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# **A Review and Identification of Fiscally Related Powers Conferred Upon or Assumed by the Executive Branch**

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

Report No. 01-04  
February 2001



**THE AUDITOR**  
STATE OF HAWAII

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## 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 are 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.



### THE AUDITOR STATE OF HAWAII

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# OVERVIEW

## *A Review and Identification of Fiscally Related Powers Conferred Upon or Assumed by the Executive Branch*

Report No. 01-04, February 2001

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### Summary

Senate Concurrent Resolution No. 47 of the Regular Session of 2000 requested that the State Auditor review and identify fiscally related powers conferred upon or assumed by the executive branch since 1987 that may be reclaimed or reasserted by the Legislature. The resolution suggests that the Legislature's dominant role in fiscal affairs under the State Constitution has, over time, shifted inappropriately to the executive branch.

During our review, we heard a variety of conflicting opinions regarding the degree to which there exists a legislative-executive imbalance. We found few specific instances in which the executive branch's fiscal powers had increased since 1987. Indeed, since 1987, the Legislature appears to have reduced the executive branch's fiscal powers in certain respects.

We concluded that Hawaii's Legislature generally resembles other states in its exercise of fiscal powers, but does not play as formidable a role in the budget development and enactment processes as in some other states. As has been done elsewhere, Hawaii's Legislature could act to curtail executive branch flexibility and exercise considerably more control over the use of state resources. The Legislature could take steps to assert its will and improve its ability to review and monitor the State's economic condition and the actions of the executive branch.

Should the Legislature desire to do so, it could pursue options to enhance its fiscal powers. The Legislature could:

- Strengthen its technical capabilities;
- Exercise more of its existing powers over appropriations;
- Take on additional budgetary powers; and
- Tighten its control over executive branch spending.

The Legislature's technical capabilities are reflected in its ability to access revenue and expenditure data and in the functions of its committees and support agencies. The Legislature could take a series of steps to expand its technical resources to review and assess a variety of fiscal data. These include:

- Establishing on-line access by the Legislature to fiscal data of every state agency;
- Starting up the Joint Legislative Budget Committee and funding the Office of the Legislative Analyst;
- Expanding full-time staffing for the Legislature's "money committees"; and
- Determining whether responsibility for financial audits of executive branch agencies should be transferred to a legislative service agency.



Hawaii's Legislature could exert some existing powers to contest the executive branch. These powers include but may not be limited to overriding the governor's vetoes and deciding on the best use of "budget provisos."

The Legislature could assume additional budgetary powers exercised by some other state legislatures. The Legislature could:

- Prepare a budget bill separate from the executive branch's bill;
- Require the use of fiscal notes to assess the impact of proposed legislation; and
- Gain control over the volume and quality of budgetary information supplied to the Legislature.

Most of the options open to the Legislature revolve around mechanisms to tighten its control over executive branch spending:

- Modify Chapter 37, HRS, to clarify the parameters under which the governor and director of finance can reduce allotments;
- Require legislative approval for budget cuts;
- Modify Chapter 37, HRS, to remove all exemptions to the allotment requirements;
- Repeal special and revolving funds that fail to demonstrate the necessary linkages;
- Revisit the budget requirements for the Hawaii Health Systems Corporation;
- Review the impact of the autonomy given to the Department of Education and the University of Hawaii;
- Authorize only those capital improvement projects that the administration has demonstrated are within state capacities to build within a specified timeframe; and
- Capitalize on opportunities offered by new accounting standards.

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## Response

The Department of Budget and Finance responded that the governor's current level of fiscal powers is reasonable when considered within the context of his substantial statewide obligations and responsibilities as mandated by the State Constitution and statutes. The department asserts that removing all or part of such budget and fiscal discretionary authority would significantly impact the governor's ability to carry out his responsibilities. Finally, the department agrees that the Legislature should expand its own technical capabilities to review and assess state fiscal data, as was intended by the creation of the Joint Legislative Budget Committee and the Office of the Legislative Analyst in Act 347, Session Laws of Hawaii 1990.

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STATE OF HAWAII

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## Foreword

Senate Concurrent Resolution No. 47 of the Regular Session of 2000 requested that the State Auditor review and identify fiscally related powers conferred upon or assumed by the executive branch since 1987 that may be reclaimed or reasserted by the Legislature. This report responds to the Legislature's request.

We wish to express our appreciation for the cooperation and assistance extended to us by various legislative staff, by officials and staff of the Department of Budget and Finance, and by others whom we contacted during the course of this review.

Marion M. Higa  
State Auditor

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# Chapter 1

## Introduction

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Senate Concurrent Resolution No. 47 of the Regular Session of 2000 requested that the State Auditor review and identify fiscally related powers conferred upon or assumed by the executive branch since 1987 that may be reclaimed or reasserted by the Legislature. The resolution states that “the basic and constant issue debated upon between the legislative and executive branches is the safeguarding and assertion of legislative authority and independence versus the need or desire for flexibility and freedom from legislative controls on the part of the executive branch.” The resolution suggests that the Legislature’s dominant role in fiscal affairs under the State Constitution has, over time, shifted inappropriately to the executive branch.

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### **The Separation of Powers Principle**

Executive and legislative branches of state governments exercise separate but complementary powers that are generally outlined in constitutional and statutory provisions. Under the broad scope of the separation of powers principle, the legislative branch is assigned the power to make laws and appropriate funds while the executive branch is charged with the responsibility of executing laws and expending funds. However, at times there can be conflict between the two branches if it is perceived that those basic powers are encroached upon. In such cases, states may be called upon to clarify the exercise of those powers.

With regard to the exercise of powers, it is clear that lawmaking power rests with the legislature and that enacting appropriation measures is an exercise of that lawmaking power. The power to appropriate the money of the state is exclusively a legislative power—it can be exercised only by the legislature.

It is also clear that it is the prerogative and duty of the governor to execute the laws. In addition, the governor has the authority to use some discretion in applying the energies and resources made available by the legislature to achieve the purposes or objectives of the laws.

### ***Governors’ budgetary powers***

Formal powers of governors include but are not limited to formulating and executing the budget, administering state agencies, and controlling state programs. Governors have initial responsibility for preparing the budget and in most states are expected to submit an executive budget bill. Alan Rosenthal, noted authority on the relationship between governors and legislatures, asserts that budget formulation may be one of the greatest and most important of all of the governor’s powers.<sup>1</sup>

Budget formulation is a vehicle for governors to initiate policy for the state and express priorities for state spending. In addition to initiation power, governors have rejection power. Governors can reject the budget passed by the legislature by vetoing line items in the appropriations bill.

Rosenthal, one of the first authors to examine the relationship between governors and legislatures, notes:

If initiation allows governors the opening salvo, the power of rejection gives them the last, or almost the last, word... Political scientists lavish considerable attention on the formal power to veto, which is possessed by all but one of the nation's governors. Only the chief executive of North Carolina lacks that power, and has tried to obtain it—albeit without success.<sup>2</sup>

Tom Loftus, the longest serving speaker of the house in the Wisconsin legislature, argues that the governor's veto power tips the balance of power in favor of the executive.<sup>3</sup> Thad Beyle, a researcher on the powers of governors, addresses this issue in a recent publication. He observes that it could be argued that "the use of the veto is a sign of gubernatorial weakness rather than strength because strong governors win the battle through negotiation rather than confrontation with the legislature."<sup>4</sup>

Some governors use the veto more often than do other governors. However, the frequency of use is not necessarily an indication of gubernatorial power.

Governors have the responsibility of administering state government. In exercising this responsibility, governors can exercise executive judgment to ensure that legislative objectives can be accomplished by a lesser expenditure of funds than appropriated. Commenting on this issue, the Supreme Judicial Court of Massachusetts found:

The constitutional separation of powers and responsibilities, therefore, contemplates that the Governor be allowed some discretion to exercise his judgment not to spend money in a wasteful fashion, provided that he has determined reasonably that such a decision will not compromise the achievement of underlying legislative purposes and goals.<sup>5</sup>

### ***The powers and responsibilities of state legislatures***

Legislatures also have a firm base for exercising power. As a rule, the executive and legislative branches participate in different phases of the budgetary process. Typically, the legislature's principal budgetary role is reviewing and modifying, as necessary, a proposed budget developed by the executive branch. Legislatures can add, subtract, or eliminate funds, programs, and projects as a consequence of their review.<sup>6</sup>

Legislatures have responsibility for reviewing the budget and adopting it in the form of an appropriations act or acts. Thus, overseeing the budget and attempting to exercise some measure of control are legislative rather than executive prerogatives.

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## Constitutional and Statutory Provisions in Hawaii

Hawaii's State Constitution and state statutes identify the powers and responsibilities of each branch of government. Constitutionally, the governor is required to present a two-year budget to the Legislature in each odd-numbered year. This budget is to include a complete plan of proposed expenditures of the executive branch, estimates of the aggregate expenditures of the judicial and legislative branches, anticipated receipts of the State, and other information that the Legislature may require. In each even-numbered year the governor may submit a bill to amend appropriations for operating and capital expenditures for the current biennium.

The Legislature is required in turn to submit to the governor an appropriation bill or bills that provide for the anticipated total expenditures of the State. The governor is not required to accept the appropriation bill. Under Article III, Section 16 of the State Constitution, the governor has the responsibility to approve and the power to veto bills passed by the Legislature. Except for items appropriated to the legislative and judicial branches, the governor may veto any specific item or items in any bill that appropriates money for specific purposes by striking out or reducing those items. Other bills can only be vetoed as a whole.

In turn, the Legislature is not required to accept any vetoes. The Legislature may convene in special session to act upon any bill returned by the governor. However, if the Legislature fails to convene, vetoed bills or line items do not become law. After the Legislature reconsiders a vetoed bill or line item or items, a two-thirds vote of all members of each house enables the bill to become law.

Provisions to control the expenditure rate of state-appropriated moneys and to reduce such expenditures must be made by law. No public money shall be expended except pursuant to appropriations made by law. Attorney General Opinion No. 97-1 asserts that constitutional and statutory provisions require a balanced budget.

The executive branch has considerable budgetary flexibility under Chapter 37, Hawaii Revised Statutes (HRS). Unless otherwise provided by law, appropriations to departments are the maximum amounts authorized for those departments and the governor and the director of finance are given explicit powers to reduce those appropriations. Under Section 37-37, HRS, the director of finance can, with the governor's

approval and after notifying departments, reduce the amount allotted to the departments. Section 37-74 also allows the Department of Budget and Finance to withhold planned expenditures if the department finds that the expenditures are greater than necessary to execute the programs at the level authorized by the governor and the Legislature, or if state revenues will be insufficient to meet the authorized expenditures.

In addition, under Section 37-46, the director of finance can transfer non-general funds to the general fund, but must inform the Legislature of that transfer. Also, Section 36-21, HRS, gives the director of finance the flexibility to invest state funds under two broad conditions:

1. When the director feels such funds are in excess of the amounts necessary to meet the immediate needs of the State; and
2. Where the director believes the investment will not impede or hinder the necessary financial operations of the State.

Legislative responsibilities are summarized in Section 37-66, HRS. The Legislature is required to:

- Consider the long-range plans...and the budget and revenue proposals recommended by the governor....
- Adopt programs and the state budget and appropriate moneys to implement the programs it deems appropriate
- Adopt other such legislation as necessary to implement state programs
- Review the implementation of the state budget and program accomplishments and execution of legislative policy implementation.

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## Previous Studies

A number of our prior studies addressed related issues. In *Hawaii Constitutional Convention Studies 1978, Article VI: Taxation and Finance*, we noted that legislative power over the purse began to slip away with the emergence of the executive budget movement. We also noted the power of the governor to execute the budget and other appropriations after they are passed by the Legislature—to grant or to withhold funds, to transfer funds from one program to another, and to otherwise modify the appropriations made.

We noted in 1978 that the Legislature had attempted to regain control but had managed to exert its influence in only two areas:

1. Specifying the details that must be included in the executive budget to be submitted to the Legislature; and
2. Insulating its own budget and the budget of the Judiciary from the item veto and the reduction veto powers of the governor.

In *Legislative Review of State Programs*, Report No. 91-11, we identified five major themes or issues:

1. Information provided to the Legislature needed to be improved;
2. The Legislature's staff resources and capacity needed to be enhanced;
3. The Legislature needed to strengthen its capability to generate independent requests for information and analysis;
4. Budgetary information should be shaped to help the Legislature focus on incremental decisions; and
5. The PPB (Planning, Programming, and Budgeting) system should be streamlined in ways designed to facilitate legislative review.

We cited the massive volume of information supplied to the Legislature and noted that the Legislature often could not make effective use of this information. This was particularly troublesome when new initiatives or programs were unveiled during the session. Such initiatives escaped probing legislative review.

In a *Study of Executive Expenditure Controls*, Report No. 91-15, we indicated that the Legislature's most important source of power and authority was its control over appropriations. The report also noted that a shift had occurred in favor of the executive branch in the expenditure of funds authorized by legislatures. Legislatures had authorized governors to withhold expenditures to below the authorized levels, to transfer and allot funds in ways other than originally legislated, and to control the overall execution of the appropriations. We found that the administration had the authority to require executive agencies to spend less than what they were appropriated. However, there was room for improvement in the way in which that authority was exercised.

In our *Study of the Fiscal Relationship Between Hawaii's Legislative and Executive Branches*, Report No. 93-2, we stated that legislative control over both budget review and budget execution had diminished over the years. Specifically, we found that:

1. With respect to budget review, the Legislature lacked the resources to deal with the executive branch on an equal footing. Current

budget documents were obscure and difficult to use, much of the needed information was missing, budget requests and information were not submitted in a timely manner, and staffing was insufficient.

2. With respect to budget execution, the Legislature had granted the executive so much latitude that legislative power to direct state policies through program appropriations had been undermined.

We stated that in Hawaii, giving the executive branch increasing authority over the enacted budget had weakened legislative control of policy. The Legislature had regularly included provisions in the general appropriations acts that allowed the governor to make transfers among appropriations and programs. The governor needed some flexibility to deal with changes in the State's financial situation, but these provisions had weakened the Legislature and undermined the democratic process.

We noted that legislative appropriations acts continued to routinely include provisions allowing the chief executive to transfer appropriations. We felt that the Legislature should seriously consider whether these flexibility provisions were necessary and warranted carry-over from one legislative appropriations act to the next.

We noted that the State's allotment system also added to executive flexibility. The executive's power to restrict appropriations made it difficult to ensure that legislative priorities were met. We stated that the Legislature could protect its priorities by enacting legislation limiting the governor's authority to make cuts.

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## Objectives of the Review

1. Determine the degree to which Hawaii's executive branch has achieved dominance in fiscal decision-making powers over the legislative branch.
2. Determine the fiscally related powers that can be asserted or reclaimed by Hawaii's Legislature.
3. Make recommendations as appropriate.

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## Scope and Methodology

Our principal period of review was FY1986-87 to FY2000-01. However, prior years were reviewed as necessary to provide sufficient analysis. We reviewed the State Constitution, key statutes, budget acts and provisions, the executive budget, gubernatorial memoranda and vetoes, legislative committee reports, and various financial documents.

In addition, we reviewed relevant studies conducted by our office, reports from the National Conference of State Legislatures, commentary by experts in the field, and Governmental Accounting Standards Board requirements. We also interviewed legislators, personnel from the Department of Budget and Finance and the Department of Accounting and General Services, a former State Auditor, and legislative staff in Hawaii and other states.

Our work was performed from May 2000 through January 2001 in accordance with generally accepted government auditing standards.

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# Chapter 2

## The Legislature Could Pursue Options To Enhance Its Fiscal Powers

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In requesting this study, Senate Concurrent Resolution No. 47 posited “a serious imbalance in executive-legislative fiscal relations, one not intended by the State Constitution.” According to the resolution, a review of “the trend in favor of executive flexibility and discretionary authority” would enable the Legislature to “reassert its dominant role in fiscal matters.” The resolution asked us to identify any fiscally related powers conferred upon or assumed by the executive branch since 1987 that may be reclaimed or reasserted by the Legislature.

During our review, we heard a variety of conflicting opinions regarding the degree to which there exists a legislative-executive imbalance. We found few specific instances in which the executive branch’s fiscal powers had increased since 1987. Indeed, since 1987, the Legislature appears to have reduced the executive branch’s fiscal powers in certain respects.

Nevertheless, we did determine that should Hawaii’s Legislature desire to do so, it has a number of options to counter the powers of the executive branch. Some of these options are designed to contest executive branch powers, and include but may not be limited to overriding the governor’s vetoes and developing a separate budget from the one prepared by the executive branch. Other options, if implemented, could check or curtail the executive branch powers. Such options include but are not limited to repealing special or revolving funds, modifying certain sections of Chapter 37, Hawaii Revised Statutes, and requiring that the Legislature approve budget cuts. To enhance its powers, the Legislature could:

- Strengthen its technical capabilities;
- Exercise more of its existing powers over appropriations;
- Take on additional budgetary powers; and
- Tighten its control over executive branch spending.

A task force of the National Conference of State Legislatures notes that state legislatures have taken on more responsibilities and exercise more authority compared to the governor and the executive branch than they did in the past.<sup>1</sup> However, the relationship between the two branches of

government is not easily resolved. Sometimes state supreme courts have been asked to referee conflicts between the legislative and executive branches over their relative powers.

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## Summary of Conclusions

1. Hawaii's Legislature generally resembles other states in its exercise of fiscal powers, but does not play as formidable a role in the budget development and enactment processes as in some other states. As has been done elsewhere, Hawaii's Legislature could act to curtail executive branch flexibility and exercise considerably more control over the use of state resources.
2. The Legislature could take steps to assert its will and improve its ability to review and monitor the State's economic condition and the actions of the executive branch.

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## The Legislature Could Take Steps To Expand Its Technical Capabilities

The Legislature's technical capabilities are reflected in its ability to access revenue and expenditure data and in the functions of its committees and support agencies. The Legislature could take a series of steps to expand its technical resources to review and assess a variety of fiscal data.

### *Option 1: Establish on-line access by the Legislature to fiscal data of every state agency*

Using advanced computer technology, legislatures can gather and analyze vast amounts of information, thus enhancing their policymaking capability. A 1994 task force of the National Conference of State Legislatures (NCSL) identified options that legislatures could pursue to maintain their policymaking capability and remain an independent, co-equal branch of government.<sup>2</sup> One option identified by the task force was to review and apply new technology to improve the efficiency of the legislative process and to increase legislatures' access to information.

In another report, the NCSL observed that effective budget oversight depends on access to high-quality fiscal data. According to the NCSL, direct on-line access by legislators to fiscal data is essential for monitoring the budget effectively. On-line access allows legislatures to monitor agency operations, conduct continuous oversight and reduce information gaps, and select fiscal information that would be useful.<sup>3</sup>

Many state legislatures have direct, on-line access to agency expenditure information. In 1992, NCSL reported that Legislatures in half the states had direct, on-line access to some type of fiscal data including revenue collections, agency expenditures, or federal funds receipts.<sup>4</sup>

Hawaii's Legislature has previously explored establishing on-line access to fiscal data from every state agency. The Supplemental Appropriations Act of 1992 required that the executive branch provide the Legislature with electronic access to budget data such as the budget journal (BJ) tables and base numbers, and other types of information the Legislature might deem appropriate. In 1997, the Legislature, through a budget proviso, required the Department of Budget and Finance to be the lead agency in providing the Legislature with electronic access to executive budget data.<sup>5</sup> The 1997 law also required the Department of Budget and Finance to coordinate with the Department of Accounting and General Services to integrate the BJ tables with the State's fiscal accounting and management information system (FAMIS) so that actual expenditure data could be displayed in the BJ tables.

The Department of Education is required to provide the Legislature with access to its information systems. Specifically, the department must provide electronic access to computer-based financial management, student information, and other information systems to the Legislature and the Auditor. However, full on-line access by the Legislature to executive branch fiscal data does not yet exist.

***Option 2: Start up the Joint Legislative Budget Committee and fund the Office of the Legislative Analyst***

An examination of available options to expand the Legislature's technical capabilities could involve a review of the roles and functions of the Joint Legislative Budget Committee and the Office of the Legislative Analyst. In this review, the Legislature may be able resolve a number of issues regarding the relationship of these two entities to the Legislature's money committees as well as to the Office of Auditor.

The Legislature through Act 347, Session Laws of Hawaii 1990, established the Joint Legislative Budget Committee and the Office of the Legislative Analyst. These two entities have been codified in Chapter 21F, Hawaii Revised Statutes (HRS), but have not become operational.

The preamble to Act 347 found that other state legislatures had fiscal policy offices that provide the legislatures with revenue and expenditure data from which economic and fiscal policies are developed.<sup>6</sup> The preamble also noted that the Hawaii Legislature had been relying on economic and fiscal analyses performed by the executive branch and the private sector and that this dependency had created an inherent conflict of interest that precluded the Legislature from operating independently. In addition, the preamble noted that the Legislature had come to rely on the use of session-only legislative staff or employees on loan from the executive branch.

Legislative expectations for the two entities are found in Act 347. It was the Legislature's intent that a new permanent legislative committee, with

the assistance of a new legislative analyst office, would perform independent, in-depth analyses of the State's budget, revenues and expenditures, economic conditions, and tax policies.

According to Chapter 21F, HRS, the Joint Legislative Budget Committee is to comprise five members of the Senate and five members of the House, selected by the senate president and house speaker. Committee members would include members of the majority and minority leadership and committee co-chairs would include the chairpersons of the Senate Ways and Means Committee and House Finance Committee.

The Joint Legislative Budget Committee is to ascertain facts and make recommendations to the Legislature concerning the State's budget, revenues and expenditures, organization, and functions, and other matters as provided by the Senate and House rules.

The Office of the Legislative Analyst is to be administered by the Joint Legislative Budget Committee. Duties of the legislative analyst's office include:

- Providing the Legislature with research and analysis of current and projected state revenues and expenditures;
- Providing the Legislature with an analysis of the governor's proposed levels of revenue and expenditures for biennial and supplemental budgets;
- Providing an analysis of the impact of the governor's proposed revenue and expenditure plans;
- Conducting research on matters of economic and fiscal policy;
- Providing economic reports and studies on the State's economy, including trends and forecasts;
- Conducting budget and tax studies and providing general fiscal and budgetary information;
- Reviewing and making recommendations on the operation of state programs in order to appraise the implementation of state laws regarding the expenditure of funds and to recommend means of improving efficiencies; and
- Recommending to the Legislature changes in the mix of revenue sources for programs, in the percentage of state expenditures devoted to major programs, and in the role of the Legislature in overseeing state government expenditures and revenue projections.

Other states have joint budget committees, legislative analyst offices, or both. Twenty-two other states have joint legislative fiscal committees. In some states, these committees have oversight functions or can formulate budget recommendations. In California, the committee acts on budget issues that arise after the enactment of the budget, usually involving an executive branch request to spend unanticipated funds or to spend budgeted money in a different way.

Some states' legislative analyst offices have duties similar to those established in Chapter 21F. For example, California's office analyzes the budget bill and reports that analysis to the Joint Legislative Budget Committee. This office also reviews requests by the administration to make changes to the budget after it is enacted, prepares special reports throughout the year on the state budget and topics of interest to the legislature, and prepares analyses of all proposed initiatives.

There are a number of issues or questions that will need to be resolved before putting the Joint Legislative Budget Committee and the Office of the Legislative Analyst into operation. For example, the relationship of the office to the two money committees will need to be resolved. The office is required to conduct analyses of the governor's proposed revenues and expenditures for biennial and supplemental budgets as well as to review the governor's proposed revenue and expenditure plans. It is not clear whether this work would duplicate that of the two money committees. In addition, the roles and responsibilities of the Joint Legislative Budget Committee and the Office of the Legislative Analyst during the interim between sessions will need to be clarified.

Also, the Legislature may wish to clarify the respective roles of the Office of the Legislative Analyst and the Office of the Auditor. For example, the roles of the Office of the Legislative Analyst and the Office of the Auditor could be better aligned by concentrating the responsibilities of the Office of the Legislative Analyst on pre-enactment analysis. Chapter 21F, HRS, could be revised to require the Office of the Legislative Analyst to analyze bills that propose to establish new special or revolving funds, trust funds, and trust accounts. In addition, Section 21F-7(a)(7) provides that the legislative analyst shall review and make recommendations on the operation of state programs in order to appraise the implementation of state laws regarding expenditures and to recommend means of improving their efficiency. This could be interpreted as a post-enactment, audit-like function that is a responsibility of the Office of the Auditor. Section 21F-7(a)(7) thus could be removed from the required purposes of the Office of the Legislative Analyst.

***Option 3: Expand full-time staffing for the Legislature’s “money committees”***

A 1989 study conducted by the National Conference of State Legislatures found that the Hawaii Legislature was understaffed in the fiscal area compared to legislatures in many other states. It noted that the House Finance Committee and the Senate Ways and Means Committee had small core staffs and were forced to rely upon temporary, relatively inexperienced individuals for concentrated budget work. The use of such temporary staff could not meet the Legislature’s needs for fiscal analysis. The study noted that due to short-term demands and time pressures, the kinds of economic and fiscal analysis that the legislators sought could not be done during sessions. The study recommended that the Legislature develop its own independent, full-time fiscal analysis capability and discontinue the practice of borrowing staff from executive agencies and the private sector.<sup>7</sup>

The money committees continue to have relatively small staffs. The Senate Ways and Means Committee has four permanent staff and 11 session staff. The House Finance Committee has seven permanent staff and 14 session staff.

Other states have effectively expanded the number of full-time staff of the money committees. Such expansion may ensure greater staff continuity from session to session and provide for a more extensive economic and fiscal analysis. However, this approach may also have some drawbacks. It may not be cost effective if both committees perform duplicative functions. In addition, should the Legislature decide to fund the Office of the Legislative Analyst, the staffing patterns for that office as well as the two money committees will need to be assessed.

***Option 4: Determine whether responsibility for financial audits of executive branch agencies should be transferred to a legislative service agency***

Article VII, Section 10 of the State Constitution and Chapter 23, HRS, require the State Auditor, whose office is attached to the Legislature, to conduct post-audits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State and its political subdivisions and to certify to the accuracy of all financial statements issued by the respective accounting officers. The Auditor must also make such additional reports and conduct such other investigations as the Legislature may direct.

Although Hawaii state government contains 18 departments and scores of other offices, boards, and commissions, the Office of the Auditor normally conducts no more than three or four financial audits each year through contracts with certified public accounting firms. Financial audits of agencies are also performed by public accounting firms under contract to the agencies themselves or under contract to the Department of Accounting and General Services. These audit reports are not routinely issued as published reports available to the public.

The National Conference of State Legislatures reports that auditing principles and standards require that the post-audit of financial transactions be conducted by an entity independent of the one being reviewed. NCSL asserts that according to this principle, executive agencies of state government should be audited by the legislative branch or by another independent office.<sup>8</sup>

Although the Office of the Auditor conducts few financial audits per year, the office's other audits and studies do address a wide range of fiscal matters of legislative concern. The Legislature could review the extent to which it wishes the Office of the Auditor to contract for the financial audits. If the Legislature decides that the Office of the Auditor should be responsible for a greater number of financial audits per year, the Legislature could consider appropriating funds to the Office of the Auditor instead of to the executive branch.

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## **The Legislature Could Exercise More of Its Existing Powers Over Appropriations**

### ***Option 1: Override the governor's vetoes***

Hawaii's Legislature could exert some existing powers to contest the executive branch. These powers include but may not be limited to overriding the governor's vetoes and deciding on the best use of budget provisos.

Nationwide, almost every governor has some degree of veto power over appropriations passed by the legislature. However, in states where the governor has veto power, legislatures can override vetoes. Both vetoes and overrides can occur in Hawaii, but overrides are rarely used.

In 43 states, the governor can veto funding for a particular line item in the appropriations bill. In 35 states, the governor can veto funding for an entire program or agency. Also, some states allow the governor to veto the language accompanying the appropriation, the language explaining how money is to be spent, and provisos on the expenditures of the appropriation.

In Alaska, California, Georgia, Louisiana, New Jersey, and New Mexico, the governor can veto almost anything in the budget bill including funding for an entire program or agency. In Louisiana, the governor can also veto the entire budget bill. Some governors have been known to veto hundreds of bills. According to a recent *Governing* magazine article, New Mexico's governor vetoed 28 bills from the 2000 legislative session. However, he has vetoed more than 200 bills in some years, and Oklahoma's current governor vetoed over 200 measures in the first six years of his term of office. In 1998, Governor George Pataki of New York used his line-item veto authority to zero out more than 1,000 items from the state budget.<sup>9</sup>

In Hawaii, the State Constitution enables the governor to veto entire bills and veto line items in appropriations bills. The governor cannot veto funding for an entire program or agency. Nor can he or she veto the language accompanying the appropriation, the language explaining how money is to be spent, or provisos on the expenditures of the appropriation.

In one example, the governor exercised his line-item veto power on House Bill No. 1900, the bill for the Supplemental Appropriations Act of 2000. Following the session, he returned the bill with a \$9,075,000 reduction in the amount of capital improvement projects authorized for FY1999-00 and \$44,017,000 for FY2000-01. He also reduced FY2000-01 program appropriations by \$3,425,000.

Legislatures can limit the effect of gubernatorial vetoes by overriding them. In all but six states, an override requires an extraordinary majority in each house: a three-fifths vote is needed in six states and a two-thirds majority is required in 38 states. While overrides are rare, occasionally legislatures have successfully challenged governors in this manner.<sup>10</sup>

Hawaii's constitution enables the Legislature to override both line-item vetoes of the budget bill and vetoes in toto of other bills. The override requires a two-thirds majority of each house. Generally, it is equally difficult to override both types of vetoes. If the veto occurs between regular legislative sessions, a special session must be convened to consider the override. The Legislature convened a special session in August 2000 but did not attempt to override the line-item vetoes of House Bill No. 1900.

***Option 2: Decide on the effective use of "budget provisos"***

The budget bills contain program appropriation provisions, capital improvement program provisos, and special provisions (sometimes called "budget provisos"). Some of these provisions serve to clarify legislative intent or specify how selected appropriations are to be used. Other provisions give the executive branch considerable flexibility in using the funds appropriated.

Hawaii's provisos reflect the capacity of legislatures nationwide to clarify intent and establish priorities in appropriations bills. Although the budgets proposed by executive branches set the agenda for budget discussion and negotiation, and in some states are adopted with relatively few changes, legislatures have considerable power to establish priorities through the budget and to stipulate how budgeted funds are to be spent. Forty-seven legislatures have the power to change the budget proposed by the executive and judicial branches of government. Only Maryland, Nebraska, and West Virginia limit the legislature's power to increase or decrease the budget items.<sup>11</sup>

Legislatures can direct the spending of state money specifically through language in the appropriations bills and accompanying documents. In Hawaii, legislative intent is articulated through sections of the budget bill, in committee reports, and in the legislative journal. The program appropriation provisos are a highly visible means of directing spending and clarifying legislative intent. In 1999, the Legislature used 59 operating budget provisos to clarify intent on the expenditure of over \$1 billion in funding to executive branch agencies. Neither the State Constitution nor state statutes limit the number of provisos.

Of the 59 program appropriation provisos in Act 91, SLH 1999 (the General Appropriations Act), a total of 41 provisos either provided for specific expenditures or allowed such expenditures. With just a few exceptions, these provisos restricted the use of funds to specific purposes.

Over one-half of the provisos required agencies to submit a plan or a report to the Legislature. Others required or allowed the transfer of funds or services; required an agency to implement specific policies, procedures, or plans; or required studies or audits. Such provisos help to solidify legislative expectations and provide the Legislature with information it needs to make fiscal decisions.

Other types of provisos can give the governor and the executive branch considerable spending flexibility. Flexibility is found in the special provisions, capital improvement program provisions, and bond issuance provisions. We reviewed these provisos in selected budget laws since 1987. The budget laws that we reviewed contained over 30 special provisos. Most of the special provisos gave the executive branch some type of flexibility in using or controlling expenditures and were included in each of the acts reviewed. However, some provisions have either been added or dropped from act to act.

One special provision from Act 91, SLH 1999, authorizes the governor to transfer operating funds between appropriations with the same means of financing, within an expending agency.<sup>12</sup> Another provision allows departments or agencies to transfer positions within the position ceiling with the prior approval of the governor.<sup>13</sup> A third provision allows the governor to transfer funds from one cost element to another within any capital improvement project, but total project costs cannot be exceeded.<sup>14</sup> Two other provisions affect capital improvement projects through the use of a project adjustment fund. Unrequired balances from capital improvement projects are to be transferred to a project adjustment fund. If the appropriations for other projects are insufficient, the governor may make supplemental allotments to those projects from the project adjustment fund.<sup>15</sup>

In some instances the Legislature has reduced the extent of the flexibility granted in prior special provisions. For example, under Act 216, SLH 1987, the governor was allowed to establish 15 permanent and 15 temporary positions to any program area. The act did not stipulate that the governor report these positions to the Legislature. However, Act 91, SLH 1999, allows the governor to establish five permanent positions and contains a requirement to report these positions to the Legislature.<sup>16</sup> In addition, through a special provision in Act 216, SLH 1987, the Legislature allowed state agencies to expend special, revolving, and trust funds in excess of legislative appropriations.<sup>17</sup> This type of provision is no longer in the budget act.

The Legislature also has given the executive branch flexibility in funding capital improvement projects through the capital improvement project provisos. In Act 91, SLH 1999, such provisions were contained in Sections 65 through 105 inclusive. Some of these provisos lapse the appropriations for projects authorized in previous budget acts. Others provide for considerable discretion on the part of the executive branch.

Bond provisos such as those found in Sections 106 through 115 inclusive of Act 91, SLH 1999, also give the executive some discretionary powers. For example, Section 106 allows the governor to use general fund savings to finance capital improvement projects financed by the general obligation bond fund. It also allows the governor to replace general obligation bonds with general obligation reimbursable bonds.

The Legislature could examine its use of budget provisos and decide whether it should continue certain provisos, codify others, and discontinue still others. The Legislature would benefit from continuing those types of provisos that most convincingly clarify legislative intent and that control, monitor, and prioritize state spending. If some of the “flexibility provisos” provide what the Legislature views as necessary flexibility to the governor or other departments of the executive branch, the Legislature could codify and incorporate those provisions into Chapter 37, Hawaii Revised Statutes. This would eliminate the need to carry them over from one appropriations act to the next. Codifying the provisos could provide greater continuity in legislative intent, provide greater stability in the application of the law, and demonstrate their importance and necessity.

Codifying the provisos may have at least one potential drawback. It may be difficult in the future to repeal codified provisions that give the executive branch flexibility or discretionary powers.

Finally, the Legislature could discontinue unnecessary provisos or provisos that give the executive branch more flexibility than the Legislature is comfortable giving. In 1993 we suggested that the

Legislature consider whether such provisions are necessary and warrant carry-over from one legislative appropriations act to the next.<sup>18</sup>

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## **The Legislature Could Take On Additional Budgetary Powers**

The Legislature could assume additional budgetary powers exercised by some other state legislatures. Although typically the executive branch prepares and proposes a state budget, some legislatures also prepare a budget separate from the one developed by the executive branch. Some legislatures also require the use of fiscal notes to promote fiscal accountability.

### ***Option 1: The Legislature could prepare a budget bill separate from the executive branch's bill***

Most state legislatures play a minor role in the budget preparation stage, limited to reacting to the appropriations bills written by the executive branch. Hawaii is one of 28 states in which the executive branch writes the appropriation bill to be introduced in the legislature. In these states, the executive branch's proposal establishes the agenda for budget discussion and negotiation and in some of these states the budget is adopted with relatively few changes. However, strong legislative budget processes dominate in a few states, where the executive budget may be largely disregarded.

Several states, including Arizona, Colorado, and Texas, prepare comprehensive budgets that are separate from the executive budget. In Arizona and Colorado, staff of joint budget committees prepare the appropriations bills. In Texas, a joint legislative agency, the Legislative Budget Board, writes the budget to be introduced. The governor's budget is developed by the Budget and Planning Office. The two money committees then develop their bills on the basis of the executive and legislative alternative budgets.

Hawaii's Legislature modifies the budget bill prepared by the executive branch, passes the amended bill, and submits it to the governor for approval. The bill passed by the Legislature can properly be viewed as the Legislature's bill. However, this is not the same as if the Legislature wrote its own bill, separate from the executive branch bill.

Hawaii's Constitution does not prohibit the Legislature from developing a budget separate from the budget proposed by the executive branch. The Constitution requires the governor to present a budget to the Legislature in each odd-numbered year. In turn, the Legislature must transmit an appropriation bill to the governor providing for the total expenditures of the State for the ensuing biennium. The Constitution is silent on the power of the Legislature to develop a budget.

The Legislature could prepare a comprehensive state budget separate from the one prepared by the executive branch. The comprehensive,

separate budget could be drafted by staff from either money committee or from a joint budget committee, as in some other state legislatures. Should the Legislature decide to start up the Joint Legislative Budget Committee and the Office of the Legislative Analyst under Chapter 21F, HRS, the responsibility for preparing the budget could fall to these entities, with appropriate amendments to Chapter 21F.

***Option 2: Require the use of fiscal notes to assess the impact of proposed legislation***

As noted in one of our 1993 studies, the Legislature could require the use of fiscal notes to assess the fiscal or financial impact of proposed legislation on state revenues and expenditures. A fiscal note examines whether a bill will increase or reduce expenditures, change the yield of an existing tax, affect personnel requirements or levels of service, affect the tax base, or change funding for existing programs. Fiscal notes help to control spending by making legislators aware of the cost implications of new legislation. In 1992, a total of 38 states were reported to rely on fiscal notes as a means of promoting fiscal accountability.

Fiscal notes prepared by legislative staff could safeguard and promote the independence of the Legislature. In order to analyze the fiscal impact of bills, the Legislature could require the executive to submit information on long-term program costs for all new programs. The Legislature could stipulate that no new program be implemented prior to careful scrutiny by the Legislature of the executive's fiscal rationale.

***Option 3: Gain control over the volume and quality of budgetary information supplied to the Legislature***

We noted in our 1991 *Legislative Review of State Programs* that the volume of information supplied to the Legislature was frequently massive and that the Legislature often could not make effective use of much of the information it received. Factors such as brief session periods and reliance on small and inexperienced staff made it difficult to process and interpret all the available information, to question its completeness, or to explore alternatives.

Coming to grips with this volume of information may require a renewed focus on the types of information that the Legislature needs rather than on what the executive branch simply supplies. In addition, streamlining the Planning, Programming, and Budgeting (PPB) system could also facilitate legislative review of the State's budgetary needs. An element of the streamlining process could include the judicious use of effectiveness measures in the PPB documents. We noted in 1991 that the budget was virtually bereft of unit-cost and cost-effectiveness measures.

A 1997 publication from The Council of State Governments promotes the use of performance measures and profiles a number of states and agencies that integrate performance data into the budget-making process.<sup>19</sup> The report cites a number of best practices and programs in

performance measurement. One of these stems from Arizona's Budget Reform Act, enacted in 1993, which compels state agencies to develop strategic plans and performance measures to support their budget requests. The original act was amended to define the process for conducting legislative program reviews. Performance measures are to be stated in terms that are consistent with a budget unit's goals and objectives and that emphasize results. The governor's office of strategic planning and budgeting and joint legislative budget committee staff review program areas and jointly produce a report of their findings. They jointly recommend whether to retain, eliminate, or modify funding of those program areas.

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## **The Legislature Could Tighten Its Control Over Executive Branch Spending**

Most of the options open to the Legislature revolve around mechanisms to tighten spending controls. These options include limiting the ability of the governor and the director of finance to reduce the allotments to state agencies, eliminating the exemptions to the allotment requirements, repealing selected special and revolving funds, revisiting the budget requirements for the Hawaii Health Systems Corporation, and other options. Adopting these measures could strengthen the Legislature's power and control over state spending without completely eliminating the fiscal flexibility of the executive branch.

### ***Option 1: Modify Chapter 37, HRS, to clarify the parameters under which the governor and director of finance can reduce allotments***

Governors in most states have some degree of authority to reduce appropriations. However, a governor's authority to reduce appropriations is typically limited.

Hawaii's allotment system contributes to executive flexibility. Section 37-31, HRS, indicates that the total appropriation for any department is deemed to be the maximum authorized for that department. It also gives the executive branch some flexibility in using those appropriations:

The governor and the director of finance should be given the powers [regarding the allotment system] in order that savings may be effected by careful supervision throughout each appropriation period with due regard to changing conditions; and by promoting more economic and efficient management of state departments and establishments.

The Department of Budget and Finance is also allowed to reduce allotments to state agencies when the director of finance determines that probable receipts for an appropriation are less than was anticipated.<sup>20</sup> The director of finance can, with the approval of the governor, and after notification to departments, reduce the amount allotted to the departments. However, the director of finance must notify the leaders of

the Legislature if the proposed reduction exceeds 2.5 percent of the total general fund appropriation made by the Legislature.

Section 37-74, HRS, allows the Department of Budget and Finance to withhold planned expenditures if the department finds that the expenditures are greater than necessary to execute the programs at the level authorized by the governor and the Legislature, or if state revenues will be insufficient to meet the authorized expenditures. Also, Section 37-74(b) states that “the appropriations by the Legislature for a biennium shall be allocated between the two fiscal years of the biennium in the manner provided in the budget or appropriations act and as further prescribed by the director of finance.”

In addition, Section 37-46, HRS, allows the director of finance to transfer non-general funds to the general fund. However, the director is to notify the Legislature within ten days of the transfer and 20 days prior to session.

The allotment system gives the governor and the director of finance the power to restrict appropriations for virtually any reason. The Legislature could modify Chapter 37, HRS, to clarify the parameters under which the governor and the director of finance can reduce allotments to departments in the executive branch. Attorney General Opinion No. 83-4 concluded that

while the allotment system authorizes the governor to avoid wasteful expenditures... or to reduce expenditures where unanticipated revenue shortfalls occur, it does not permit the executive branch to prioritize authorized expenditures and reallocate resources, for to do so would be an usurpation of the legislature’s appropriation powers.<sup>21</sup>

By clarifying the parameters, the Legislature could limit the amount and frequency of such restrictions.

***Option 2: Require legislative approval for budget cuts***

In a number of states, legislatures play a role in cutting the enacted budget. However, in Hawaii, the Legislature has no specific role.

According to NCSL, some states, such as Alabama and Oklahoma, require the full legislature’s approval for reductions other than across-the-board reductions. In Connecticut, legislative approval is needed where the total appropriated amount must be reduced by more than 5 percent. In Arkansas, the legislature biennially determines the share of any budget cuts that an agency must absorb in the event of a deficit. Massachusetts requires legislative approval of gubernatorial cuts. In

New Mexico, appropriations may be reduced only by an act of the legislature. Twelve states require the governor to consult with the legislature before cutting the enacted budget.

As in some other states, Hawaii's Legislature could require that all cuts be approved by the Legislature, stipulate that cuts can only be made "across the board," or provide for a maximum percent reduction. Adopting one or more of these approaches may require amendments to Chapter 37, HRS, which currently contains none of these scenarios.

***Option 3: Modify Chapter 37, HRS, to remove all exemptions to the allotment requirements***

Section 37-40, HRS, contains exemptions to the allotment requirements. The Legislature has modified this section before to reduce executive flexibility. In 1995, the Legislature amended the section to remove the exception for revolving funds.<sup>22</sup> As a result, only trust funds are currently exempt under the section.

According to state statute, trust funds can be expended without appropriations. It is not clear whether the statute allowing for such expenditures conflicts with the State Constitution.

Section 37-40, HRS, allows expenditures from trust funds to be made without appropriation or allotment. However, expenditures cannot be in excess of the amount standing to the credit of the fund. This provision allowing expenditures without appropriation may contravene the State Constitution, which forbids the expenditure of public money except pursuant to appropriations made by law.

Chapter 37 defines a trust fund as "a fund in which designated persons or classes of persons have a vested beneficial interest or equitable ownership, or which was created or established by a gift, grant, contribution, devise or bequest which limits the use of the fund to designated objects or purposes." However, the chapter is silent on whether a trust fund is considered to be "public money." If trust funds are considered to be "public money" then Section 37-40 could be revised to remove trust funds from the exceptions to the allotment system.

***Option 4: Repeal special and revolving funds that fail to demonstrate the necessary linkages***

Special and revolving funds are financing mechanisms created outside the state general fund to provide ongoing support for specific activities or programs in state government. From an agency's perspective these mechanisms may guarantee funding and provide agencies with flexibility to spend excess money without seeking legislative appropriations. However, from a legislative perspective such funds may have less than desirable rationales. They may guarantee for a program a continuing source of revenue that is not fully controlled by the appropriations process.

In one of our 1991 reports on special and revolving funds, we quoted a 1961 report that special funds have led to a lack of accurate accounting of state resources, excess cash reserves being held in special fund accounts, and the practice of earmarking resources instead of budgeting for expenditures.<sup>23</sup> We also noted that special funds give agencies full control over their unappropriated cash reserves, provide a means to avoid the general fund expenditure ceiling, and over time erode the general fund. In another report, we stated that special and revolving funds have distorted the State's financial picture and have eroded the Legislature's control of state finances.<sup>24</sup>

Earmarking through the use of special and revolving funds can serve legitimate purposes. In a 1978 report we stated that earmarking is more defensible when a clear benefit-user charge linkage exists and less defensible when linkage is lacking and earmarking is used solely as a political shield to protect a program by providing it with an automatic means of support.<sup>25</sup>

Left unchecked, a shift from general fund to special fund financing of government programs surrenders control over those funds to the executive branch. The loss of control can extend to virtually the entire operations of a department. During the 1999 legislative session, the Legislature surrendered control over the Department of Commerce and Consumer Affairs' spending when it consolidated a majority of that department's funds into a single Compliance Resolution Fund and allocated \$2.5 million of franchise tax revenues into the fund for each fiscal year beginning July 1, 1999. All revenues, fees, and fines collected by the department are to be deposited into the fund. The fund is used to fund the operations of the department with the exception of the costs related to the Hawaii Broadcasting Authority.

Special fund appropriations accounted for over 21 percent (or \$1.3 billion) of the \$6.0 billion appropriated for executive branch operating costs for FY2000-01 in Act 281, SLH 2000. The Legislature also appropriated slightly over \$250 million in revolving funds.

The Legislature could repeal special and revolving funds that fail to demonstrate the necessary linkages, transfer the balances of those funds to the general fund, and require that the programs previously funded by such funds be henceforth included under the general fund. A number of recommendations from our 1992 report, *Loss of Budgetary Control: A Summary Report of the Review of Special and Revolving Funds*, Report No. 92-14, are still timely. Among other recommendations, we suggested that the Legislature consider repealing the special and revolving funds recommended for repeal in our prior reports, and setting sunset dates for all existing and newly established special and revolving funds.<sup>26</sup>

***Option 5: Revisit the budget requirements for the Hawaii Health Systems Corporation***

In our 1992 *Study of the Division of Community Hospitals*, Report No. 92-6, we found that state laws and policies on budgeting and expenditures had resulted in unrealistic budgets, cash flow problems, deficits, and poor financial management for the community hospitals. The study recommended that the Legislature establish a public corporation to operate the community hospitals and suggested that a special master, along with a transition team, study and plan for the transfer. Act 262, SLH 1996, created the Hawaii Health Systems Corporation. Under Chapter 323F, HRS, the corporation's operating and capital improvement budgets are not subject to review or approval of the governor or any state agency, except where state general funds or capital improvement moneys are requested.

During the 2000 legislative session, a report of the House Finance Committee raised concerns about the impact of Act 262, which had resulted in the corporation being removed from the State's budgeting requirements. The report noted that this has made it difficult for the Legislature to have the same comprehensive oversight of corporation expenditures it had with all other state agencies.<sup>27</sup> Despite the concerns of the House Finance Committee, the Legislature appropriated \$13 million in general funds and \$239 million in special funds for operating costs to the corporation for FY2000-01.<sup>28</sup>

The Hawaii Health Systems Corporation also received emergency general fund appropriations totaling \$38 million over the course of three out of four fiscal years from FY1996-97 through FY1999-00. Appropriating funds to the corporation outside the State's budget requirements provides autonomy to the corporation but may defeat the Legislature's attempts to control state spending.

The Hawaii Health Systems Corporation was created to provide better health care to people, including those served by small rural facilities, by freeing the facilities from unwarranted bureaucratic oversight. Although the corporation was provided with greater flexibility and autonomy, under Section 323F-21, HRS, the Legislature retains some review and oversight authority.

Our office is currently conducting a study of the corporation. Recommendations on how the Legislature could tighten controls may be included in the study report.

***Option 6: Review the impact of the autonomy given to the Department of Education and the University of Hawaii***

The Legislature has given greater fiscal autonomy to the Department of Education and the University of Hawaii than to other executive branch agencies. The Department of Education and the University of Hawaii are both exempted from the allotment system. Also, Section 37-41.5, HRS, allows the Department of Education to carry over up to five percent of EDN 100 (School Based Budgeting) funds and EDN 150

(Comprehensive School Support Services) funds. Such funds do not lapse until the end of the first fiscal year of the next fiscal biennium.

Also, Section 302A-1115 allows the Department of Education to reallocate existing vacant positions and implement internal reorganizations without regard to position variance requirements of the Department of Budget and Finance, provided that these actions redirect resources from state and district offices to the schools.

Act 234, SLH 2000, amended Chapter 29 to stipulate that certain federal funds received by the Department of Education shall not be returned to the general fund. In addition, the department is allowed to increase the federal fund expenditure ceiling if those funds exceed the authorized appropriations.

During the 2000 legislative session, Senate Bill No. 539 proposed a constitutional amendment to give the University of Hawaii autonomy in matters involving only the internal structure, management, and operation of the university. The amendment was ratified in the 2000 general election.

At the request of the Legislature our office published reports in 1991 and 1993 on the administrative flexibility granted to the University of Hawaii and the Department of Education. We noted in 1993 that neither the university nor the department could demonstrate that increased flexibility had resulted in improvements in their educational services.<sup>29</sup> However, we also noted that based upon the performance of both entities in implementing the flexibility granted to them in 1986, the administrative flexibility should be extended indefinitely.<sup>30</sup>

We addressed the issue of carryover funds in our 1992 report entitled, *A Study of Curriculum, Budgeting, and Repair and Maintenance for Hawaii's Public Schools*. We suggested that the Legislature could include a provision requiring the Department of Education to report on the amounts that are carried over and the benefits that result from this practice. Currently Section 37-41.5, HRS, requires the department to submit annual reports to the Legislature and the director of finance on the amount of funds carried over.

The impact of these flexibility measures is currently unknown. The Legislature could require the Office of the Auditor or the Legislative Reference Bureau to review the impact of the autonomy given to the university and the education department.

***Option 7: Authorize only those capital improvement projects that the administration has demonstrated are within state capacities to build within a specified timeframe***

The Legislature typically authorizes a significant amount of funds for capital improvement projects (CIP). Under Act 91, SLH 1999, the Legislature authorized \$723.7 million for capital improvement projects in the state for FY1999-00. The governor's budget request (House Bill No. 1900, 2000 legislative session) increased CIP funding for the current fiscal year (FY2000-01) from \$466.8 million to over \$770 million. In turn, Act 281, SLH 2000, authorized \$860 million for FY2000-01 for approximately 530 capital improvement projects in the state. This represented almost \$90 million more than the original executive request.

Despite the levels of such appropriations, it is unclear whether state agencies have the capacity to construct every project that has been authorized. The Legislature may be giving up power to the executive branch by authorizing more projects and funds than needed. In addition, this creates a large backlog of projects. Because of the long lead time between authorization and implementation, there is the potential for costs to escalate and original appropriation amounts may no longer be adequate to meet those costs.

Projects that are due to lapse may serve as an indication of the extent to which state agencies lack the capacity to construct the projects in a timely manner. In House Bill No. 1900, the governor proposed lapsing \$191.2 million in proposed general obligation bond and general obligation reimbursable bond projects. Almost \$160 million of this amount was for pre-FY1999-00 authorizations.

The Legislature could authorize only those capital improvement projects that are within the capacities of state agencies to build within a specified timeframe. The Legislature could require the Department of Budget and Finance to ensure that executive branch agencies refrain from requesting CIP appropriations when the appropriations cannot reasonably be expected to be expended within the time frame for which the appropriations are requested.

***Option 8: Capitalize on opportunities offered by new accounting standards***

The Governmental Accounting Standards Board (GASB) has introduced new financial reporting requirements for state and local governments. These standards apply to all state and local government entities, including public employee retirement systems, hospitals, healthcare systems, and universities. These requirements are effective in three phases after FY2001-02 based on a government's total annual revenues. However, earlier implementation is encouraged. Hawaii's comptroller has informed Hawaii's state agencies that audited financial statements for FY2001-02 should conform to the GASB Statement 34 requirements.<sup>31</sup> State agencies have been asked not to apply these provisions before the required deadline.

All state and local entities must present a section entitled Management's Discussion and Analysis (MD&A) as part of a comprehensive financial report. This section must include but not be limited to a description of the basic financial statements and an analysis of those statements, as well as a description of the capital asset and long-term debt activity during the year.

Government entities also need to report infrastructure assets. Infrastructure assets are long-lived capital assets that can be preserved for a greater number of years than most capital assets. Such assets include roads, bridges, tunnels, dams, and street lighting systems. They must also report construction in progress. An official from the standards board reports that financial statement user groups are realizing the positive effects of the new standards.

State agencies are required to follow GASB Statement 34 standards. Inclusion of these requirements in comprehensive financial reports could provide for a more objective, complete, useful, and easily readable analysis of the financial activities of state government entities.

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## Notes

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27. House Standing Committee Report No. 868-00 on House Bill No. 1900, Regular Session of 2000.
28. Section 3, Act 281, SLH 2000.
29. Hawaii, The Auditor, *Final Report on Administrative Flexibility Granted to the University of Hawaii and the Department of Education*, Report No. 93-14, Honolulu, November 1993, p. 5.
30. Ibid.
31. Comptroller's Memorandum No. 2000-13, to Heads of Departments dated June 8, 2000.

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## Response of the Affected Agency

### Comments on Agency Response

We transmitted a draft of this report to the Department of Budget and Finance on February 7, 2001. A copy of the transmittal letter to the department is included as Attachment 1. The department's response is included as Attachment 2.

The department responded that the governor's current level of fiscal powers is reasonable when considered within the context of his substantial statewide obligations and responsibilities as mandated by the State Constitution and statutes. The department asserts that removing all or part of such budget and fiscal discretionary authority would significantly impact the governor's ability to carry out his responsibilities. Finally, the department agrees that the Legislature should expand its own technical capabilities to review and assess state fiscal data, as was intended by the creation of the Joint Legislative Budget Committee and the Office of the Legislative Analyst in Act 347, Session Laws of Hawaii 1990.

We made a few minor editorial changes in the final report.

ATTACHMENT

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

February 7, 2001

**COPY**

The Honorable Neal Miyahira  
Director of Finance  
Department of Budget and Finance  
250 South Hotel Street  
Honolulu, Hawaii 96813

Dear Mr. Miyahira:

Enclosed for your information are three copies, numbered 6 to 8 of our draft report, *A Review and Identification of Fiscally Related Powers Conferred Upon or Assumed by the Executive Branch*. We ask that you telephone us by Friday, February 9, 2001, on whether or not you intend to comment on our conclusions. If you wish your comments to be included in the report, please submit them no later than Friday, February 16, 2001.

The 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

Enclosures

BENJAMIN J. CAYETANO  
GOVERNOR



NEAL MIYAHIRA  
DIRECTOR

WAYNE H. KIMURA  
DEPUTY DIRECTOR

STATE OF HAWAII  
DEPARTMENT OF BUDGET AND FINANCE  
P.O. BOX 150  
HONOLULU, HAWAII 96810-0150

February 15, 2001

EMPLOYEES' RETIREMENT SYSTEM  
HAWAII PUBLIC EMPLOYEES HEALTH FUND  
OFFICE OF THE PUBLIC DEFENDER  
PUBLIC UTILITIES COMMISSION

ADMINISTRATIVE AND RESEARCH OFFICE  
BUDGET, PROGRAM PLANNING AND  
MANAGEMENT DIVISION  
FINANCIAL ADMINISTRATION DIVISION

Ms. Marion M. Higa  
State Auditor  
Office of the Auditor  
465 South King Street, Room 500  
Honolulu, Hawaii 96813-2917

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OFC. OF THE AUDITOR  
STATE OF HAWAII

Dear Ms. Higa:

Thank you for the opportunity to address recommendations and options proposed in your draft report, "*A Review and Identification of Fiscally Related Powers Conferred Upon or Assumed by the Executive Branch.*" We would like to submit the following comments.

- 1 We recognize that there has been long-standing debate between the Legislative and Executive branches regarding appropriate levels of budgetary and fiscal authority available to each respective branch. However, we continue to maintain that the Governor's current level of fiscal powers are reasonable when considered within the context of his substantial statewide obligations and responsibilities as mandated by the State Constitution and Statutes.

The Governor is constitutionally and statutorily charged with the responsibility of preserving the fiscal integrity of the State while ensuring program responsibilities are accomplished in the most efficient and cost effective way possible on a day-to-day basis. Removal of all or part of such budget and fiscal discretionary authority would significantly impact the Governor's ability to carry out his responsibilities.

- 2 We agree that the Legislature should expand its own technical capabilities to review and assess State fiscal data, as was intended by the creation of the Joint Legislative Budget Committee and Office of the Legislative Analyst in Act 347, SLH 1990, and codified as Chapter 21F, HRS.

We hope our comments will be of assistance in your evaluation of fiscal powers.

Aloha,

NEAL MIYAHIRA  
Director of Finance