Financial Audit of the Maui Memorial Hospital and Hana Medical Center

A Report to the Governor and the Legislature of the State of Hawaii

Report No. 96-6
January 1996

THE AUDITOR
STATE OF HAWAII

The Office of the Auditor

The missions of the Office of the Auditor are assigned by the Hawaii State Constitution (Article VII, Section 10). The primary mission is to conduct post audits of the transactions, accounts, programs, and performance of public agencies. A supplemental mission is to conduct such other investigations and prepare such additional reports as may be directed by the Legislature.

Under its assigned missions, the office conducts the following types of examinations:

1. *Financial audits* attest to the fairness of the financial statements of agencies. They examine the adequacy of the financial records and accounting and internal controls, and they determine the legality and propriety of expenditures.

2. *Management audits*, which are also referred to as *performance audits*, examine the effectiveness of programs or the efficiency of agencies or both. These audits are also called *program audits*, when they focus on whether programs are attaining the objectives and results expected of them, and *operations audits*, when they examine how well agencies are organized and managed and how efficiently they acquire and utilize resources.

3. *Sunset evaluations* evaluate new professional and occupational licensing programs to determine whether the programs should be terminated, continued, or modified. These evaluations are conducted in accordance with criteria established by statute.

4. *Sunrise analyses* are similar to sunset evaluations, but they apply to proposed rather than existing regulatory programs. Before a new professional and occupational licensing program can be enacted, the statutes require that the measure be analyzed by the Office of the Auditor as to its probable effects.

5. *Health insurance analyses* examine bills that propose to mandate certain health insurance benefits. Such bills cannot be enacted unless they are referred to the Office of the Auditor for an assessment of the social and financial impact of the proposed measure.

6. *Analyses of proposed special funds* and existing *trust and revolving funds* determine if proposals to establish these funds and existing funds meet legislative criteria.

7. *Procurement compliance audits* and other *procurement-related monitoring* assist the Legislature in overseeing government procurement practices.

8. *Fiscal accountability reports* analyze expenditures by the state Department of Education in various areas.

9. *Special studies* respond to requests from both houses of the Legislature. The studies usually address specific problems for which the Legislature is seeking solutions.

Hawaii's laws provide the Auditor with broad powers to examine all books, records, files, papers, and documents and all financial affairs of every agency. The Auditor also has the authority to summon persons to produce records and to question persons under oath. However, the Office of the Auditor exercises no control function, and its authority is limited to reviewing, evaluating, and reporting on its findings and recommendations to the Legislature and the Governor.

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OVERVIEW

THE AUDITOR
STATE OF HAWAII

Financial Audit of the Maui Memorial Hospital and Hana Medical Center

Summary

The Office of the Auditor and the certified public accounting firm of Deloitte & Touche LLP conducted a financial audit of the Maui Memorial Hospital and Hana Medical Center for the fiscal year July 1, 1994 to June 30, 1995. The audit examined the financial records and systems of accounting and internal controls and tested these for compliance with applicable laws and regulations.

In the opinion of Deloitte & Touche LLP, the financial statements present fairly the Maui Memorial Hospital and Hana Medical Center's financial position and their results of operations for the fiscal year ended June 30, 1995. These statements are in conformity with generally accepted accounting principles.

As defined in the report on the internal control structure, Deloitte & Touche LLP noted no material weaknesses in the internal control structure and its operation. It also noted, with respect to items tested, that the hospital and center have complied with applicable laws and regulations.

We found, however, that the Maui Memorial Hospital could improve its business office operations and security procedures by implementing or revising certain operating procedures. More specifically, cash discounts granted to two insurers may not be authorized or based upon sound reasoning. We estimate these discounts cost the hospital about $3 million in lost revenues. Revenue and collection practices need to be improved. The hospital owes the state general fund almost $16 million and the ability to pay off the debt rests on improving the hospital's revenue and collections. The hospital's utilization review practices should be improved to help contain costs and increase revenues. Internal financial reporting is inadequate. Management needs timely and useful financial information.

We also found that long-term care patients are now occupying acute care beds. Left unchecked, this practice may have serious financial implications. Finally, hospital security procedures should be improved. Security procedures in a hospital should provide a measure of safety for patients and employees, and prevent the loss of hospital assets.

Recommendations and Response

We recommend that the Division of Community Hospitals and the hospital determine the propriety of discounts to insurers. We also recommend that the hospital consider pursuing collection of the discounted amounts.

We recommend that the hospital take steps to improve its revenue and collection practices. The hospital should ensure that patients are billed for all services and supplies by recording requisition information in patient billing records. It should continue to work with the division to improve automated billing procedures and develop electronic billing capabilities. It should obtain and verify insurance coverage for all outpatients and patients treated and discharged by the emergency room. The hospital should prepare patient bills soon after discharge and make sensible payment arrangements for balances due. Additionally, the hospital should verify all insurer payments.

We recommend the hospital expand the role of the utilization review process as a means to contain costs and improve revenues. We also recommend that the hospital prepare budgets and financial reports which include monthly financial statements, comparisons of budgets to departmental activities, cash flow forecasts, and other performance measures.

We further recommend that the division and the hospital develop plans to meet the needs of long-term care patients and determine the fiscal impact of such plans. We also recommend that the hospital strengthen its security procedures by limiting employees' entry and exit to specified doors, limiting use of emergency exits to their designated purpose, requiring all hospital employees to wear identification badges while on duty, and requiring outside contractors to wear visitors' badges and notify the security guards of their schedules.

The department generally concurs with our findings and plans to use our report as a guide for improvement. The department states that it will seriously consider our recommendations and use them to better improve the management and operation of Maui Memorial Hospital/Hana Medical Center. The department believes that converting the Division of Community Hospitals from a division within the Department of Health to a public benefit corporation for community hospitals will enhance its ability to solve problems specific to the hospital.

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Financial Audit of the Maui Memorial Hospital and Hana Medical Center

A Report to the Governor and the Legislature of the State of Hawaii

Conducted by

The Auditor
State of Hawaii
and Deloitte & Touche LLP

Submitted by

THE AUDITOR
STATE OF HAWAII

Report No. 96-6
January 1996

Foreword

This is a report of our financial audit of the Maui Memorial Hospital and Hana Medical Center for the fiscal year July 1, 1994 to June 30, 1995. The audit was conducted pursuant to Section 23-4, Hawaii Revised Statutes, which requires the State Auditor to conduct postaudits of all departments, offices, and agencies of the State. The audit was conducted by the Office of the Auditor and the certified public accounting firm of Deloitte & Touche LLP.

We wish to express our appreciation for the cooperation and assistance extended by the officials and staff of Maui Memorial Hospital, the Hana Medical Center, and the Division of Community Hospitals.

Marion M. Higa
State Auditor

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Chapter 1

Introduction

This is a report of our financial audit of the Maui Memorial Hospital and Hana Medical Center. The audit was conducted by the Office of the Auditor and the independent certified public accounting firm of Deloitte & Touche LLP.

The audit was conducted pursuant to Section 23-4, Hawaii Revised Statutes, which requires the Auditor to conduct post audits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State and its political subdivisions.

Background

Maui Memorial Hospital is the successor to the old Malulani Hospital, which was established in 1884 under the reign of Queen Kapiolani. The Franciscan Sisters operated the hospital until 1927, at which time the County of Maui assumed full responsibility for its operation and management. Hana Medical Center was established in 1964 and is a diagnostic and treatment center which serves the people of the Hana District of Maui. It is treated as a satellite of Maui Memorial Hospital. In 1967, Act 203, Session Laws of Hawaii, transferred several hospital management functions from the counties to the State, and in 1969, the state director of health was made the sole "governing authority" over all county/state hospitals. In 1989, the Division of Community Hospitals of the State Department of Health was established to be responsible for the planning, construction, improvement, management, control, maintenance, and operation of these hospitals.

Maui Memorial Hospital sits on about 16 acres of state-owned land, is licensed for 180 beds, and currently employs 685 persons. Averaging over 150 patients per day, the hospital had an operating budget in FY1994-95 of approximately $69.8 million. Hana Medical Center, employing 15 people, had an operating budget of approximately $1.2 million in FY1994-95.

Organization

Maui Memorial Hospital is headed by a hospital administrator who is appointed by the director of health. The hospital is organized into nine departments, which are described below.

- Administrative Services is responsible for: personnel, purchasing and storeroom, utilization review, quality assurance, infection control, administration, and risk management.

- Data Processing records, classifies, summarizes, transmits, stores, and retrieves clinical and management information.
- Patient Services is responsible for patient accounting services and financial accounting, budget, and billing services.
- Nursing Services provides nursing care to all patients and is also responsible for operating room supplies and central supplies.
- Clinical Services is responsible for: physical therapy, occupational therapy, respiratory therapy, radiology, laboratory, anesthesia, pharmacy, social services, medical records, and medical library.
- Dietary Services provides clinical dietetic services to patients, as well as food services and meal production, for patients and employees of the hospital.
- Plant Operation and Maintenance is responsible for the general maintenance of the hospital's buildings and equipment.
- Housekeeping provides cleaning services to patients' rooms, hallways, and other parts of the hospital.
- Laundry is responsible for washing and disinfecting hospital linens.

Hana Medical Center is headed by a hospital administrator who is appointed by the director of health. The medical center is organized into three departments, which are described below.

- Nursing Services provides nursing care for outpatient and emergency services, and operates the pharmacy, laboratory, and ambulance.
- Radiology performs radiological procedures for diagnostic purposes.
- Groundskeeping provides grounds maintenance and general housekeeping services.

Management Advisory Committee

Section 323-66, Hawaii Revised Statutes, provides for the establishment of a public health facility management advisory committee in each county. The committee advises the director of health on planning, construction, improvement, maintenance, and operation of the public health facilities within its jurisdiction.

Objectives of the Audit

1. Report on the fair presentation of the combined financial statements of Maui Memorial Hospital and Hana Medical Center for the year ended June 30, 1995.

2. Assess the adequacy, effectiveness, and efficiency of the systems and procedures for the financial accounting, internal control, and financial reporting of Maui Memorial Hospital and Hana Medical Center; and recommend improvements.

3. Ascertain whether expenditures and other disbursements have been made and all revenues and other receipts have been collected and accounted for in accordance with federal and state laws, rules and regulations, and policies and procedures.

Scope and Methodology

We audited the financial records, transactions, accounting systems, and internal controls of Maui Memorial Hospital and Hana Medical Center for the fiscal year July 1, 1994 to June 30, 1995. We also reviewed those transactions, systems, and procedures for compliance with applicable laws and regulations.

The audit examined the accounting, reporting, and internal control structures to identify deficiencies and to make appropriate recommendations for improvements.

The accountants' opinion as to the fairness of the combined financial statements presented in Chapter 3 is that of Deloitte & Touche LLP. The audit was conducted from July 1995 through December 1995. The audit work relating only to Chapter 3 was conducted July 1995 through September 1995. The audit was conducted in accordance with generally accepted government auditing standards.

Chapter 2

Internal Control Practices

Internal controls are steps instituted by management to ensure that objectives are met and resources are safeguarded. This chapter presents our findings and recommendations on the financial accounting and internal control practices and procedures of Maui Memorial Hospital.

Summary of Findings

We find that Maui Memorial Hospital could improve its business office operations and security procedures by implementing or revising certain operating procedures. More specifically, we find that:

1. Cash discounts granted to two insurers may not be authorized or based upon sound reasoning. We estimate these discounts cost the hospital about $3 million in lost revenues.

2. Revenue and collection practices need to be improved. The hospital owes the state general fund almost $16 million. The ability to pay off the debt rests on improving the hospital's revenue and collections.

3. Internal financial reporting is inadequate. Management needs timely and useful financial information.

4. Long-term care patients are now occupying acute care beds. Left unchecked, this practice may have serious financial implications.

5. Hospital security procedures should be improved. Security procedures in a hospital should provide a measure of safety for patients and employees, and prevent the loss of hospital assets.

Cash Discounts Granted to Two Insurers may be Improper

For the past several years, Hawaii Medical Services Association (HMSA) and Kaiser Foundation Health Plan have been paying the hospital, at discounted amounts, for services provided to their members —9.5 percent off billings for services to HMSA inpatients and 12.5 percent off billings for Kaiser inpatients and outpatients. We found that these discounts may not have been authorized and that the reasoning behind them is unclear. Therefore, the hospital may not be receiving all amounts due from these companies. The division and the hospital need to take action to resolve the matter.

Revenues in FY 1994-95 from HMSA and Kaiser approximated $27.7 million and $17.7 million, respectively, and the discounts taken are estimated to be about $3 million. The discounts were allegedly negotiated by the former director of health as an incentive to speed up payments from these two payors to all of the division's hospitals. However, we found no documentation to support either the amount of the discounts, or to show that the discounts, in fact, were to "speed up" payments from the two payors.

Although the hospital has a contract with HMSA, we found no written agreement or contract terms authorizing the 9.5 percent discount. Division and hospital staff contend that there is no written authorization for it. On the other hand, HMSA officials allege that the contract allows the discount.

Kaiser has no written contract with the hospital, it simply deducts 12.5 percent from the hospital's eligible charges and sends discounted payments to the hospital. Kaiser bases its discount "on the assumption that the 12.5 percent discount is comparable to the discount HMSA's members are receiving."[1]

We were unable to verify the authorization for the discounts because we found no documentation. Also, we were unable to determine whether the discounts have sped up payments to the hospital. Regardless of whether the discounts are authorized, their size does not make any real economic sense if they are only to expedite payment. The benefit of obtaining payment on time may not match the cost of the discount. For example, a 9.5 percent discount to speed up payment by one month is equivalent to borrowing money at an annual interest rate of 114 percent.

Neither the hospital nor the Division of Community Hospitals has been able to determine whether the hospital is able to recover the amount of the discounts taken by HMSA and Kaiser. The division recently began looking into this issue, but has taken no concrete action to resolve it. The hospital has chosen not to pursue collection of the discounts from HMSA, Kaiser, or even the patients to whom services were provided. This is a significant amount of revenue to simply write off because it is not received.

The division needs to determine whether the discounts taken by HMSA and Kaiser are proper. It also must determine how to recover the amount discounted. The division and the hospital may need to obtain legal assistance from the Attorney General. We urge the hospital and the division to take a more aggressive course of action toward resolution than either has pursued so far.

Recommendations

We recommend that the Division of Community Hospitals and the hospital determine the propriety of these discounts. We also recommend that the hospital consider pursuing collection of the discounted amounts.

Revenue and Collection Practices Need to be Improved

The hospital needs to improve its revenue and collection practices in order to (1) pay moneys it owes the State, and (2) operate autonomously from the Department of Health. The hospital owes the state general fund almost $16 million for past central service and departmental expenses as required by Sections 36-27 and 36-30, Hawaii Revised Statutes. Central service expenses include such items as cash and debt management, accounting, and payroll services provided by other state departments. Departmental expenses include Department of Health administrative and support services costs. In addition, millions of dollars for buildings, improvements, and equipment have been financed by state taxpayers.

Because the Department of Health believes that the hospital can operate more effectively if it were independent, it has begun efforts to remove the hospital's operations from the department and to allow it to operate autonomously. If the hospital is to succeed as an autonomous entity, it must generate sufficient cash to finance its operations and repay moneys owed to the State's general fund.

The hospital needs to develop a method of maximizing the collection of all accounts due it. However, the hospital has historically had difficulty collecting amounts due from patients. Each year an inordinately large percentage of revenues is deemed uncollectible. At June 30, 1995, $13.5 million was deemed to be uncollectible.

In FY1994-95, bad debts expense from patients' accounts totaled $4 million, approximately 6.5 percent of net patient revenues for the year. In prior years, the hospital failed to collect between 6 to 7 percent of its net revenues. This compares unfavorably to the industry average of about 3 percent. If the hospital's collection practices improved to the industry average, we estimate annual collections would increase by $2+ million.

Cash flow can also be increased by improved revenue and collection practices. We found that patients are not always charged for services, billing procedures are inefficient, patients' insurance data is not always obtained, and patients are not required to pay their bills in a timely manner. We also found that insurance payments are not checked for accuracy and the hospital may not be able to collect Medicare claims after January 1, 1996.

Patients are not always charged for services

The hospital should bill all charges to the patients. Because the hospital uses manual processes to record many patient charges, the hospital sometimes loses information and fails to charge patients for all supplies and services provided.

For example, the hospital failed to bill patients for $185,600 worth of supplies used. The hospital uses a manual system to requisition patient supplies; however, this requisition information was not recorded in the hospital's computerized patient billing records. Consequently, patients were not charged for the supplies used.

Manual requisition slips also are used for the following ancillary services: angiography, anesthesia, CT scan, central supply, dialysis, electrocardiogram, emergency room, endoscopy, nuclear medicine, oncology, pharmacy, surgery, and ultrasound. Because of the volume of manual requisition slips used and the inability to account for all requisition slips, there is no assurance that the hospital is charging patients for all of these services.

Information processing is inefficient

Our Report No. 95-21, "*Audit of the Information System of the Division of Community Hospitals,*" identified inefficiencies in the hospital's billing procedures. For example, the hospital manually inputs billing data into a personal computer, when such data is already in the hospital's main computer.[2] This duplication of effort is not only inefficient, but it means that billings cannot be sent out on time. Such delays often contribute to subsequent collection problems.

Patient insurance information is not always obtained

The hospital must obtain accurate patient demographic data and verify insurance coverage so patients and insurance companies can be accurately billed for services rendered. Generally, the hospital does this with inpatients. However, the hospital fails to verify outpatient insurance coverage and does not obtain required insurance pre-approvals. Some insurers will not pay on a claim for which they have not granted "pre-approval." These insurers require that they be informed in advance of the medical procedure to be performed in order to either deny or "pre-approve" insurance coverage for the procedure. The hospital also sometimes fails to obtain required billing information from patients treated and discharged directly from the emergency room.

Outpatient insurance verification

Outpatients served by the hospital are in and out in one day. These patients are treated by doctors who are not employed by the hospital, but who use the hospital's facilities. For their own services, the doctors directly bill patients and the patients' insurance companies. The hospital must collect for its services directly from the patients and their insurance companies.

Insurers reject outpatient billing claims when the hospital fails to obtain and verify outpatient insurance information. When this happens, the hospital must charge patients to obtain payment for services. Because patients may not be able to pay, bad debts subsequently increase.

The hospital must have patient insurance information to determine the amount that it should collect from these patients and their insurance companies. The hospital has no policy requiring that outpatient insurance coverage be obtained and verified. The hospital should develop and implement such a policy for all outpatients.

Emergency room patients' demographic and insurance data

During the year, the hospital emergency room directly treated and discharged 16,700 patients whose injuries or illnesses did not require inpatient hospital care. Hospital policies do not require emergency room personnel to obtain complete demographic and insurance data from the patient. Only the minimum information necessary to establish a patient record (e.g., name, date of birth, physician's name) is obtained. This is insufficient for billing purposes.

Additional information subsequently must be obtained by the admitting department. Since the emergency room directly discharges the patients, this information is often obtained much later, or in some cases, not at all. The hospital may not be able to collect emergency room fees when it fails to obtain requisite billing data. It should develop and implement procedures to ensure this information is collected before patients are discharged from the emergency room.

Patients are not required to pay in a timely manner

The hospital is fairly lax in its collection practices. Delays in billing patients, lenient credit policies, and inattention to securing payment up front or arranging payment plans all contribute to collection problems.

Patients are not billed immediately

The hospital sends bills to patients only after it has settled with the appropriate insurance carriers, usually several months after patients have been discharged. This is too long to wait to solicit patient payments. Many hospitals estimate the patients' share of the cost of services and invoice patients soon after discharge. In fact, many hospitals participating in medical insurance plans know what insurers will pay and simply bill patients the difference. To wait months before seeking payment from patients is simply poor business practice.

Unrealistic time payment plans

The hospital has arranged unrealistic payment plans for several patients who have large outstanding balances. No interest is charged on past due balances and payment plans provide for monthly payments as low as $100 on outstanding balances in excess of $20,000. At that rate, it would take approximately 17 years for the hospital to be paid in full. The hospital is not in the business of making long-term, zero-interest loans. It should discontinue allowing long-term payment plans and charge interest on past due balances.

No arrangements for payments of large amounts due

The amount a patient owes is determined by the length of stay, services provided, and the patient's insurance plan. The hospital can improve its collection if patients' bills were reviewed with patients and payment plans were developed at the time of discharge. Payment plans include outright settlement of the balance upon discharge, use of credit card payments, installment notes, and referrals to financial institutions. These all are accepted hospital collection practices and should be pursued.

Amounts received from insurers are not verified

Amounts received from insurers were $43 million less than the amounts billed. Of this, an estimated $3 million represent the discounts taken by HMSA and Kaiser. The remainder is a result of insurance plans' agreements with the hospital which place limits on the maximum amount that insurers and patients are required to pay for procedures performed.

For example, an insurance plan's agreement with the hospital may stipulate that the insurance will pay 80 percent of *customary charges* and the patient pays 20 percent of *customary charges*. These *customary charges* often are less than the hospital's standard rates. Because of the agreement with the insurance plan, the hospital receives less than the amounts billed. The difference between the hospital's charges and the amounts the insurers and the patients pay under these agreements are called contractual adjustments and will never be recovered.

The hospital accepts all insurers' payments without verifying that the payment is correct. The hospital simply records the difference between the amount billed and the amount received as a contractual adjustment and takes no further action.

The hospital should not unquestionably accept insurers' payments. A better practice would be to estimate the amounts to be received from insurers and compare them to the payments received. The hospital can then investigate any differences to determine possible underpayments.

Electronic billing requirements may impact Medicare collections

Effective January 1, 1996, the Health Care Financing Administration will require all Medicare providers to electronically bill for Medicare services. Hospitals that do not comply will not be paid. Currently, none of the community hospitals are able to transmit bills electronically. Because the hospital lacks sufficient in-house data processing expertise, it must rely on the Division of Community Hospitals to modify the main computer system to enable it to transmit Medicare bills electronically.

Recommendations

We recommend that the hospital take steps to improve its revenue and collection practices. The hospital should:

a. Ensure that patients are billed for all services and supplies by recording requisition information in patient billing records;

b. Continue to work with the division to improve automated billing procedures and develop electronic billing capabilities;

c. Obtain and verify insurance coverage for all outpatients and patients treated and discharged by the emergency room;

d. Prepare patient bills soon after discharge and make sensible payment arrangements for balances due; and

e. Verify all insurer payments.

Utilization Review Practices Can Minimize Revenue Loss

The hospital cannot afford to provide patient care that insurers deem unnecessary and, therefore, will not pay for. Utilization review is an independent review of patients' records to determine that patient care is consistent with patient needs. It can also be an effective tool in minimizing revenue loss.

Insurance plans quite often pay for hospital services based on standard "levels of treatment" and "length of stay" for specific ailments. For example, the standard length of stay for an appendectomy may be three days. Standard treatment would include surgery, post-operative recovery, nursing services, and medication for pain and inflammation. If a patient receives treatment or medication not included in the standards, or is kept in the hospital longer than the standard length of stay allowed under the insurance plan, the hospital will not be paid for the additional treatment and excess days.

In this case, each extra day a patient stays in a semi-private room can result in several hundreds of dollars of lost revenue. Also, the hospital may not get paid for medication and services. With 180 beds available, the potential for revenue loss and unchecked, unrecoverable costs is significant.

Effective utilization review can identify potential problems with patient treatment or length of stay. It can reduce costs by identifying treatments not normally required by the illness or surgery. It can enhance revenues by specifying additional documentation needed to support treatments not normally required by the illness or surgery. In this case, the additional documentation may result in increased revenues from the insurers. The hospital has one person responsible for all utilization review functions. The focus of the utilization review has been limited to treatments provided for illnesses. Review is not being conducted to determine the potential for cost savings or improved revenues. The hospital should consider strengthening the utilization review department with additional resources.

Recommendation

We recommend the hospital increase the role of the utilization review process as a means to contain costs and improve revenues.

Monthly Financial Reporting Should be Improved

A successful hospital relies on good financial information. Such information enables management to monitor hospital performance. Currently, the hospital prepares monthly financial reports that focus on accounts receivable and cash collections. The hospital should also compare its budget to its actual revenue and expenses and produce other financial information consistent with industry standards.

Budgeting system should be improved

Budgets should be prepared at the level of detail that is most meaningful to those responsible for their attainment. For the hospital, this detail is at the department level (e.g. Pharmacy, Oncology, Surgery, etc.). Department managers should compare actual departmental performance against the budget and analyze significant variances. The hospital's budget is not prepared at this level of detail because the hospital prepares its budget following Department of Budget and Finance (B&F) guidelines. Although B&F guidelines provide a uniform budgeting process which all state agencies must follow in reporting to the Legislature, this format is not useful to hospital departments.

The hospital's financial accounting system can compare departmental revenues and expenses to the budget. However, budgets are not being prepared at the departmental level and the system does not generate such reports. As a result, management cannot monitor departmental activity against budgets and plans.

Useful reports are not prepared

Hospital reports only cover cash and accounts receivable. Other reports should be prepared and used to enable management to analyze departmental operations, to forecast cash receipts and cash

disbursements, and to compare certain performance measures to industry standards. These reports include:

- Monthly financial statements to portray the hospital's financial position and results of operations at the end of each month and year-to-date,
- Cash flow forecasts to compare projected and actual cash receipts and disbursements, and
- Performance reports to compare certain key ratios of the hospital with industry standards. Key ratios include patient capacity, payer mix, liquidity, productivity, and other measures.

Recommendation

We recommend that the hospital prepare budgets and financial reports which include monthly financial statements, comparisons of budgets to departmental activities, cash flow forecasts, and other performance measures.

Long-term Care Patients For Which the Hospital Is Not Licensed Occupy Acute Care Beds

The hospital is licensed for 180 acute care beds but has no license for long-term care beds. However, the hospital provides care to an increasing number of long-term care patients because of the shortage of long-term care beds on Maui. During the past year, a daily average of 40 long-term care patients occupied acute care beds as compared to 32 in 1994. These patients could not be discharged due to the non-availability of space at a private nursing facility or at Kula Hospital (the only two long-term care—skilled nursing and intermediate care—facilities) on Maui. Long-term care patients occupying acute care beds cause several problems.

First, the hospital is not licensed to care for, or designed to accommodate long-term care patients. Second, when the hospital has more patients than licensed beds, acute care patients are kept in the emergency room, operating room, and in hallways. Private rooms are converted to double occupancies and makeshift beds are set up in wards. This could jeopardize the hospital's accreditation and licensing.

This situation also can have a negative financial impact on the hospital. Medicare or Medicaid, which generally pay for services provided to long-term care patients, barely covers the cost of providing that care. Congressional changes to Medicare and Medicaid may further reduce these revenues.

As long as the hospital does not have to turn away higher paying acute care patients, the financial impact is not severe. However, should the hospital have to turn away acute care patients, the financial impact could be significant.

Recommendation

We recommend that the Division of Community Hospitals and the hospital develop plans to meet the needs of long-term care patients and determine the fiscal impact of such plans.

Hospital Security Procedures Need to be Improved

Security procedures in a hospital should provide a safe environment for patients and employees, protect confidential hospital and patient records, and prevent loss. Many people, including employees, physicians, inpatients, outpatients, visitors, and outside contractors enter the hospital every day. When access to the hospital is not controlled, the hospital is not secure.

Security procedures can be improved by monitoring the movement of people entering and leaving the hospital. The hospital has hired security guards from the Department of Public Safety to monitor such movement. However, procedures could be improved and additional safeguards can be instituted.

Employee entrances and exits are not specified

Employees can enter and leave the hospital through the main entrance, rear entrance, side doors and emergency exits. However, only the front entrance is regularly monitored. Consequently, the hospital has difficulty detecting internal pilferage. Recently, an employee was arrested for allegedly stealing hospital equipment. Internal controls should be strengthened to limit employees' ingress and egress to specified doors.

Employees use certain emergency exits as normal entrances and exits. Although emergency exits automatically lock from the outside, employees sometimes wedge objects under the door, which negates the control provided by automatically locking emergency exits.

Employees' identification badges are not always worn

The hospital issues identification badges to employees who should wear them while on duty. This measure should ensure that only authorized personnel enter restricted areas. However, hospital employees do not always wear their identification badges, and the policy is not enforced. As a result, security guards cannot effectively monitor the movement of authorized personnel in restricted areas.

Identification and location of outside contractors is not monitored

The hospital regularly employs outside contractors for repairs and equipment maintenance. Contractors are sometimes allowed access to restricted areas. Security personnel cannot clearly identify these contractors because visitors' badges are not issued. In addition, security guards are not always informed of contractors' schedules or work locations. Internal controls should be strengthened by issuing visitors' badges to contractors and informing security guards of scheduled work and work location.

Recommendations

We recommend that the hospital strengthen its security procedures by:

a. Limiting employees' ingress and egress to specified doors;

b. Limiting use of emergency exits to their designated purpose;

c. Requiring all hospital employees to wear identification badges while on duty; and

d. Requiring outside contractors to wear visitors' badges and notifying the security guards of their schedule.

Chapter 3

Financial Audit

This chapter presents the results of the financial audit of Maui Memorial Hospital and Hana Medical Center (hospital) for the year ended June 30, 1995. It includes the independent auditors' report and reports on the internal control structure and compliance with laws and regulations. It also displays financial statements, together with explanatory notes, and supplemental schedules.

Summary of Findings

In the opinion of Deloitte & Touche LLP (Deloitte & Touche), based on their audit, the financial statements present fairly, in all material respects, the financial position of the hospital at June 30, 1995, and the results of its operations and cash flows for the year then ended in conformity with generally accepted accounting principles, except that the reasonableness of the amounts accrued for self-insured unemployment and workers' compensation claims cannot be determined.

Deloitte & Touche noted no matters involving the internal control structure and its operation that they considered to be material weaknesses as defined in the report on the internal control structure. They also noted, with respect to items tested, that the hospital has complied, in all material respects, with laws and regulations applicable to the hospital.

Independent Auditors' Report

To the Auditor
State of Hawaii

We have audited the following financial statements of Maui Memorial Hospital and Hana Medical Center (Hospital):

Balance sheet, June 30, 1995 (Exhibit A);

Statement of revenues and expenses of unrestricted funds, year ended June 30, 1995 (Exhibit B);

Statement of changes in fund balances, year ended June 30, 1995 (Exhibit C);

Statement of cash flows of unrestricted funds, year ended June 30, 1995 (Exhibit D).

These financial statements are the responsibility of the management of the Hospital. Our responsibility is to express an opinion on these financial statements based on our audit.

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

As discussed in the notes to the financial statements, the financial statements referred to above present only the activities of the Hospital and are not intended to present fairly the financial position and results of operations of the State of Hawaii, in conformity with generally accepted accounting principles.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Hospital at June 30, 1995, and the results of its operations and the cash flows of unrestricted funds for the year then ended in conformity with generally accepted accounting principles.

As discussed in the notes to the financial statements, the Hospital is self-insured for unemployment and workers' compensation claims. At June 30, 1995, the Hospital accrued $358,900 for estimated losses from asserted and unasserted claims, based on the amount of claims paid during the year ended June 30, 1995. However, the reasonableness of such amount cannot be determined, as the Hospital has not accumulated sufficient data, such as the nature of each claim or relevant trend factors, to analyze the claims.

Our audit was made for the purpose of forming an opinion on the financial statements taken as a whole. The following supplemental schedules, which are also the responsibility of the management of the Hospital, are presented for purposes of additional analysis and are not a required part of the basic financial statements:

Combining balance sheet information, June 30, 1995 (Schedule I);

Combining statements of revenues and expenses of unrestricted funds information, year ended June 30, 1995 (Schedule II);

Supplemental schedule of Operating expenses, year ended June 30, 1995 (Schedule III);

Selected hospital statistics, years ended June 30, 1995 and 1994 (unaudited) (Schedule IV);

Supplemental schedule of reconciliation of construction in progress with the State of Hawaii, June 30, 1995 (Schedule V);

Supplemental schedule of reconciliation of cash on deposit with the State of Hawaii, June 30, 1995 (Schedule VI);

Modified cash flow report, year ended June 30, 1995 (unaudited) (Schedule VII);

Aging of gross patient accounts receivable, June 30, 1995 (Schedule VIII).

The supplemental schedules, except for that portion marked "unaudited" on which we express no opinion, have been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, are fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

/s/ Deloitte & Touche LLP

Honolulu, Hawaii
September 8, 1995

Independent Auditors' Report on the Internal Control Structure Based on the Audit of the Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Auditor
State of Hawaii

We have audited the financial statements of Maui Memorial Hospital and Hana Medical Center (Hospital) as of and for the year ended June 30, 1995, and have issued our report thereon dated September 8, 1995. Our report included an explanatory paragraph relating to the reasonableness of the accrual for self-insured unemployment and workers' compensation claims.

We conducted our audit in accordance with generally accepted auditing standards and *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 of material misstatement.

The management of the Hospital is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility,

estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of the Hospital for the year ended June 30, 1995, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operations that we consider to be material weaknesses as defined above.

This report is intended for the information of the Auditor, State of Hawaii and management of the Hospital. However, this report is a matter of public record and its distribution is not limited.

/s/ Deloitte & Touche LLP

Honolulu, Hawaii
September 8, 1995

Independent Auditors' Report on Compliance Based on the Audit of the Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Auditor
State of Hawaii

We have audited the financial statements of Maui Memorial Hospital and Hana Medical Center (Hospital) as of June 30, 1995 and for the year then ended, and have issued our report thereon dated September 8, 1995. Our report included an explanatory paragraph relating to the reasonableness of the accrual for self-insured unemployment and workers' compensation claims.

We conducted our audit in accordance with generally accepted auditing standards and *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 of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to the Hospital is the responsibility of the management of the Hospital. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the Hospital's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards*.

This report is intended for the information of the Auditor, State of Hawaii and management of the Hospital. However, this report is a matter of public record and its distribution is not limited.

/s/ Deloitte & Touche LLP

Honolulu, Hawaii
September 8, 1995

Descriptions of Financial Statements

The following is a brief description of the financial statements audited by Deloitte & Touche. The financial statements are attached at the end of this chapter.

Balance sheet (Exhibit A). This statement presents assets, liabilities, and fund equity of all fund types used by the Hospital on an aggregate basis.

Statement of revenues and expenses of unrestricted funds (Exhibit B). This statement presents revenues and expenses of unrestricted funds used by the Hospital on an aggregate basis.

Statement of changes in fund balances (Exhibit C). This statement presents changes in fund balances for all fund types used by the Hospital on an aggregate basis.

Statement of cash flows of unrestricted funds (Exhibit D). This statement presents cash flows from operating, investing, and financing activities of the Hospital's unrestricted funds on an aggregate basis.

Notes to the Financial Statements

Explanatory notes, which are pertinent to an understanding of the financial statements and financial condition of the funds included in the scope of the audit, are discussed in this section.

Organization and summary of significant accounting policies

Organization. Maui Memorial Hospital and Hana Medical Center (the combined facilities hereafter referred to as "Hospital") are part of the Division of Community Hospitals of the State of Hawaii (State), Department of Health. The State appropriates funds for certain capital improvement projects.

Financial statement presentation. The accompanying financial statements are presented in accordance with the hospital audit guide published by the American Institute of Certified Public Accountants, Audits of Providers of Health Care Services.

The financial statements of Maui Memorial Hospital and Hana Medical Center have been combined. All significant interfund transactions have been eliminated.

Net patient service revenues. Net patient service revenues are reported on an accrual basis in the period in which services are provided, at established rates, less any charitable allowances and contractual adjustments.

Net patient service revenues include amounts to be received from Medicare and Medicaid programs. Receipts from Medicare and Medicaid may be more or less than the established billing rates of the Hospital depending upon the nature of the service provided. The

amounts are determined either by use of cost reimbursement formulas or predetermined rates. Differences are accounted for as contractual adjustments. Retroactively-calculated, third-party contractual adjustments are accrued on an estimated basis in the period the services are rendered and adjusted in future periods as required.

Inventories. Inventories, consisting principally of supplies, are valued at the lower of cost (first-in, first-out method) or market.

Property. Buildings, improvements, and equipment are recorded at cost or estimated fair market value at the date of donation. Donated buildings, equipment, and land are considered additions to the permanent capital of the Hospital and, therefore, are credited directly to the unrestricted fund balance. Equipment under capital leases are recorded at the present value of future payments. Buildings, improvements, and equipment are depreciated by the straight-line method over their estimated useful lives. Normal repairs and maintenance expenses are charged to operations as incurred. Land on which the Hospital is situated is owned by the State and is being provided at no cost to the Hospital.

The Hospital's capital improvement projects are managed by the State's Department of Accounting and General Services. At the completion of the project, the related costs are transferred to the Hospital's property accounts.

Accrued vacation. The cost of employees' vacation pay is recorded at the time vacation benefits are earned.

Grants and donations. Restricted grants and donations are credited directly to the applicable fund balance. Resources restricted for specific operating purposes are transferred to the unrestricted fund and reflected as other operating revenues to the extent expended by the unrestricted fund during the year. Funds which are restricted for property expenditures are transferred from the restricted fund to the unrestricted fund to the extent expended within the year.

Interest. The Hospital reports as expense the interest paid by the State for general obligation bonds whose proceeds were used for hospital construction. A corresponding contribution from the State is reported as nonoperating revenue. The bonds are obligations of the State, to be paid by the State's General Fund, and are not reported as liabilities of the Hospital.

Interest costs incurred on borrowed funds during the period of construction are capitalized as a component of the cost of acquiring the assets.

Contracts with third-party payors

The Hospital is reimbursed for services provided to patients under certain programs administered by governmental agencies. Reimbursement for these services, depending on the type of program and time period, is based on either a prospective payment system or on a cost methodology as defined in the regulations and principles prescribed by the U.S. Department of Health and Human Services.

Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. The Hospital's payment classification of patients under the Medicare prospective payment system is subject to review based on a validation audit by the program's professional review organization.

Inpatient nonacute services, outpatient services, defined capital, and medical education costs related to Medicare beneficiaries are paid based upon a cost reimbursement methodology. The Hospital is reimbursed on the basis of interim rates during the year with final settlement determined after submission of annual cost reports by the Hospital and audits by the Medicare Fiscal Intermediary. Such cost reports have been audited by the Intermediary through June 30, 1992.

Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed based upon a prospective payment system.

The amounts due from Medicare, Medicaid, and HMSA 65C+ at June 30, 1995 consist of reimbursements under cost reports submitted for the following fiscal years:

	Medicare	HMSA Medicaid	65C+	Total
1993	$438,433	$ 71,349		$ 509,782
1994	426,714	75,652	$ 488,664	991,030
1995				
Total	$865,147	$147,001	$ 488,644	$ 1,500,812

The Hospital has also entered into reimbursement agreements with certain commercial insurance carriers and preferred provider organizations. The basis for reimbursement under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined per diem rates.

Property, plant and equipment

Property, plant and equipment consisted of the following at June 30, 1995:

Land	$	212,684
Building and improvements		37,033,244
Equipment		19,776,629
Construction in progress		903,920
		57,926,477
Less accumulated depreciation		(16,151,096)
Property, plant, and equipment - net	$	41,775,381

Capital lease obligations

The Hospital leases equipment under capital leases which are included in property, plant, and equipment. At June 30, 1995, future rental payments were approximately as follows:

1996	$	1,088,000
1997		1,056,000
1998		986,000
1999		552,000
2000		414,000
Total future minimum payments		4,096,000
Less amount representing interest		(691,000)
Total capital lease obligations		3,405,000
Current portion		(814,000)
Noncurrent portion	$	2,591,000

Capital lease payments for the year ended June 30, 1995 approximated $1,178,000 (including interest of approximately $343,000).

At June 30, 1995, the cost of the leased equipment approximated $4,921,000 (accumulated depreciation of approximately $990,000).

Hospital-based physician services arrangements

The Hospital has hospital-based physician services arrangements relating to certain ancillary services, such as pathology, laboratory, radiology, nuclear medicine, ultrasound, CT scan, anesthesiology, radiation oncology, etc. These arrangements are generally related to administrative services, clinical personnel, space rental, and clinical services. Reimbursement arrangements vary by the contractor and range

from fixed amounts per month to 100% reimbursement of the charges. The physicians bill the major insurance carriers and individual patients directly for their professional services.

In compliance with Medicare and Medicaid regulations, the Hospital bills the Medicare and Medicaid programs for the services provided to the Hospital's patients by the contractors. The billings are included in the Hospital's net patient service revenues; and rent charged to the contractors for use of the Hospital's premises are included in other operating revenues. Reimbursements to the contractors are included in operating expenses, primarily in the other professional services category.

Due to State of Hawaii

The amounts due to State of Hawaii primarily represent the accumulated unpaid portions of annual administrative expenses allocated to the Hospital for central service, departmental administration, divisional administration, and information processing service.

In June 1995, Act 211 was passed, whereby the allocation of central service and departmental administration expenses to the Hospital was eliminated, retroactive to July 1, 1993. Accordingly, the financial statements for the year ended June 30, 1995 have been adjusted to reflect the elimination of such expenses for the year ended June 30, 1994, totaling $3,255,913, by decreasing due to State of Hawaii and fiscal and administrative services expenses.

The Hospital paid off its fiscal year 1995 allocation of divisional administration expenses of $685,033 prior to year end. No amounts were allocated for information processing service during the year ended June 30, 1995.

Retirement benefits

Pension plan. All full-time employees of the Hospital participate in the Employees' Retirement System of the State of Hawaii (System), a cost-sharing, multiple-employer public employee retirement system. The Hospital's contributions for fiscal 1995 approximated $2,279,000.

The System is composed of a contributory retirement plan and a noncontributory retirement plan. Eligible full-time employees, in service and a member of the existing contributory plan on June 30, 1984, were given an option to remain in the existing plan or join the noncontributory plan, effective January 1, 1985. All new eligible employees hired after June 30, 1984 automatically become members of the noncontributory plan. Both plans provide death and disability benefits and cost of living increases. Benefits are established by State statute. In the contributory plan, employees may elect normal retirement

at age 55 with 5 years of credited service or elect early retirement at any age with 25 years of credited service. Such employees are entitled to retirement benefits, payable monthly for life, of 2% of their average final salary, as defined, for each year of credited service. Benefits fully vest on reaching five years of service; retirement benefits are actuarially reduced for early retirement. Covered contributory plan employees are required by State statute to contribute 7.8% of their salary to the plan; the Hospital is required by State statute to contribute the remaining amounts necessary to pay contributory plan benefits when due. In the noncontributory plan, employees may elect normal retirement at age 62 with 10 years of credited service or at age 55 with 30 years of credited service, or elect early retirement at age 55 with 20 years of credited service. Such employees are entitled to retirement benefits, payable monthly for life, of 1.25% of their average final salary, as defined, for each year of credited service. Benefits fully vest on reaching ten years of service; retirement benefits are actuarially reduced for early retirement. The Hospital is required by State statute to contribute all amounts necessary to pay noncontributory plan benefits when due.

The "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement systems and employers.

The System does not make separate measurements of assets and pension benefit obligations for individual employers. The pension benefit obligation at June 30, 1994 (the latest date available) for the System as a whole, determined through an actuarial valuation performed as of that date, was $7 billion. The System's net assets available for benefits on that date (valued at market) were $5.4 billion, leaving an unfunded pension benefit obligation of $1.6 billion.

For historical trend information, showing the System's progress in accumulating sufficient assets to pay benefits when due, see the System's June 30, 1994 annual financial report.

Post-retirement health care and life insurance benefits. In addition to providing pension benefits, the State provides certain health care and life insurance benefits for retired State employees. Contributions are based upon negotiated collective bargaining agreements, and are funded by the State as accrued. The Hospital's share of the expense for post-retirement health care and life insurance benefits for the year ended June 30, 1995 was approximately $996,000.

Employee housing. The State leases a building and furnishings to house certain employees. The original terms of the lease provide that the Hospital pay monthly lease rent of $15,700, adjusted annually by the Consumer Price Index (CPI) as published by the U.S. Department of Labor Bureau of Standards as adjusted for Hawaii (approximately $22,000 as of June 30, 1995). The initial term of the lease is for 120 months with the State reserving the option to extend the term for an additional five years. The lessor has also granted the State an option to purchase the building and furnishings throughout the lease period at prices specified in the lease agreement. The Hospital in turn leases units in the building to employees on a month-to-month basis for $500 per month. Lease rental income for the year ended June 30, 1995 approximated $71,000. Lease expense for the year ended June 30, 1995 approximated $268,000.

Future minimum rental payments (including fiscal 1995 CPI adjustment) for fiscal years ending after June 30, 1995 are as follows:

1996	$ 268,000
1997	268,000
1998	268,000
1999	268,000
2000	223,000
Total	$ 1,295,000

Contingencies

Concentration of credit risks. The Hospital grants credit without collateral to its patients, primarily local residents who are insured under third-party payor agreements. At June 30, 1995, the mix of the "active" (excludes accounts with the State's Attorney General's office and collection agencies) patient service receivables was as follows:

Medicare	24%
Kaiser Permanente	18
HMSA	16
Medicaid	8
QUEST	8
Other third-party payors	13
Other	13

Professional liability. The Hospital is insured for professional liability claims up to $10 million per claim and no limit in the aggregate on a claims-made basis. The State's Attorney General advises that any judgments rendered against the Hospital in excess of the Hospital's professional liability coverage as a result of pending or threatened litigation will require special legislative appropriations and will not be charged against the Hospital's appropriations.

Self-insurance for unemployment and workers' compensation claims. The Hospital is self-insured for unemployment and workers' compensation claims which are expensed when incurred. At June 30, 1995, the Hospital accrued $358,900 for estimated losses from asserted and unasserted claims, based on the amount of claims paid during the year ended June 30, 1995. However, the reasonableness of such amount cannot be determined, as the Hospital has not accumulated sufficient data, such as the nature of each claim or relevant trend factors, to analyze the claims.

Accumulated sick pay. Sick leave accumulates at the rate of one and three-quarters working days for each month of service without limit and can be taken only in the event of illness. Sick leave is not convertible to pay upon termination of employment. However, a public employee who retires or leaves government service in good standing with sixty days or more of unused sick leave is entitled to additional service credit in the Employees' Retirement System. Accumulated sick leave at June 30, 1995 was approximately $5.5 million based on current salary rates.

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

Exhibit A

BALANCE SHEET
JUNE 30, 1995

ASSETS

CURRENT ASSETS:	
Cash:	
On deposit with the State of Hawaii	$ 1,982,836
On hand	6,000
Total cash	1,988,836
Receivables:	
Patient accounts receivable - less allowances of $28,844,435	18,440,015
Due from third-party payors	1,500,812
Other	223,943
Total receivables	20,164,770
Inventories	786,313
Total current assets	22,939,919
PROPERTY, PLANT AND EQUIPMENT - Net	41,775,381
RESTRICTED FUNDS - Gift trust fund	104,737
TOTAL	$64,820,037

LIABILITIES AND FUND BALANCES

CURRENT LIABILITIES:	
Capital lease obligations - current portion	$ 814,104
Accounts payable	2,998,525
Accrued salaries and wages	549,340
Accrued vacation	2,776,897
Other liabilities	824,315
Total current liabilities	7,963,181
DUE TO STATE OF HAWAII	15,797,513
CAPITAL LEASE OBLIGATIONS - Less current portion	2,590,640
Total liabilities	26,351,334
FUND BALANCES:	
Unrestricted	38,363,966
Restricted	104,737
Total fund balances	38,468,703
TOTAL	$64,820,037

See notes to financial statements.

Exhibit B

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

STATEMENT OF REVENUES AND EXPENSES OF UNRESTRICTED FUNDS
YEAR ENDED JUNE 30, 1995

NET PATIENT SERVICE REVENUES	$61,296,869
OTHER OPERATING REVENUES:	
Rental income	509,516
Cafeteria and other	240,842
Total operating revenues	62,047,227
OPERATING EXPENSES:	
Nursing services	23,089,132
Other professional services	16,228,469
Fiscal and administrative services	9,598,255
General services	5,393,418
Provision for uncollectible accounts	3,964,126
Depreciation	2,068,533
Total operating expenses	60,341,933
INCOME FROM OPERATIONS	1,705,294
NONOPERATING REVENUES (EXPENSES):	
Contributions from State of Hawaii:	
Net transfers	2,966,669
For payment of interest	1,985,507
Interest expense - net of $289,618 capitalized	(1,695,889)
Nonoperating revenues - net	3,256,287
EXCESS OF REVENUES OVER EXPENSES	$ 4,961,581

See notes to financial statements.

Exhibit C

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

STATEMENT OF CHANGES IN FUND BALANCES
YEAR ENDED JUNE 30, 1995

UNRESTRICTED FUNDS:	
Balance at beginning of year	$33,402,385
Excess of revenues over expenses	4,961,581
Balance at end of year	$38,363,966
RESTRICTED FUNDS:	
Balance at beginning of year	$ 51,995
Restricted contributions	52,742
Balance at end of year	$ 104,737

See notes to financial statements.

Exhibit D

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

STATEMENT OF CASH FLOWS OF UNRESTRICTED FUNDS
YEAR ENDED JUNE 30, 1995

OPERATING ACTIVITIES:	
Income from operations	$ 1,705,294
Adjustments to reconcile income from operations to net cash provided by operating activities:	
Loss on disposals of property and equipment	103,855
Depreciation	2,068,533
Operating transfers from the State of Hawaii	1,518,897
Changes in operating assets and liabilities:	
Receivables	(881,213)
Inventories	(160,427)
Accounts payable	624,720
Due to State of Hawaii	(3,255,913)
Other assets and liabilities	461,878
Net cash provided by operating activities	2,185,624
CAPITAL AND CAPITAL-RELATED FINANCING ACTIVITIES:	
Capital expenditures	(1,251,506)
Principal payments on capital lease obligations	(835,706)
Net cash used in capital and capital-related financing activities	(2,087,212)
NET INCREASE IN CASH	98,412
TOTAL CASH, BEGINNING OF YEAR	1,890,424
TOTAL CASH, END OF YEAR	$ 1,988,836
SUPPLEMENTAL CASH FLOW INFORMATION:	
Interest paid on capital lease obligations	$ 342,772
Non-cash financing and investing activities:	
• Construction in progress contributed by the State of Hawaii	1,447,772
• Interest capitalized on construction projects	289,618

See notes to financial statements.

Schedule I

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

COMBINING BALANCE SHEET INFORMATION
JUNE 30, 1995

ASSETS	Maui Memorial Hospital	Hana Medical Center	Elimi-nations	Combined Total
CURRENT ASSETS:				
Cash:				
On deposit with the State of Hawaii	$ 1,929,608	$ 53,228		$ 1,982,836
On hand	5,925	75		6,000
Total cash	1,935,533	53,303		1,988,836
Receivables:				
Patient accounts receivable - net	18,114,788	325,227		18,440,015
Due from third-party payors	1,500,812			1,500,812
Other receivables	544,847		$ (320,904)	223,943
Total receivables	20,160,447	325,227	(320,904)	20,164,770
Inventories	786,313			786,313
Total current assets	22,882,293	378,530	(320,904)	22,939,919
PROPERTY, PLANT AND EQUIPMENT:				
Land	212,684			212,684
Buildings and improvements	36,463,701	569,543		37,033,244
Equipment	19,237,311	539,318		19,776,629
Construction in progress	860,943	42,977		903,920
	56,774,639	1,151,838		57,926,477
Less accumulated depreciation	(15,578,108)	(572,988)		(16,151,096)
Property, plant and equipment - net	41,196,531	578,850		41,775,381
RESTRICTED FUNDS -				
Gift trust fund	99,200	5,537		104,737
TOTAL	$ 64,178,024	$ 962,917	$ (320,904)	$ 64,820,037

Schedule I

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

COMBINING BALANCE SHEET INFORMATION (Continued)
JUNE 30, 1995

LIABILITIES AND FUND BALANCES	Maui Memorial Hospital	Hana Medical Center	Elimi-nations	Combined Total
CURRENT LIABILITIES:				
Capital lease obligations - current portion	$ 814,104			$ 814,104
Accounts payable	2,764,254	$ 234,271		2,998,525
Accrued salaries and wages	518,047	31,293		549,340
Accrued vacation	2,725,616	51,281		2,776,897
Other liabilities	374,109	771,110	$ (320,904)	824,315
Total current liabilities	7,196,130	1,087,955	(320,904)	7,963,181
DUE TO STATE OF HAWAII	15,564,879	232,634		15,797,513
CAPITAL LEASE OBLIGATIONS - Less current portion	2,590,640			2,590,640
Total liabilities	25,351,649	1,320,589	(320,904)	26,351,334
FUND BALANCES:				
Unrestricted	38,727,175	(363,209)		38,363,966
Restricted	99,200	5,537		104,737
Total fund balances	38,826,375	(357,672)		38,468,703
TOTAL	$64,178,024	$ 962,917	$ (320,904)	$64,820,037

Schedule II

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

COMBINING STATEMENTS OF REVENUES AND EXPENSES OF UNRESTRICTED FUNDS INFORMATION YEAR ENDED JUNE 30, 1995

	Maui Memorial Hospital	Hana Medical Center	Combined Total *
NET PATIENT SERVICE REVENUES	$60,943,264	$ 353,605	$61,296,869
OTHER OPERATING REVENUES:			
Rental income	509,516		509,516
Cafeteria and other	240,618	224	240,842
Total operating revenues	61,693,398	353,829	62,047,227
OPERATING EXPENSES:			
Nursing services	22,491,346	597,786	23,089,132
Other professional services	15,924,790	303,679	16,228,469
Fiscal and administrative services	9,325,181	273,074	9,598,255
General services	5,292,957	100,461	5,393,418
Provisions for doubtful accounts	3,937,269	26,857	3,964,126
Depreciation	2,033,303	35,230	2,068,533
Total operating expenses	59,004,846	1,337,087	60,341,933
INCOME FROM OPERATIONS	2,688,552	(983,258)	1,705,294
NONOPERATING REVENUES (EXPENSES):			
Contributions from State of Hawaii:			
Net transfers	2,192,197	774,472	2,966,669
For payment of interest	1,962,188	23,319	1,985,507
Interest expense	(1,695,758)	(131)	(1,695,889)
Nonoperating revenues - net	2,458,627	797,660	3,256,287
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	$ 5,147,179	$ (185,598)	$ 4,961,581

* No eliminations required.

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

SCHEDULE III

SUPPLEMENTAL SCHEDULE OF OPERATING EXPENSES
YEAR ENDED JUNE 30, 1995

	Maui Memorial Hospital				Hana Medical Center			
	Salaries and Wages	Supplies and Other Expenses	Total	Percent of Total Expenses*	Salaries and Wages	Supplies and Other Expenses	Total	Percent of Total Expenses*
NURSING SERVICES:								
Administration	$12,792,918	$ 2,009,415	$14,802,333	24 %	$ 48,489	$ 36	$ 48,525	4 %
Operating room	1,610,095	1,964,486	3,574,581	6				
Emergency	1,588,553	353,560	1,942,113	3	274,738	102,213	376,951	28
Central service and supply	340,868	612,206	953,074	2				
Inhalation therapy	406,007	522,709	928,716	1				
Delivery room	8,440	182,866	191,306					
Nursing education	94,016	5,207	99,223			(350)	(350)	
Ambulance service						172,660	172,660	13
	16,840,897	5,650,449	22,491,346	36	323,227	274,559	597,786	45
OTHER PROFESSIONAL SERVICES:								
Laboratory	55,705	5,886,967	5,942,672	10	16,203	16,712	32,915	2
Pharmacy	600,452	1,741,440	2,341,892	4		197,627	197,627	14
Radiology	189,911	4,029,247	4,219,158	7	57,744	15,393	73,137	5
Medical records and library	474,931	170,464	645,395	1				
Anesthesiology	130,523	243,303	373,826	1				
Nuclear medicine		567,160	567,160	1				
Oncology	221,304	250,792	472,096	1				
Bloodbank		296,544	296,544	1				
Physical therapy	246,651	93,799	340,450	1				
Echocardiology		286,215	286,215					
Social services	157,608	551	158,159					
Ultrasound		177,968	177,968					
Occupational therapy	91,049	12,206	103,255					
	2,168,134	13,756,656	15,924,790	27	73,947	229,732	303,679	21

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

SCHEDULE III

SUPPLEMENTAL SCHEDULE OF OPERATING EXPENSES (Continued)
YEAR ENDED JUNE 30, 1995

	Maui Memorial Hospital				Hana Medical Center			
	Salaries and Wages	Supplies and Other Expenses	Total	Percent of Total Expenses*	Salaries and Wages	Supplies and Other Expenses	Total	Percent of Total Expenses*
FISCAL AND ADMINISTRATIVE:								
Employee benefits		$ 7,295,476	$ 7,295,476	12 %		$ 121,491	$ 121,491	9 %
Administrative	$ 1,273,995	936,082	2,210,077	3	$ 61,618	15,145	76,763	6
Fiscal service	1,395,566	905,460	2,301,026	4	53,933	12,553	66,486	5
Insurance		660,779	660,779	1		28,887	28,887	2
Medical care evaluation	83,819	9,364	93,183					
Reversal of 1994 central service and departmental administrative expenses		(3,235,360)	(3,235,360)			(20,553)	(20,553)	
	2,753,380	6,571,801	9,325,181	20	115,551	157,523	273,074	22
GENERAL SERVICES:								
Plant operation and maintenance	761,690	1,968,853	2,730,543	4	62,977	31,572	94,549	7
Dietary	793,265	496,639	1,289,904	2		1,605	1,605	
Housekeeping	659,541	172,626	832,167	1		1,267	1,267	
Laundry and linen	319,536	107,030	426,566	1		1,220	1,220	
Motor service		13,777	13,777			1,820	1,820	
	2,534,032	2,758,925	5,292,957	8	62,977	37,484	100,461	7
PROVISION FOR DOUBTFUL ACCOUNTS		3,937,269	3,937,269	6		26,857	26,857	2
DEPRECIATION		2,033,303	2,033,303	3		35,230	35,230	3
TOTAL	$24,296,443	$34,708,403	$59,004,846	100 %	$575,702	$761,385	$1,337,087	100 %

*Excludes reversal of 1994 expenses.

Schedule IV

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

SELECTED HOSPITAL STATISTICS
YEARS ENDED JUNE 30, 1995 AND 1994 (Unaudited)

	1995	1994
NUMBER OF LICENSED BEDS:		
Acute	152	135
Psychiatric	10	10
Other - Nursery	18	18
Total licensed beds	180	163
OCCUPANCY:		
Patient days and percent of occupancy:		
Acute:		
Days	51,394	48,278
Percent	83%	98%
Acute psychiatric care:		
Days	2,316	3,278
Percent	63%	90%
Newborn:		
Days	2,966	3,146
Percent	45%	48%
Total:		
Days	56,676	54,702
Percent	78%	92%
SUNDRY PATIENT DATA:		
Acute admissions	8,179	8,474
Acute discharges	8,168	8,464
Newborn deliveries	1,591	1,623
Meals served - patients	178,009	185,343
Average daily census	147	141
Average length of stay (days)	6.3	6.1
Pounds laundered	1,168,911	1,109,320
Average net patient services revenues per patient day	$1,082	$1,057
Average total operating expenses per patient day	$1,065	$1,177

Schedule IV

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

SELECTED HOSPITAL STATISTICS (Continued)
YEARS ENDED JUNE 30, 1995 AND 1994 (Unaudited)

	1995	1994
DEPARTMENTAL DATA:		
Surgical procedures:		
Inpatient	*	*
Outpatient	*	*
Radiological examinations	46,799	48,605
Laboratory tests	221,600	133,437
Emergency room registrations	20,627	19,383
Outpatient visits (nonemergency)	*	*
Home health services	N/A	N/A
Number of pharmacy items issued	612,276	575,337
Physical therapy treatments	11,550	15,883
Occupational therapy treatments	11,360	9,879
Operations (number of minutes)	887,762	830,514
Deliveries	1,591	1,620
EKG examinations	9,496	12,958
Anesthetics given	4,432	4,192

* Hospital statistic is not available.

Schedule V

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

SUPPLEMENTAL SCHEDULE OF RECONCILIATION OF CONSTRUCTION IN PROGRESS WITH THE STATE OF HAWAII
JUNE 30, 1995

Reconciliation of the Hospital's construction in progress with the State Comptroller's central accounting records as of June 30, 1995 is as follows:

	Maui Memorial Hospital	Hana Medical Center	Total
CAPITAL PROJECTS FUNDED BY THE STATE:			
Second Increment Renovation:			
Balance, June 30, 1994:			
Capital expenditures	$ 28,353		$ 28,353
Capitalized interest	893		893
Fiscal 1995 additions:			
Capital expenditures	747,095		747,095
Capitalized interest	25,361		25,361
Balance, June 30, 1995	801,702		801,702
Renovation and Expansion:			
Balance, June 30, 1994:			
Capital expenditures		$21,653	21,653
Capitalized interest		1,230	1,230
Fiscal 1995 capital expenditures:			
Capital expenditures during fiscal 1995		17,720	17,720
Capitalized interest		2,374	2,374
Balance, June 30, 1995		42,977	42,977
Other Projects:			
Balance, June 30, 1994:			
Capital expenditures	1,936		1,936
Capitalized interest	61		61
Fiscal 1995 capital expenditures:			
Capital expenditures during fiscal 1995	55,374		55,374
Interest capitalized during fiscal 1995	1,870		1,870
Balance, June 30, 1995	59,241		59,241
BALANCE PER HOSPITAL	860,943	42,977	903,920
LESS CAPITALIZED INTEREST	(55,645)	(3,604)	(59,249)
BALANCE PER STATE OF HAWAII	$805,298	$39,373	$844,671

Schedule VI

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

SUPPLEMENTAL SCHEDULE OF RECONCILIATION OF CASH ON DEPOSIT WITH THE STATE OF HAWAII
JUNE 30, 1995

	Appropriation Symbol	Maui Memorial Hospital	Hana Medical Center	Total
SPECIAL FUNDS:				
	S-84-356-H		$ 134	134
	S-86-355-H	$ 1,039		$ 1,039
	S-87-355-H	12,821		12,821
	S-88-355-H	987		987
	S-89-355-H	83		83
	S-91-355-H	4,021		4,021
	S-93-355-H	357,258		357,258
	S-94-355-H	33,351		33,351
	S-94-356-H		1	1
	S-95-355-H	1,504,347		1,504,347
	S-95-356-H		53,093	53,093
	S-95-385-H	8,409		8,409
Total Special Funds		1,922,316	53,228	1,975,544
TRUST FUNDS:				
Gift fund	T-95-910-H	99,200	5,537	104,737
Deposits	T-95-920-H	7,292		7,292
TOTAL PER STATE OF HAWAII		$2,028,808	$58,765	$2,087,573
REFLECTED IN CURRENT ASSETS		$1,929,608	$53,228	$1,982,836
REFLECTED AS RESTRICTED FUNDS		99,200	5,537	104,737
TOTAL PER HOSPITAL		$2,028,808	$58,765	$2,087,573

Schedule VII

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

MODIFIED CASH FLOW REPORT
YEAR ENDED JUNE 30, 1995 (Unaudited)

	Maui Memorial Hospital	Hana Medical Center	Total
RECEIPTS:			
HMSA	$17,928,146	$ 56,074	$17,984,220
Medicare	9,116,917	8,942	9,125,859
Kaiser Permanente	7,473,871	1,142	7,475,013
Patient payments	3,940,135	144,520	4,084,655
Medicaid	3,980,598	26,578	4,007,176
QUEST	2,069,500	20,584	2,090,084
Other third-party payors	11,635,321	31,292	11,666,613
Other	944,095	221,957	1,166,052
Total receipts	57,088,583	511,089	57,599,672
EXPENDITURES AND ENCUMBRANCES:			
Allocations	60,881,240	1,215,602	62,096,842
Less excess of allocations over expenditures and encumbrances	(2,457,514)	(570)	(2,458,084)
Total expenditures and encumbrances	58,423,726	1,215,032	59,638,758
EXCESS OF EXPENDITURES AND ENCUMBRANCES OVER RECEIPTS	(1,335,143)	(703,943)	(2,039,086)
TRANSFERS FROM STATE OF HAWAII	91,188	525,688	616,876
UNENCUMBERED CASH, JULY 1, 1994	934,679	139,905	1,074,584
PRIOR YEAR REVERSIONS	29,786		29,786
UNENCUMBERED CASH DEFICIENCY, JUNE 30, 1995	$ (279,490)	$ (38,350)	$ (317,840)

Schedule VIII

MAUI MEMORIAL HOSPITAL AND HANA MEDICAL CENTER

AGING OF GROSS PATIENT ACCOUNTS RECEIVABLE
JUNE 30, 1995

UNBILLED	$ 5,871,940
CURRENT	9,347,706
31 - 60 DAYS	5,522,492
61 - 90 DAYS	2,774,518
91 - 120 DAYS	2,801,030
121 - 150 DAYS	1,415,981
Over 151 DAYS	19,550,783
TOTAL	$47,284,450

Notes

Chapter 2

1. Letter to Mr. Bertrand Kobayashi, Deputy Director, Community Hospitals from Mr. Dean Y. Hayashi, Manager, Government Reimbursement, Kaiser Foundation Health Plan, Inc., November 2, 1995

2. Hawaii, The Auditor, *Audit of the Information System of the Division of Community Hospitals*, Report No. 95-21, Honolulu, October 1995, p. 11

Responses of the Affected Agencies

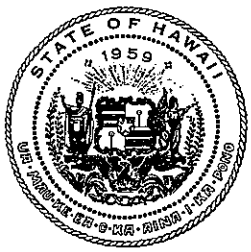
Comments on Agency Responses

We transmitted a draft of this report to the Department of Health on January 9, 1996. A draft of the report was also transmitted to the Maui Memorial Hospital. A copy of the transmittal to the Department of Health is included as Attachment 1. A similar letter was sent to the Maui Memorial Hospital. The Department of Health, in consultation with the Maui Memorial Hospital, responded for both, and that response is included as Attachment 2.

The department generally concurs with our findings and says that it will seriously consider our recommendations and use them to improve the management and operation of Maui Memorial Hospital/Hana Medical Center. The department believes that its proposal to the 1996 Legislature to convert the Division of Community Hospitals into an autonomous and independent public corporation would enhance its ability to solve problems specific to the hospital. Pending any legislative approval of a conversion proposal, the department plans to proceed in making improvements. We are pleased that the department is not relying solely on a decision on its autonomy proposal before taking corrective actions.

ATTACHMENT 1

STATE OF HAWAII
OFFICE OF THE AUDITOR
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917



MARION M. HIGA
State Auditor

(808) 587-0800
FAX: (808) 587-0830

January 9, 1996

COPY

The Honorable Lawrence H. Miike
Director of Health
Department of Health
Kinau Hale
1250 Punchbowl Street
Honolulu, Hawaii 96813

Dear Dr. Miike:

Enclosed for your information is a copy number 9 of our draft report, *Financial Audit of the Maui Memorial Hospital and the Hana Medical Center*. We ask that you telephone us by Friday, January 12, 1996, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Friday, January 19, 1996.

The Maui Memorial Hospital, Governor, and presiding officers of the two houses of the Legislature have also been provided copies of this draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

Marion M. Higa
State Auditor

Enclosure

BENJAMIN J. CAYETANO
GOVERNOR OF HAWAII

LAWRENCE MIIKE
DIRECTOR OF HEALTH

STATE OF HAWAII
DEPARTMENT OF HEALTH
P.O. BOX 3378
HONOLULU, HAWAII 96801

In reply, please refer to:
File:

January 22, 1996

RECEIVED
JAN 22 3 24 PM '96
OFC. OF THE AUDITOR
STATE OF HAWAII

Ms. Marion Higa, State Auditor
Office of the Legislative Auditor
465 South King Street, Room 500
Honolulu, Hawai'i 96813

Dear Ms. Higa:

We have received your draft of "Financial Audit of the Maui Memorial Hospital and Hana Medical Center" and we would like to thank you and your staff for identifying potential areas for improving fiscal and general operations. These areas are being reviewed by hospital management and actions will be taken to address shortcomings to the extent practical to improve operations. Your report on these concerns will be used as a guide for improvement at Maui Memorial Hospital/Hana Medical Center. We appreciate the opportunity to comment on your findings.

Before we comment on your report, I would like to say that the hospital administrators and managers that participated in this audit are most hopeful that legislation being proposed in this 1996 legislative session will provide the legal framework to enable State-operated community hospitals to operate more efficiently and without the impediments of a larger bureaucratic structure. We feel that our legislative proposal to the 1996 Legislature to convert the Division of Community Hospitals from a division within the Department of Health to a public benefit corporation for community hospitals will enable greater flexibility in operation, greater local autonomy, and greater abilities to deal directly and expeditiously to solve problems specific to an individual hospital. The findings in your audit would support ways to better address these shortcomings.

The following represent abbreviated comments to the five (5) summary findings that you have outlined in Chapter 2 of your audit:

Recommendation 1 questions the soundness and authorization for cash discounts given to two insurers.

We agree that both the hospital and the central division office must review the appropriateness as well as the rationale behind the giving of discounts to these insurers. However, we question the calculation of the discounts costing the hospital in lost revenue ($3 to $5 million) and hospital staff will be discussing this with you in separate correspondence.

Recommendation 2 identifies the need to improve revenue and collection practices. We generally agree with your findings; however, we again question the magnitude of the figure that you deem to be "uncollectible as of 6/30/95 ($29 million). Again, we will be discussing this with you in separate correspondence. The major shortcoming we have in this area appears to be the identification of estimated charges and related patient's share of the bill at discharge or after services have been provided. We feel that the greatest opportunity to improve in this area is to improve our electronic automation capabilities so this information is readily available at patient discharge. The issue concerning the acceptability of Medicare "paper" claims has been discussed with the fiscal intermediary and we are advised that paper or "hard copy" claims will continue to be accepted for an indeterminable period of time. The hospital will continue to work on the implementation of electronic claims filing (ECF) of Medicare claims. We expect to have ECF function on or around the close of the first quarter of 1996.

Unbilled charges are, indeed, problematic for the majority of hospitals and Maui Memorial Hospital needs to take steps to decrease unbilled charges. We agree that the hospital's failure to bill patients/insurers for $185,600 in supplies charges must be improved. However, the hospital billed over $16.4 million in supplies charges and the magnitude of the $185,600 in missing supplies charges represents about 1 percent of the total. It is also important to note that the $185,600 is not all collectible since over 50 percent of hospital patients are in fixed payment categories, such as Medicare, Medicaid, and related insurance plans. We are implementing a hospital-wide supply cart exchange program which will provide hospital management greater control over such missing charges.

The use of manual requisition/charge slips is not uncommon, but we do agree that a more efficient system

needs to be considered to assure the capture of charges for ancillary services. However, at the present time, we have no evidence that manual requisition and charge slips for ancillary services are not working. We see this as an area for further study.

We believe your discussion identifying inefficiencies in the information processing of billing data refers primarily with a DRG grouper used by the hospital's medical records department. We are in agreement that it is generally inefficient that a separate personal computer with a separate DRG grouper program be used when the hospital's mainframe computer should be able to possess the same program. However, we do not believe that having the grouper program on a separate computer delays the hospital's billing and collection efforts.

Recommendation 3 suggests internal financial reporting is inadequate. We feel that the term "inadequate" exaggerates the issue. There are some financial reports that are lacking, namely, departmental budgets; however, the hospital is developing a hospital department budget for the remainder of FY 1996 and this should be fully implemented for FY 1997. The hospital prepares the following reports which are reviewed by management:

1) Statement of Profit and Loss
2) Balance Sheet
3) Summary Trial Balance
4) Detail Trial Balance
5) Schedule of Revenues
6) Schedule of Other Revenue
7) Schedule of Deductions from Revenue
8) Schedule of Expenses
9) Detail Schedule of Expenses on a Cash Basis
10) Detail Schedules of Revenue, Payroll, Other Expenses as Compared to Allotment

We think it is accurate to say the hospital lacks some important financial reports, but to say that reporting is inadequate, we believe, overstates the problem. We agree with the recommendation to use regional and national performance/productivity ratios to measure our own performance.

Recommendation 4 identifies the magnitude and seriousness of long-term care patients occupying hospital acute beds. This is a very serious problem statewide and not just for Maui Memorial Hospital. We concur with the Auditor's recommendation.

Recommendation 5 suggests that hospital security procedures should be improved. We are in general agreement that hospital security is an important area in the overall operations of the hospital and that we must review this recommendation carefully. The report identifies potential areas of concern and the hospital will review the practicality and logistics of implementing these recommendations. Fortunately, the hospital does not appear to have had major problems of asset loss and safety issues relating to staff and patients. We appreciate the Auditor's comments and suggestions in this area and we will consider them seriously.

In closing, this report is valid in a number of critical areas. We appreciate your office bringing these to light and we will seriously consider your final recommendations and use these to better improve the management and operation of Maui Memorial Hospital/Hana Medical Center.

Thank you for allowing us to comment on this audit. Please extend our appreciation to your staff for their efforts and work to improve our processes and outcomes for Maui Memorial Hospital.

Sincerely,

BERTRAND KOBAYASHI, Ph.D.
Deputy Director for Community Hospitals

c: Lawrence Miike, Director