some of these practices are similar to those which existed at the Kula Sanatorium and the Hilo Hospital when we conducted audits of those institutions (see our audit reports entitled, *Management Audit of Kula Sanatorium* and *Financial Audit of the Hilo Hospital*).

1. **Return of unrequired balance of appropriations to the State general fund.** Since *actual* hospital receipts were sufficient to finance the total requirements of the hospital, the \$94,536 that was appropriated and allotted to the hospital for the fiscal year as a supplement to *estimated* hospital receipts was required to be returned to the State general fund. The return, however, was unduly delayed and was not made until April 1969, nine months after the close of the fiscal year. *We recommend that the hospital take such necessary measures as to insure the expeditious return of all future unrequired appropriation balance.*

2. **Vending machine.** Revenue from the vending machine in the hospital building is used by the hospital's employee association. Revenue generated from the use of public buildings constitutes public funds. As public funds, there must be some earmarking under legal authority

to enable the use of the revenue for a special purpose. We find neither a statute nor governmental policy which permits the use of the vending machine revenue for employee's benefit. *Until some statutory authority is found and government policy formulated to permit earmarking of the income for use by employees, we recommend that all revenue from the vending machine be treated and deposited as hospital revenue and included in the hospital's revenue estimates for budget purpose.*

3. **Free coffee for employees.** At the time of our audit, the hospital was providing free coffee to its employees in the morning and afternoon. We saw no justification for this practice and recommended immediate discontinuance of this gratuity. The hospital has adopted this recommendation and its employees are now required to pay for coffee.

4. **Fidelity bond.** The hospital purchases fidelity bonds to insure performance by its employees holding positions of trust. The State can provide identical insurance coverage at less cost under its *blanket* comprehensive crime policy. *We recommend that the hospital discontinue purchasing its own fidelity bond and, together with the State department of health, make necessary arrangements with the State department of accounting and general services to include the hospital employees within the State's comprehensive crime policy.*

**PART IV**  
**A MEMORANDUM ON THE COMMENTS MADE BY THE AFFECTED AGENCIES**

A preliminary report on the audit of the Kauai Veterans Memorial Hospital was completed in May 1969. We distributed copies of the report to the State department of health and the Kauai Veterans Memorial Hospital via transmittal letters, copies of which are attached as Attachment nos. 1 and 2. The agencies were requested to submit to us their comments no later than May 20, 1969.

The comments of the State department of health are attached as Attachment no. 3. The comments of the Kauai Veterans Memorial Hospital are attached as Attachment no. 4.

We are pleased to note that the agencies agree with our recommendations and indicate that the recommendations are being implemented.

Clinton T. Tanimura  
Auditor

ATTACHMENT NO. 1

*COPY*

THE OFFICE OF THE AUDITOR  
State of Hawaii  
Iolani Palace  
Honolulu, Hawaii 96813

May 8, 1969

Dr. Walter B. Quisenberry  
Director  
Department of Health  
State of Hawaii  
Honolulu, Hawaii

Dear Dr. Quisenberry:

Enclosed is a copy of our preliminary report on the financial audit of the Kauai Veterans Memorial Hospital for the fiscal year ended June 30, 1968. The term, "preliminary," indicates that the report has not been released for general distribution. However, copies of the report have been sent to the Superintendent of the Kauai Veterans Memorial Hospital, the Mayor of the County of Kauai, the Governor, and the presiding officers of both houses of the State legislature.

I would appreciate receiving your written comments on this report. I have also asked the hospital for its comments. All comments must be in our hands by May 20, 1969. The report will be finalized and released shortly thereafter.

If you wish to discuss the report with us, we will be pleased to meet with you on or before May 14, 1969. Please call our office to fix an appointment. A "no call" will be assumed to mean that a meeting is not required.

We are deeply thankful for the assistance received by our representatives from your staff.

Sincerely,  
/s/ Clinton T. Tanimura  
Clinton T. Tanimura  
Legislative Auditor

Encl.

Clinton T. Tanimura  
Auditor

ATTACHMENT NO. 2

*COPY*

THE OFFICE OF THE AUDITOR  
State of Hawaii  
Iolani Palace  
Honolulu, Hawaii 96813

May 8, 1969

Mr. Frank Crabtree  
Superintendent  
Kauai Veterans Memorial Hospital  
Waimea, Kauai 96796

Dear Mr. Crabtree:

Enclosed is a copy of our preliminary report on the financial audit of the Kauai Veterans Memorial Hospital for the fiscal year ended June 30, 1968. The term, "preliminary," indicates that the report has not been released for general distribution. However, copies of the report have been transmitted to the Mayor of the County of Kauai, the Director of the State Department of Health, the Governor, and the presiding officers of both houses of the State Legislature.

The report contains several recommendations. I would appreciate receiving your written comments on them, including information as to the specific actions you have taken or intend to take with respect to each of them. I have also asked the Director of the State Department of Health for his comments. All comments must be in our hands by May 20, 1969. The report will be finalized and released shortly thereafter.

If you wish to discuss the report with us, we will be pleased to meet with you on or before May 14, 1969. Please call our office to fix an appointment. A "no call" will be assumed to mean that a meeting is not required.

We sincerely appreciate the assistance and cooperation which you and members of your staff have extended to our representatives.

Sincerely,  
/s/ Clinton T. Tanimura  
Clinton T. Tanimura  
Legislative Auditor

Encl.

*COPY*

STATE OF HAWAII  
DEPARTMENT OF HEALTH  
P. O. Box 3378  
Honolulu, Hawaii 96801

May 15, 1969

Mr. Clinton T. Tanimura  
Legislative Auditor  
Office of the Auditor  
State of Hawaii  
Honolulu, Hawaii

Dear Mr. Tanimura:

Re: Financial Audit of the Kauai Veterans Memorial Hospital

This is in response to your request for comments on the subject report.

We believe it to be noteworthy that the operations of Kauai Veterans Memorial Hospital for the 1967-1968 fiscal year were self-supporting and did not require the expenditure of State funds specifically appropriated in its budget for day-to-day operations. This is a significant achievement and represents an objective which we intend to pursue in the operation of Act 97/203 hospitals to the fullest extent that circumstances and constraints permit.

With respect to the recommendations, a coordinated effort between this department and the hospital staff will be made to implement the required changes and to resolve specific problem areas. Where certain recommendations have general application to several or all hospitals; we will take the necessary actions to handle the problem areas on a system-wide basis.

Clinton T. Tanimura

May 15, 1969

The financial audits of the various County/State hospitals are helpful to us in meeting our management responsibilities. We appreciate the efforts of your office and you may be assured of our continuing cooperation and assistance.

Very sincerely,

/s/ Walter B. Quisenberry

WALTER B. QUISENBERRY, M.D.  
Director of Health

cc: Mayor of Kauai  
Kauai Veterans Memorial Hospital

COPY

KAUAI VETERANS MEMORIAL HOSPITAL  
Waimea, Kauai, Hawaii 96796

May 13, 1969

Mr. Clinton T. Tanimura  
Legislative Auditor  
State of Hawaii  
Iolani Palace  
Honolulu, Hawaii 96813

Dear Mr. Tanimura:

SUBJECT: Financial Audit of KVMH  
FY Ended June 30, 1968

We received your audit report dated May 7, 1969. We wish to make the following corrections and comments:

- I. Corrections  
Page 2, line [13]—Change 1,414 to 1,549 patients admitted.  
Page 3, [EXHIBIT I], line 15—Change 6.8 to 5.9 average length of stay (1967)  
Page 3, [EXHIBIT I], line 15—Change 8.4 to 8.7 average length of stay (1968)
- II. Compliance with Perquisite Policies  
Your recommendation to submit the required perquisite reports to the Director of Health will be forwarded immediately.
- III. Inventory Control  
A perpetual inventory system for drugs and supplies is being implemented and will be ready for fiscal year 1969-1970.
- IV. Depositing of Cash Receipts  
The practice of making daily deposits has been adopted.

Mr. Clinton T. Tanimura

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May 13, 1969

- V. Return of Unrequired Balance of Appropriation  
Future excess funds will be returned at an early date as recommended. After studying your audit, we have broadened our knowledge in the categorizing of fund receipts.
- VI. Vending Machine  
We will follow your recommendation.
- VII. Fidelity Bond  
We shall write to the State Department of Health and arrange for this coverage. This should take effect July 1, 1969, when our current policy expires.

We thank you for the opportunity to comment. Your recommendations are well taken.

Sincerely,

KAUAI VETERANS MEMORIAL HOSPITAL

/s/ Frank Crabtree

Frank Crabtree, Administrator

mhm

cc: Walter B. Quisenberry, M.D., Director of Health  
Honorable Antone K. Vidinha, Mayor, County of Kauai

# PUBLISHED REPORT OF THE LEGISLATIVE AUDITOR

## Audit Reports

- 1966 1. Examination of the Office of the Revisor of Statutes, 66 pp. (out of print).
- 1967 1. Overtime in the State Government, 107 pp.  
2. Management Audit of Kula Sanatorium, 136 pp.
- 1968 1. Financial Audit of the Department of Health for the Fiscal Year Ended June 30, 1967, v.p. (out of print).  
2. Financial Audit of the Department of Planning and Economic Development for the Fiscal Year Ended June 30, 1967, v.p. (out of print).  
3. Financial Audit of the Department of Regulatory Agencies for the Fiscal Year Ended June 30, 1967, v.p. (out of print).  
4. Financial Audit of the Department of Hawaiian Home Lands for the Fiscal Year Ended June 30, 1967, 54 pp.  
5. Financial Audit of the Oahu Transportation Study for the Period July 1, 1962 to August 31, 1967, 68 pp.  
6. Financial Audit of the Hawaii Visitors Bureau for the Period July 1, 1966 to January 31, 1968, 69 pp.  
7. State Capital Improvements Planning Process, 55 pp.  
8. Financial Audit of the Hilo Hospital for the Fiscal Year Ended June 30, 1967, 43 pp.  
9. Financial Audit of the Hawaii Visitors Bureau for the Period July 1, 1967 to June 30, 1968, 42 pp.
- 1969 1. Financial Audit of the General Fund, State of Hawaii, for the Fiscal Year Ended June 30, 1968, v.p.  
2. Financial Audit of the Judicial Branch, State of Hawaii, for the Fiscal Year Ended June 30, 1968, v.p.  
3. Financial Audit of the State Department of Budget and Finance for the Fiscal Year Ended June 30, 1968, v.p.  
4. General Audit of the Department of Personnel Services, State of Hawaii, 129 pp.  
4. A Summary of the General Audit of the Department of Personnel Services, 53 pp.

## Other Reports

- 1965 1. Long and Short Range Programs of the Office of the Auditor, 48 pp. (out of print).  
2. A Preliminary Survey of the Problem of Hospital Care in Low Population Areas in the State of Hawaii, 17 pp. (out of print).
- 1966 1. Procedural Changes for Expediting Implementation of Capital Improvement Projects, 9 pp. (out of print)
- 1967 1. The Large School: A Preliminary Survey of Its Educational Feasibility for Hawaii, 15 pp.  
2. State-City Relationships in Highway Maintenance, and Traffic Control Functions, 28 pp.  
3. Manual of Guides of the Office of the Legislative Auditor, v.p.
- 1969 1. Transcript of Seminar in Planning-Programming-Budgeting for the State of Hawaii, 256 pp.  
2. Airports System Financing Through Revenue Bonds, 9 pp.  
3. Second Annual Status Report on the Implementation of Act 203, Session Laws of Hawaii 1967 (Relating to State-county Relationships), 13 pp.  
4. An Overview of the Governor's 1969-70 Capital Improvements Budget, 61 pp.  
5. A Supplementary Report on the Audit of the Hawaii Visitors Bureau, 2 pp.

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