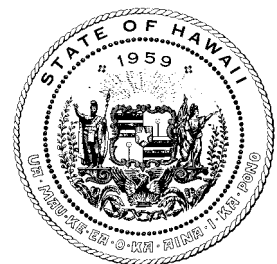


2001 Annual Report

State of Hawaii
Office of the Auditor



Marion M. Higa
State Auditor

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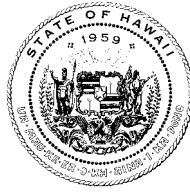
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STATE OF HAWAII
OFFICE OF THE AUDITOR

**MISSION OF THE OFFICE OF
THE AUDITOR**

THROUGH POSTAUDITS OF THE
ACCOUNTS, PROGRAMS, AND PER-
FORMANCE OF STATE AGENCIES,
THE OFFICE SEEKS TO ASSURE
THE ACCOUNTABILITY OF GOV-
ERNMENT AGENCIES FOR THEIR
IMPLEMENTATION OF POLICIES,
MANAGEMENT OF PROGRAMS,
AND EXPENDITURE OF PUBLIC
FUNDS. THE OFFICE REPORTS ITS
FINDINGS AND RECOMMENDA-
TIONS TO THE GOVERNOR AND
THE LEGISLATURE TO GIVE POLI-
CY MAKERS TIMELY, ACCURATE,
AND OBJECTIVE INFORMATION
FOR DECISION MAKING.

The Honorable Members of the Legislature
The Honorable Benjamin J. Cayetano, Governor

March 27, 2002

Ladies and Gentlemen:

This Annual Report highlights the work and activities of the Office of the Auditor in calendar year 2001. The reports we issued and the staff support we provided to special legislative projects this past year covered a wide range of state agencies and addressed many important public issues.

The government agencies serving the citizens of Hawaii are entrusted with billions of dollars in public funds. These monies are generated by the taxes we pay and there is an expectation that these funds will be spent wisely. My office remains firm in its commitment to ensuring that these funds are safeguarded and that the agencies that manage them are accountable. While we lend a critical eye to the agencies we review, we are mindful that we, too, are accountable for the work that we do and I am confident that we have upheld the trust that the public has placed in my office.

As we move into a new year, rest assured that we remain committed to our principles and will continue to execute our audits, studies, and other work with professionalism, objectivity, independence and integrity. The information provided in this annual report is a good illustration of that commitment.

Again, thank you for your support.

Sincerely,

Marion M. Higa
State Auditor

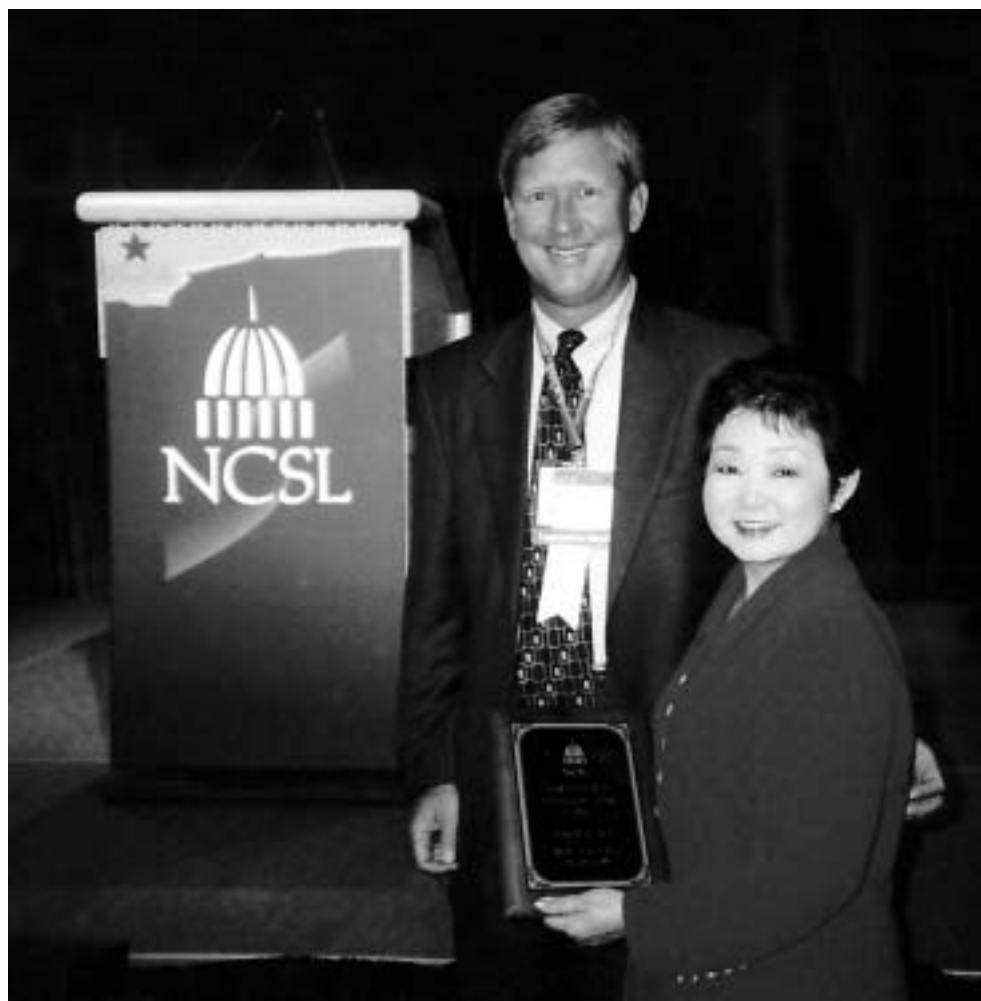
2001 – A Year Filled with Triumphs and Challenges

The year 2001 saw the world change forever. The tragic events of September 11th, the subsequent war in the Middle East, and the impact on the global economy have had far reaching effects. Here in Hawaii, we have experienced the ripple effects of these world events in the form of an alarming decline in visitors to our state, thousands of layoffs, reduced tax revenues and economic recession. Now, perhaps more than ever, the work of our office has taken on a heightened sense of urgency and importance. As the State moves ahead to meet the economic challenges of the coming year, we will no doubt be called upon to continue our efforts to closely examine state government and ensure that government programs are managed with efficiency, accountability and fiscal responsibility.

As in years past, the Legislature has come to rely on our office to provide timely, accurate data on important government programs. This trend continued in 2001. We worked closely with the Joint Senate-House Investigative Committee as it investigated the State's compliance with the *Felix* consent decree. Although we encountered some

resistance in our effort to obtain information regarding how *Felix* funds are being spent, the Legislature is supporting our endeavors and legislation is pending that would enhance our access capabilities. At the Legislature's request, we also conducted a follow-up management audit of the *Felix* consent decree. In an ongoing effort to assist the Department of Education, our office once again determined the appropriate allocation of the department's general funds to charter schools.

The year did not pass without a few challenges. Our office was named in a lawsuit filed by a particular charter school regarding various funding issues. As of the date of publication of



Marion Higa receives the *Staff Achievement Award* at the 2001 NCSL Annual Meeting from incoming ASI Staff Co-Vice Chair, Gary Olsen of Michigan.

this annual report, the lawsuit proceeds. Although we have consistently maintained that our office is not the most appropriate agency to determine the funding allocation, we will continue to follow the letter of the law and the Legislature's assignment of the allocation calculations to us.

In addition to our work with education-related matters, our office also issued several high-profile reports, including audits of the Hawaii Tourism Authority and the Department of Health's Adult Mental Health Division. The serious nature of our findings garnered attention from the Legislature and the public, and generated considerable discussion about these programs.

While the staff of the Office of the Auditor takes personal pride and satisfaction in the work that it does, it is always nice to be recognized for that hard work. In 2001, our office received a Certificate of Recognition of Impact award from the National Legislative Program Evaluation Society (NLPES) for our Actuarial Study and Operational Audit of the Hawaii Public Employees Health Fund, Report No. 99-20. This report, along with others submitted nationwide, were evaluated on such criteria as impact on the public, legislation passed, suggested program improvements, and cost savings as a result of audit recommendations. Our office also received a favorable evaluation from the National State Auditors Association. Our office is "audited" by the national association every three years in a peer review, which evaluates our own policies and procedures, as well as our quality controls. State Auditor Marion Higa was also recognized for her hard work as Staff Co-Vice Chair of the Assembly of State Issues for the past two years and received the Staff Achievement Award. The auditor accepted this prestigious national award at the National Conference of State Legislatures (NCSL) Annual Meeting. And the auditor reports countless instances of strangers and acquaintances alike congratulating the office on the insightful reports we produce.

Staff development remains a high priority in our office and we continue our belief that every audit organization should have a program to

ensure that its staff maintain professional proficiency through continuing education and training. In 2001, we offered a variety of training opportunities to our staff that were taught by both local and national professionals. Courses included updates on government auditing standards, interviewing techniques, non-statistical sampling and internal control evaluation, computer training, and fraud detection and evaluation. We also attended training conferences on the mainland and served as presenters ourselves at some of them. These training courses help ensure that our audit staff is well prepared to conduct the important work that we do.

STAFF OF THE OFFICE OF THE AUDITOR

Marion M. Higa
State Auditor

Leslie I. Tanaka
Deputy Auditor

J. James McMahon
Assistant Auditor

Van Lee
Assistant Auditor

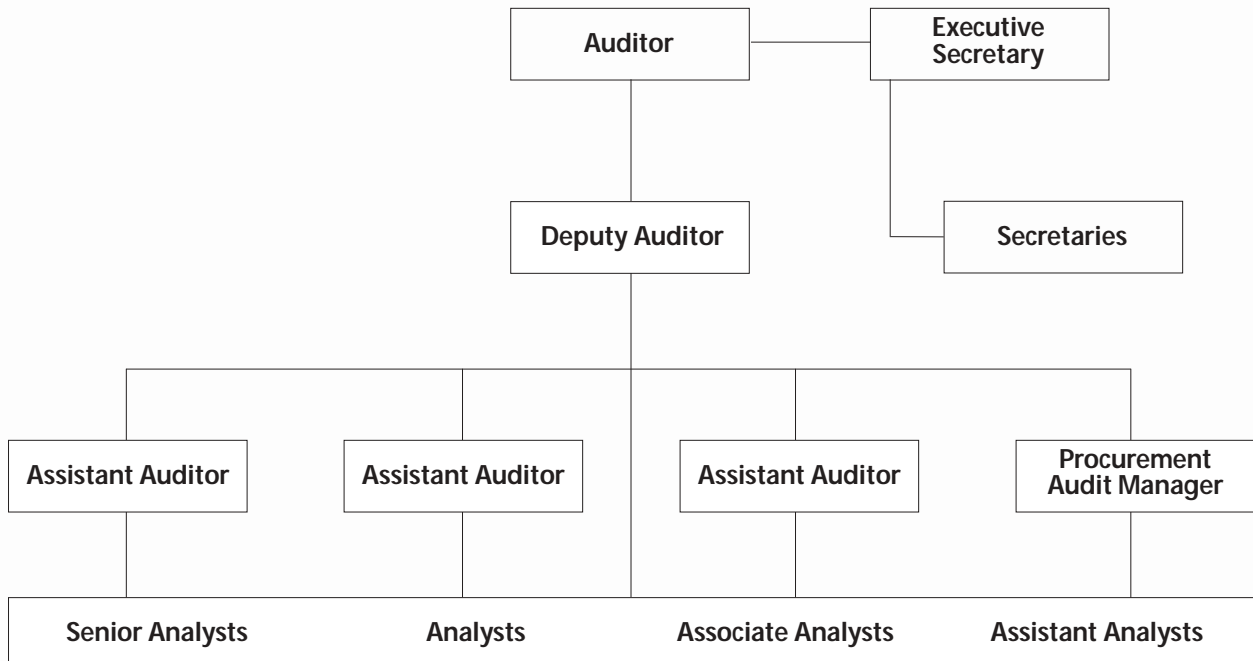
Kerry S. Nagai
Assistant Auditor

Analysts
Urs C. Bauder
Patricia A. Card
Douglas P. Chun

Maria B.J. Chun
Melanie A. Chinen
Lisa K.P. Hankins
Sherry N. Hayashi
Cory B. Hokama
Al Katagihara
Melvia C. Kawashima
Gansin K.S. Li
Cindy S. Mosser
Troy Shimasaki
Tony Smalley
Jade T.L. Takehiro
Janet M. Taylor
Maria C.B. Torres-Kitamura
Joseph W. Trias

Office Services
Evelyn H. Kanja
Debbie M.A. Higa
Pat Mukai

ORGANIZATION OF THE OFFICE OF THE AUDITOR



Themes of 2001 Reports

We have published 17 full reports since our previous annual report. These include 11 performance audits and special studies, 2 financial audits, 1 analysis of a proposed expansion of occupational regulation, 1 sunset evaluation, and 2 follow-up reports. We also produced 69 short reviews of proposed special and revolving funds for the 2001 legislative session. Our work this past year covered a variety of issues that impact our community.

FISCAL ACCOUNTABILITY

Government has the awesome task of providing a variety of services to our citizenry. Funding for these services is derived from taxes paid by hard working men and women throughout our community. As taxpayers, we expect that government will utilize our tax dollars to provide the best possible service in a cost-effective and efficient manner. Much of our work this year involved taking a careful look at how state agencies managed our tax dollars as they strived to fulfill their respective missions.

We conducted financial audits of the Med-QUEST Division of the Department of Human Services and of the Housing and Community Development Corporation of Hawaii. In both audits, we identified deficiencies in the financial accounting and internal control practices of the agencies. One particular shortcoming with the Med-QUEST program included a material weakness, the worst possible type of reportable condition, which could have resulted in a potential loss of \$7 million.

A management audit of the Hawaii Tourism Authority also revealed an alarming array of poor fiscal management of funds. The authority has been entrusted thus far with \$144.5 million in state resources. Yet it has awarded approximately 390 contracts and agreements totaling over \$137 million with inadequate internal controls, exposing the authority to waste and potential fraud.

We are required by statute to determine the share of the Department of Education's general funds to be allocated to new century charter schools. In this, our fourth such allocation, we were given

new statutory directives that resulted in an initial allocation of \$2,997 per pupil for FY 2001-02. During the course of our work, we became aware that four of the six charter schools expended more funds in the prior fiscal year than they were allotted, resulting in a total deficit of over \$261,000.

These reports, along with others that we publish, point out the shortcomings in some of our government programs and make recommendations to improve the way agencies spend tax dollars. Left unchecked, some of the problems we found could result in significant waste of valuable resources and raise the potential for fraud.

SAFEGUARDING OUR NATURAL RESOURCES

We here in Hawaii are blessed with some of the most spectacular natural resources on earth. As residents, we take pride in our lush, fertile lands, pristine beaches, and unique wildlife that attract millions of visitors to our islands each year. Safeguarding these precious natural resources is important to our way of life and two of our reports focused on improving our management of these resources.

We issued a progress report on Act 125, Session Laws of Hawaii 2000, which directed the Auditor to initiate and coordinate all efforts to establish a public land trust information system. The significance of a public land trust information system is reflected in the historical purpose of the public land trust. When Hawaii became a state in 1959, the Admissions Act transferred the bulk of the ceded lands—those lands ceded by the Republic of Hawaii to the United States upon annexation as a territory — to the State of Hawaii to be held in trust for five purposes. However, the Department of Land and Natural Resources lacked a comprehensive inventory of these public lands. An information system would assist the department in developing an accurate inventory and ensure that lands within the public land trust are properly identified and their uses consistent with the law.

Our office issued a progress report on a two-phase

project to develop a public land trust information system. Our consultant on this project completed phase one, which involved identifying relevant issues, tasks, plans and cost projections. Phase two, which is the implementation phase, is on hold pending further legislative direction.

Our office also conducted a management audit of the state boating program within the Department of Land and Natural Resources. The department is tasked with managing and operating small boat harbors and boating facilities throughout the state. Their proper maintenance and operation allow people to engage in recreational boating, commercial and personal fishing, and maritime related business activities.

Despite two previous audits citing poor management of boating facilities, little had changed. We found again that the boating program's mismanagement and neglect have deteriorated facilities to the point where their continued use threatens public safety. Many facilities need major repairs and face permanent closure if not addressed. We recommended that the boating division establish realistic strategic plans to wrestle with both the short and long term problems of the boating program.

Properly identifying our public lands is an essential obligation of state government. Our continued vigilance in moving forward with this monumental yet important task will ensure that public lands are given the care and stewardship necessary for future generations to enjoy. The future of our small boat harbors are also at stake. As an ocean-state, it is puzzling that our boat harbors were allowed to operate under such poor conditions. If the myriad of problems we identified are not addressed, the State risks further deterioration of some of our most prized natural resources and potential economic producers.

CONSUMER PROTECTION

Among our office's many functions is that of complying with the Hawaii Regulatory Licensing Reform Act, Chapter 26H, Hawaii Revised Statutes, that directs the Auditor to analyze proposed legislation to regulate a previously unregulated occupation. The licensing reform act was crafted on the principle that providing regulatory protection for consumers is prudent, but those protections should be justified.

Regulation is an exercise of the State's police powers and should not be taken lightly. The 2000 Legislature directed our office to study the need to regulate the alarm industry and analyze proposed legislation to expand existing regulation. Our review found that expanded statewide regulation of the alarm industry would be difficult to justify and the proposed regulating scheme had many drawbacks. In this instance, we concluded that expanding regulation was not in the best interest of the consumer or the industry.

The licensing reform act also directs the Auditor to evaluate each regulatory board, commission and program prior to the repeal date. The law states that professions and vocations should be regulated only when necessary to protect the health, safety, or welfare of consumers. We evaluated the regulation of marriage and family therapists, which is scheduled for repeal on December 31, 2002. Our study found that regulation of marriage and family therapists is not warranted and we recommended that the law be allowed to sunset.

HELPING THOSE WITH SPECIAL NEEDS

Providing services for those with special needs in our community is an integral function of our government. Citizens living with varying degrees of mental health ailments, both young and old, turn to the State for services that allow them to function and contribute to society. We issued two reports on programs designed to provide mental health services to our community.

One report focused on the Adult Mental Health Division of the Department of Health. The division is responsible for coordinating and administering a comprehensive, integrated mental health system for individuals 18 years of age or older. In our assessment of whether the division adequately planned for the treatment of patients in the least restrictive and most therapeutic environment, we concluded that the division disregarded long-range planning and instead sought "quick fixes" to resolve outstanding federal court orders. We found that millions of dollars were spent on a transition plan without proper evaluation, patient safety was compromised at the state hospital, and internal management controls were lacking. We made several recommendations to improve the program's operations, management and effectiveness.

In our follow-up and management audit of the executive branch's compliance with the *Felix* consent decree, which provides mental health and education services, we focused on the departments' capabilities for accounting, reporting, managing, and forecasting the cost of compliance. We also reviewed management controls intended to monitor compliance with the federal law. We found that the system of care created in response to the *Felix* consent decree has not achieved the expected results. The system of care focused more on procedures than on effective services. Our recommendations covered a variety of areas for improvement, including more detailed reporting and analysis by the departments, implementation of cost accounting and decision support systems, and the submission of interagency consolidated financial reports.

While providing quality mental health services is essential to our community, it is also very costly. Our findings and recommendations will hopefully help our policy makers to maximize resources and improve the delivery of much needed services.

EDUCATION

Recognizing that a quality education involves high standards both in and outside the classroom, we issued two reports that focused on improving our education product. Our *Review and Assessment of the Department of Education's Development of Educational Standards* examined Hawaii's educational standards in light of a national report that gave our state poor marks in educational standards for certain disciplines. We, along with our contracted research organization, found that the content standards are generally coherent and organized, but could be improved. We recommended several changes that may add clarity and comprehensiveness to the standards.

Our management audit of the Department of Education's storeroom demonstrated a continued need to evaluate operations within all state agencies. Established over thirty years ago, the storeroom was designed to purchase educational, office and custodial supplies in bulk and sell them to the public schools at cost plus an 8 percent mark up premium. A 1996 audit of the storeroom revealed suspect practices in unwarranted, excessive ordering that resulted in obsolete inventory and, therefore, unnecessary

costs. In our most recent audit, we found no appreciable improvement. We labeled the storeroom a "dinosaur" because we found that the storeroom increases the schools' workload, wastes taxpayers' money, and is no longer an efficient means to purchase and distribute school supplies. We recommended that the Legislature abolish the storeroom and allow the department the opportunity to procure needed supplies through more advantageous arrangements.

Arguably, education is the most important tool we have to ensure a viable workforce and economic growth opportunities for our state. Providing a top-notch education for our youngsters with limited resources is a challenge that requires balancing innovation and creativity with fiscal prudence and accountability. Our reports strive to strike that delicate balance. Our findings and recommendations address not only fiscal issues, but operational and management issues that, if and when corrected, will go a long way toward our collective goal of operating an education system that is responsive, accountable and able to provide meaningful learning.

Essay: Getting Rid of Dinosaurs

Millions of years ago dinosaurs roamed the earth. These creatures played an integral part in the circle of life on our planet and dominated the landscape for centuries. Dinosaurs were successful in staying atop the food chain because they were able to evolve in an ever-changing world. Adapting to changes in the environment and the evolution of other species were key to their survival. Eventually, however, the dinosaurs were unable to meet the challenges of the harsh world they lived in and were rendered extinct. Other, stronger, more viable species took their place.

Much like the dinosaurs, some government programs, too, have dominated our landscape. At their inception, these programs were the pinnacle of efficiency and met the needs of their constituency. Over the years they evolved and adapted to changes in the environment and sustained viability. However, like the dinosaurs, some government programs, despite their size, longevity and history, simply cease to meet the challenges of their environment and are rendered extinct. Or at least they should be.

One of these government “dinosaurs” was identified in our Management Audit of the Department of Education’s Storeroom, Report No. 02-02. Although the storeroom program is not very big or dominant, it is perhaps indicative of a government that continues to maintain a host of programs that once served the public well, but simply no longer maintain efficiency, reliability or sustainability.

In our report, we noted that the storeroom began operating nearly 30 years ago as the public school system’s central purchasing center. Taking advantage of bulk purchasing, volume discounts and centralized distribution, the storeroom sold educational, office and custodial supplies to the schools at an 8 percent mark up. For years, the storeroom provided supplies to the schools with very little change in its operation. However, change was on the horizon. In 1990, the Legislature amended the storeroom’s funding mechanism from general funds to a revolving fund. This new funding mechanism brought with it the expectation that the storeroom would be self-sufficient. In 1993, the storeroom relocated its central warehouse. A financial audit

conducted in 1996 revealed many problems with the storeroom and recommendations for improvement were made. Our most recent report found that improvements were not made and concluded that the storeroom had become, “...a dinosaur that is no longer needed and should be eliminated.”

Hawai’i is not the only jurisdiction battling its “dinosaurs.” In January 2001, the Joint Legislative Audit and Review Commission (JLARC) of the Virginia General Assembly conducted a study on the distribution of food and housekeeping products from the Virginia Distribution Center (VDC) to state and local government agencies. Created in 1960, the VDC’s mission was to purchase high volume, standardized items for resale to state agencies and localities. It offers more than 900 products, most of which are food related items, janitorial supplies and paper products. The VDC’s primary customers are prisons, mental health and mental retardation facilities, and universities. It is a mandatory source of food and housekeeping products for state agencies and an optional source of supplies for local government agencies. Upon review, the JLARC found that the VDC did not appear to adequately meet the food product requirements of retail-oriented customers such as Virginia’s public four-year universities, which might be better served by a single vendor. Similar findings were made with regard to other products in the VDC inventory. The JLARC also found that over the last five years, the VDC has generated small profits in three years and small losses in two years. Sales have been flat and expenses continued to increase.

In 1999, the JLARC also conducted a review of Virginia’s Statewide Human Services Information and Referral (I&R) Program. This statewide human service information system dates back to 1984 and was designed to collect and maintain accurate and complete human services resource data on a statewide basis, link citizens with appropriate community resources, and provide information to assist decision-makers in allocating financial and other resources. The JLARC review found that the I&R system is not well developed, even though it has been established for a number of years and has been the focus of numerous studies and

recommendations for improvement. JLARC noted that while changes to the current structure would improve performance, the larger policy question is whether the General Assembly wants to continue funding the current system or whether there are alternative arrangements that might be used to more effectively achieve its information and referral objectives.

The State of Florida also sought to eliminate a particular “dinosaur” in its government. In 1996, the Office of Program Policy Analysis and Government Accountability examined the vehicle fleet management activities of state agencies, particularly the Equipment Management Information System (EMIS), to determine how agencies used the system and if it was meeting their needs. Established in 1974, the EMIS maintained data on motor vehicles owned by the State of Florida, including cars, trucks, vans, heavy equipment, and watercraft, which numbered well over 23,000 in 1996. The review found that many agencies were not satisfied with EMIS’s performance or costs. Difficulty of use, untimely reports, and inaccurate data were identified as problem areas. The review also noted that the EMIS system is old and expensive to operate. The annual cost to operate the mainframe system is approximately \$500,000. Comparatively, the State of Texas uses a PC-based program to manage its fleet of 28,000 vehicles with a one-time cost of \$150,000 and annual maintenance cost of \$15,000. The review concluded that the EMIS is approaching obsolescence.

Some states are taking a broader approach in identifying their “dinosaurs.” The State of Illinois, for example, embarked on a statewide performance review with a goal to streamline state government. Since 1999, the governor has implemented bold initiatives that include:

- Eliminating 26 obsolete boards and commissions
- Consolidating 16 state bonding authorities into one state finance authority
- Re-writing the 600-page school code
- Re-writing the State’s 40 year-old criminal code.

The federal government also has a variety of programs that can be classified as potential “dinosaurs.” A political watchdog organization released a “Top 10 Obsolete Government

Programs” list in 1997. It includes programs such as the Natural Resource Conservation Service, which was established in 1935 to help farmers minimize soil erosion. According to the organization, the 12,000-person agency had 2,500 field offices and costs taxpayers \$800 million per year. Yet the U.S. General Accounting Office has found zero difference in soil erosion between areas that participate in the program and those that don’t. If Congress were to cut this program, it would save taxpayers \$3.5 billion over five years. Another example is the Rural Electrification Administration (REA), also created in 1935, which was supposed to help bring electricity to rural areas. In 1949, it expanded to include telephone service. Given the advancement in technology and energy distribution over the last 65 years, this program may no longer be necessary. Five-year savings: \$1.8 billion.

The Office of the Auditor, like our colleagues around the country, has been making a concerted effort to identify “dinosaurs” in government and advocate replacing them with more viable species that can better adapt to our ever-changing world. While it is not our intent to render all government programs “extinct,” it is imperative that we take a hard look at how innovations in technology and shifts in our economic, political and social institutions can send once great programs into obsolescence. The Office of the Auditor remains resolute in its effort to move government forward and, when necessary, drag prehistoric programs out from the tar pits and into the 21st century.

Summary of Reports – 2001 Work Program

PERFORMANCE AUDITS AND STUDIES

- Establishment of a **Public Land Trust Information System**, Phase One (Unnumbered Report)
- Review of **Revolving Funds, Trust Funds, and Trust Accounts** of the Judiciary and the Departments of Commerce and Consumer Affairs, Hawaiian Home Lands, Health, and Human Services, Report No. 01-07
- Audit of the **Employment and Training Fund**, Report No. 01-08
- Audit of the Management of **State Boating Facilities** by the Department of Land and Natural Resources, Report No. 01-09
- Analysis of a Proposal to Expand the Regulation of the **Alarm Industry**, Report No. 01-11
- Audit of the **Adult Mental Health Program**, Report No. 01-13
- A Review and Assessment of the Department of Education's **Development of Educational Standards**, Report No. 01-15
- Management Audit of the Department of Education's **Storeroom**, Report No. 02-02
- New Century **Charter School** Allocation Project - FY2001-02, Report No. 02-03

- Management Audit of the **Hawaii Tourism Authority**, Report No. 02-04
- Review of **Revolving Funds, Trust Funds, and Trust Accounts** of the Office of the Governor, Office of the Lieutenant Governor, Department of Education and Hawaii State Public Library System, and Office of Hawaiian Affairs, Report No. 02-05
- Audit of the **Adult Mental Health Division's** Management of Contracted Community Services, Report No. 02-06

FINANCIAL AUDITS

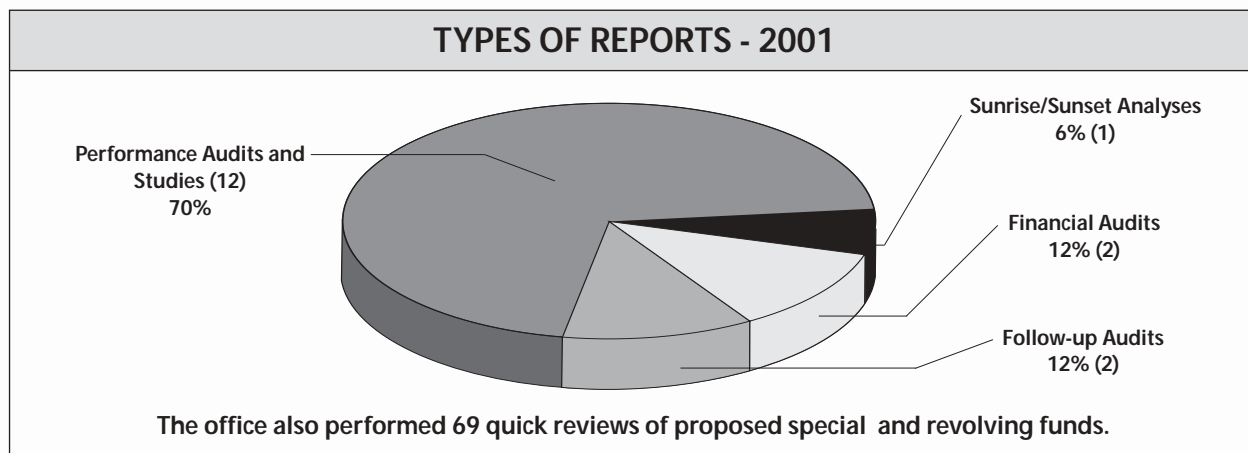
- Financial Audit of the **Med-QUEST Division** of the Department of Human Services, Report No. 01-10
- Financial Audit of the **Housing and Community Development Corporation of Hawaii**, Report No. 01-14

SUNRISE/SUNSET ANALYSES

- Sunset Evaluation Report: **Marriage and Family Therapists**, Report No. 02-01

FOLLOW-UP AUDITS

- Update of the 1992 Summary of **Special and Revolving Funds**, Report No. 01-12
- Follow-up and Management Audit of the **Felix Consent Decree**, Report No. 01-16



Establishment of a Public Land Trust Information System, Phase One, (Unnumbered Report)

This progress report was submitted in response to Act 125, Session Laws of Hawaii (SLH) 2000, which directed the Auditor to initiate and coordinate all efforts to establish a public land trust information system. The project is divided into two phases. In the first phase, relevant issues, tasks, plans, recommended system, and projected costs are identified. The second phase will encompass the actual implementation of the information system. Through a competitive bid process, R. M. Towill Corporation was selected as the consultant to complete the first phase of the project. The consultant concluded that a geographic information system (GIS) is the preferred method to develop an information system and notes that limited capabilities of certain government agencies can impede the implementation of a public land trust information system. The consultant recommends the continued involvement of the State Auditor to facilitate access to information necessary for the completion of the project. The report also identified Phase II objectives, which include the placement and administration of a completed public land trust information system and the review of cost options for program implementation.

Review of Revolving Funds, Trust Funds, and Trust Accounts of the Judiciary and the Departments of Commerce and Consumer Affairs, Hawaiian Home Lands, Health, and Human Services, Report No. 01-07

Section 23-12, HRS, requires the State Auditor to review all existing revolving and trust funds every five years. The review is to include a five-year financial summary, an evaluation of the original intent and purpose of each fund, and the degree to which each fund achieves its stated purpose. Revolving funds are often established with an appropriation of seed money from the general fund. Revolving funds must demonstrate the capacity to be self-sustaining. Trust funds invoke a fiduciary responsibility of state government to care for and use the assets held for the benefit of those with a vested interest in the assets. The revolving funds, trust funds, and trust accounts must continue to

serve the purpose for which they were created and not require continuing general fund appropriations. In addition, revolving funds must exhibit linkage between its benefits and charges and be an appropriate financing mechanism for the program or operation. A trust fund must also provide benefits or services for its intended beneficiaries and meet the statutory definition of a trust fund. Of the 97 funds and accounts we reviewed this year, 26 were revolving funds, 43 were trust funds, and 28 were trust accounts.

Audit of the Employment and Training Fund, Report No. 01-08

The Employment and Training Fund was created to assist employers and incumbent workers through innovative training programs designed to improve the long-term employability of Hawaii's people. We conducted this audit of the fund as directed by the Legislature through Act 197, SLH 2000. Our audit focused primarily on evaluating the Workforce Development Division's administration of the Employment and Training Fund program and on the financing of the fund. We found that the Employment and Training Fund has not demonstrated its effectiveness. The fund has not conducted any meaningful, substantive evaluations of its programs, which hinders an accurate assessment of the worth of the fund and the effectiveness of its programs. The fund's monitoring oversight of its grants is inadequate and the process for awarding macro grants is lengthy. We also found the fund's financing structure has insulated it from legislative scrutiny and oversight. Its status as a special fund and its source of assessment revenues has ensured automatic support for the fund. The fund's revenue sources and expenditures are not clearly linked in all cases. We also examined the fund's assessment moratorium and training fee structure.

Audit of the Management of State Boating Facilities by the Department of Land and Natural Resources, Report No. 01-09

Inadequate management of state boating facilities has been a recurring problem. Prior audits in 1993 and 1998 reported on these

deficiencies. In our present audit, we found that little had changed in the poor conditions of these state boating facilities. The boating program's mismanagement and neglect have deteriorated facilities to the point where their continued use threatens public safety. Many facilities need major repairs and face permanent closure if not addressed. Such problems have resulted partly from poor planning, an insufficient fee structure, paying a disproportionate share of the department's enforcement expenses, and funding programs with special fund moneys that should be supported by general funds. We also found that the boating division lacks adequate controls to ensure the accuracy and integrity of its financial affairs. The boating division is still unable to accurately determine the cost of operating its boating facilities. Finally, in the midst of current boating program problems, consideration is being given to transferring the program to the Department of Transportation. We concluded that administrative deficiencies within the land department needed to be corrected before such a decision is made.

Financial Audit of the Med-QUEST Division of the Department of Human Services, Report No. 01-10

The Office of the Auditor and the certified public accounting firm of KPMG LLP conducted a financial audit of the Med-QUEST Division of the Department of Human Services. The audit examined the financial records and transactions of the division; reviewed the related systems of accounting and internal controls; and tested transactions, systems, and procedures for compliance with laws and regulations. We found deficiencies in the financial accounting and internal control practices of the division. One deficiency included a material weakness, the worst possible type of reportable condition, which could have resulted in a potential loss of over \$7 million. We also found pervasive non-compliance with established policies and procedures and the existence of weak internal controls that could cost the State and Hawaii's taxpayers additional dollars. We also found that the division has not performed certain assessments in accordance with federal regulations and has failed to properly manage its cash resources.

Analysis of a Proposal to Expand the Regulation of the Alarm Industry, Report No. 01-11

The Legislature, through House Concurrent Resolution No. 65, House Draft 1, of the 2000 Regular Session, requested the State Auditor to study the need to regulate the alarm industry and to consider House Bill No. 2125 of 2000, which proposed to expand regulation of the industry under Chapter 436M, Hawaii Revised Statutes. The resolution suggested that the proliferation of false alarms in Honolulu is detrimental to public health, safety, and welfare; is a costly diversion of county resources; and is partly the result of the absence of a licensing or permitting program. We concluded that expanded statewide regulation of the alarm industry would be difficult to justify. Security false alarms have social costs that warrant regulation. However, the harm is uncertain and solutions are limited. The regulatory options have drawbacks. If action is deemed necessary, certain regulatory options are more feasible and enforceable than others. Fire false alarms are a lesser problem requiring little action. We also found that House Bill No. 2125 contained many flaws. Finally, we found that a "grandfather" clause in the existing alarm industry law is unfair.

Audit of the Adult Mental Health Program, Report No. 01-13

The Adult Mental Health Division of the Department of Health is responsible for coordinating and administering a comprehensive integrated mental health system for individuals 18 years of age and older. We assessed whether the division adequately planned for the treatment of patients in the least restrictive and most therapeutic environment, and concluded that the division disregarded long-range planning and instead sought "quick fixes" to resolve outstanding federal court orders stemming from a 1991 settlement agreement that sought to remedy alleged deficiencies in confinement, care, and treatment of patients at the Hawaii State Hospital. Furthermore, the division requested and spent millions of dollars to transition the state hospital to a psychosocial rehabilitation center through expanded community-based services without first formally identifying needs and developing the necessary infrastructure to support those needs. Our review of hospital

operations found that further improvements are needed to ensure that patients are adequately protected from harm and provided with sufficient treatment. We found patient safety was compromised by staff's failure to follow hospital procedures when secluding and restraining patients and that half of the patients in our sample were not meaningfully engaged in the formulation of their treatment goals and preferences. Our review of the hospital operations also indicated that management controls for overtime, leave, and inventories continue to need improvement in order to protect state resources from misuse and waste. Finally, we found that inadequate oversight of sick and vacation leave allow staff to misuse leave.

Financial Audit of the Housing and Community Development Corporation of Hawaii, Report No. 01-14

The Office of the Auditor and the certified public accounting firm of KPMG LLP conducted a financial audit of the Housing and Community Development Corporation of Hawaii for the fiscal year July 1, 1999 to June 30, 2000. The audit examined the financial records and transactions of the corporation; reviewed the related systems of accounting and internal controls; and tested transactions, systems, and procedures for compliance with laws and regulations. We found deficiencies in the financial accounting and internal control practices of the corporation. These deficiencies included the corporation's inadequate planning for the implementation of its new information system that resulted in numerous delays and additional costs to the corporation. The corporation is not timely in its execution of some contracts and has failed to implement internal control procedures in managing its subsidies. Furthermore, we found an unacceptably large number of applicants on the waiting list for low-income housing and tenant rental assistance programs. We also identified an instance where a report was not submitted in a timely manner, which could have resulted in a "freeze" of federal financial assistance. Finally, we found that there is an inadequate segregation of duties over the corporation's petty cash fund.

A Review and Assessment of the Department of Education's Development of Educational Standards, Report No. 01-15

Senate Concurrent Resolution No. 57 of the 2000 legislative session requested the State Auditor to review and assess the Department of Education's (DOE) development of educational standards for public schools statewide to ensure that Hawaii's standards for competency in the basic educational skills are on par with the standards of other states. We contracted with Mid-Continent Research for Education and Learning (McREL) to assess the DOE's content standards for language arts, mathematics, science, and social studies and to compare the department's standards with core subject standards in selected states. McREL assessed each content standard for coherence, clarity, and comprehensiveness. Generally, the DOE's content standards for language arts, mathematics, science, and social studies are coherent and well organized. However, the level of specificity of some benchmarks is inconsistent. Furthermore, in the language arts content standards, two strands (categories of standards) differ in character and scope from the other language arts strands, which make them less effective as content organizers. In general, content standards for language arts, mathematics, science, and social studies cover significant concepts and skills. However, all of the subject areas would benefit from the inclusion of skills and concepts found in highly regarded state and national documents. Overall, the documents reflect an appropriate level of rigor, although issues concerning specificity of language in some of the subject areas make the level of rigor difficult to determine.

Management Audit of the Department of Education's Storeroom, Report No. 02-02

To reduce costs for its 260 - plus public schools, the Department of Education created a central storeroom some 30 years ago to purchase educational, office, and custodial supplies in bulk. The storeroom then sells these supplies to public schools at cost plus an 8 percent markup for delivery charges. In our 1996 *Financial Audit of the Public School System*, Report No. 96-8, we noted that the storeroom's practice of unwarranted, excessive ordering resulted in obsolete inventory costs. In our present audit, we

found no appreciable improvement. Overall, we found that the storeroom increases the schools' workload, wastes taxpayer money, and is no longer an efficient means to purchase and distribute school supplies. The lack of inventory management, an onerous procurement system, slow distribution of educational supplies, high operational costs, antiquated operations, and mismanagement have resulted in the squandering of state resources. These deficiencies underscore our belief that the central storeroom is a dinosaur that is no longer needed and should be eliminated.

Sunset Evaluation Report: Marriage and Family Therapists, Report No. 02-01

We evaluated the regulation of marriage and family therapists under Chapter 451J, HRS, which is scheduled for repeal on December 31, 2002. We concluded that the State should no longer regulate marriage and family therapists; the regulatory law should be allowed to expire as scheduled. However, if regulation is continued, improvements are needed in the law and its administration. Specifically, we found that the regulation of marriage and family therapists is not warranted. There is little evidence of harm in Hawaii. Since the start of the regulatory program in 1998, the Regulated Industries Complaints Office of the Department of Commerce and Consumer Affairs has received only one complaint against a marriage and family therapist. Furthermore, the benefits of regulation are uncertain. Consumer protections would exist even without the regulatory program. "Licensure" fees do not fully support the program, and anticipated cost savings and improved access to care from regulation have not materialized. However, if regulation of marriage and family therapists is continued, the regulatory law needs attention to improve the operations of this program.

New Century Charter School Allocation Project, Report No. 02-03

In this, our fourth year of determining the allocations for charter schools in Hawaii, we determined that the FY2001-02 allocation of general funds to charter schools should be based on a rate of \$2,997 per pupil. This rate reflects

modifications to the allocation methodology necessary to comply with changes mandated by Act 209, SLH 2001, including a provision that the current allocations shall not exceed the department's per pupil expenditures for the previous year. The FY2000-01 allocation was based on a methodology that identified costs as either fixed, variable, and or a transfer of function. Fixed costs are relatively independent of student enrollment while variable costs are directly affected by student enrollment. Transfer of function refers to costs for centralized functions and activities traditionally provided by the department that the department and a charter school have agreed will be assumed by the charter school. Because of new allocation requirements under Act 209, we eliminated the fixed cost element of the previous years because it was based on average position costs rather than a per pupil base. Costs previously used to develop the fixed cost element are now included in the determination of the per pupil calculation. Regarding the role of the Auditor, we continue to note as we have in previous reports that our role in the allocation process should be reviewed. We acknowledge the legislative preference that we determine the allocation but note that this is an executive branch function more properly placed in that branch.

Management Audit of the Hawaii Tourism Authority, Report No. 02-04

We found that the Hawaii Tourism Authority is plagued by an alarming array of management deficiencies. The authority's Board of Directors has the principal responsibility for fulfilling the authority's mission of managing the strategic growth of Hawaii's visitor industry. We found that the board has failed to provide the vision, leadership, and direction necessary to ensure that the authority achieves its primary mission. The authority's strategic planning process was deficient, and measuring the direct impact of the authority's efforts is difficult. We found suspect the history and justification behind the authority's decision to contract with Fishman Enterprises, Inc., to serve as chief executive officer overseeing the staff and operations of the authority for a three-year period. We also found unclear and deficient management and operational leadership. For example, the authority has yet to establish some of the basic

organizational fundamentals and controls; this has led to internal conflict over the role board members should play in the authority's operations. Moreover, we found that the board should have been more careful about ethics laws and public meeting laws. Furthermore, we found that inadequate management of the authority has not ensured the appropriate use of \$144.5 million in state resources. The authority is unable to adequately account for its significant financial and human resources.

Review of Revolving Funds, Trust Funds, and Trust Accounts of the Office of the Governor, Office of the Lieutenant Governor, Department of Education and Hawaii State Public Library System, and the Office of Hawaiian Affairs, Report No. 02-05

Section 23-12, HRS, requires the State Auditor to review all existing revolving and trust funds every five years. This is our second review of the revolving funds, trust funds, and trust accounts of the aforementioned agencies. Of the 35 funds and accounts we reviewed, 7 were revolving funds, 18 were trust funds, and 10 were trust accounts. For each fund or account reviewed, we present a five-year financial summary, the purpose of the fund or account, and conclusions about its use.

Audit of the Adult Mental Health Division's Management of Contracted Community Services, Report No. 02-06

The Department of Health's Adult Mental Health Division provides outpatient and inpatient mental health services to individuals 18 years of age and older. Outpatient services are provided by state operated mental health centers and by a network of community providers. The division's recent focus on preparing patients for community reintegration has resulted in significant funding increases for community-based services. During FY 2000-01, nearly \$48 million was designated for outpatient services. We found the division chief was derelict in her duty to properly manage community-based contract services. A review of 20 percent of the service contracts that were open during FY 1999-2000 or during the first half of FY 2000-01 revealed that millions of dollars were spent without ensuring the maximum purchasing

value of public funds. Contracts were awarded to vendors without assuring that all proposals were fairly evaluated and without following specifications set forth in the request for proposals. We also found that the division fostered a "quid pro quo" environment in which personal gain seemed to precede the State's interest. The division also failed to ensure that the \$20 million it paid community services providers between July 1999 and December 2000 was spent prudently. Poor contract monitoring and follow-up were also identified, as well as the possibility that providers may have cared for patients at unlicensed special treatment facilities.

Update of the 1992 Summary of Special and Revolving Funds, Report No. 01-12

This update examined all special and revolving funds created since July 1, 1990 that are administered by, or are administratively attached to, 18 state agencies. The update also included a review of significant operational changes for those funds reviewed in our prior 1991 and 1992 reports. Special and revolving funds associated with the following agencies were reviewed:

- Department of Accounting and General Services
- Department of Agriculture
- Department of the Attorney General
- Department of Budget and Finance
- Department of Business, Economic Development and Tourism
- Department of Commerce and Consumer Affairs
- Department of Defense
- Department of Education
- Department of Health
- Department of Human Resources Development
- Department of Human Services

- Department of Labor and Industrial Relations
- Department of Land and Natural Resources
- Department of Public Safety
- Department of Taxation
- Department of Transportation
- University of Hawaii
- Judiciary

individual education programs (IEPs) and Department of Health treatment plans are not linked to educational goals.

Follow-Up and Management Audit of the Felix Consent Decree, Report No. 01-16

The Office of the Auditor conducted a follow-up audit of recommendations from several prior audits related to the *Felix* consent decree. This report also responds to a legislative request and concerns about fiscal issues related to the decree, as well as a legislative mandate for assistance with assessments of new mental health programs for students. We assessed selected aspects of the Departments of Health and Education, specifically, their capabilities for accounting, reporting, managing, and forecasting the cost of compliance with *Felix* requirements. We reviewed management controls intended to monitor compliance with the federal law and examined the responsible agencies' efforts to implement previous audit recommendations. We found that the system of care created in response to the *Felix* consent decree has not achieved the expected results. The system of care focused more on procedural compliance than on a system to effectively help children. In addition, the system is largely based on treatments that cannot demonstrate effectiveness. We also found that the Departments of Education and Health do not provide a full picture of the costs of complying with the consent decree. The departments lack an adequate financial management infrastructure to support the *Felix* compliance effort. Costs reported by the departments are intermingled with other programs, are inaccurate, and suffer from a lack of transparency. Finally, we found the system for monitoring service delivery improvements to be inadequate and lacking assessment to ensure that mental health services are appropriate and effective. The Department of Education lacks objective, measurable goals in

Actions Reported on Previous Recommendations

(Report Nos. 00-14 through 01-06)

Report Title: **Fiscal Accountability Audit of the Department of Education: Analysis of Selected School Expenditures**

Report No.: 00-14

RECOMMENDATIONS

The Board of Education should require the Department of Education to provide reports of greater detail similar to those produced by *InSite - The Financial Analysis Model for Education™*.

The Legislature should expand the reporting requirements under Section 302A-1004(b), HRS, to include meaningful comparisons of expenditures. The reporting requirement should include, at a minimum, program expenditures and per pupil cost by location, function, sub-function, and program.

ACTIONS REPORTED

The board reports that the Department of Education (DOE) has decided to use the Hawaii School Expenditure Reporting System (HSERS) which provides financial information in a format similar to the one generated by InSite, but which has other options customized to the department's needs.

HSERS is part of the department's significant progress toward achieving a standards-based educational system with high expectations and increased accountability at all levels. The HSERS reports are located on the DOE website.

Reports include:

- a. Statewide Expenditures by Function and Sub-Function.
- b. Expenditures by School by Function and Sub-Function.
- c. Per Pupil Expenditures by Schools and Function.
- d. Total Expenditures by Educational Level by Function and Sub-Function.
- e. Total Expenditures by Schools and Budget Program Code.
- f. Per Pupil Expenditures by Schools and Budget Program Code.

No legislation was enacted.

RECOMMENDATIONS

The Department of Health should continue to ensure that safe drinking water is distributed to the public through a comprehensive monitoring program. The director of health can improve oversight of public water systems by ensuring that the Safe Drinking Water Branch:

- a. Monitors for all contaminants as required by the Safe Drinking Water Act and carefully reviews all monitoring results;

- b. Evaluates its current chain of custody policies and procedures to determine whether they reflect current practices and revises them as necessary;

- c. Reviews all chain of custody reports to verify that drinking water samples are appropriately documented and, as necessary, provides training in proper chain of custody procedures and documentation;

ACTIONS REPORTED

The branch will continue to assure that all contaminants required by the Safe Drinking Water Act are monitored as required and that all results are carefully reviewed for compliance. While the department itself cannot analyze all regulated contaminants, the branch will strive to assure that sufficient certified laboratories are available for water suppliers to accomplish all required monitoring. At the same time, the branch will do its utmost to assure that the State Laboratories Division has appropriate equipment to perform the many drinking water analyses of which it is capable and support its efforts to increase its capability.

The branch is attempting to convert an approved revolving fund position from a Geologist I to an Environmental Health Specialist V position and establish this position to fulfill quality assurance requirements and address all quality assurance issues.

The proper completion of chain of custody forms has been the subject of articles in the branch newsletter entitled, "Water Spot," for bacteriological samples in March 2001, and chemical samplers in July/August 2001. In addition, bacteriological samplers attending a training held on August 30, 2001 were given a session on the proper completion of chain of custody report forms. Further, specific water systems with custody completion problems were identified, and these systems have been contacted and instructed regarding correct custody procedures and documentation with good results. Meetings have been held with the State Laboratories Division on possible actions to resolve chain of custody completion problems. Incomplete and/or erroneous chain of custody forms and accompanying samples are being rejected as the final resolution for this type of failure.

RECOMMENDATIONS

- d. Completes, at a minimum, sanitary surveys required by the Total Coliform Rule and makes an effort to conduct sanitary surveys of other high-risk systems;

- e. Develops a systematic program for follow-up on sanitary survey recommendations;

- f. Expedites its decision of either adopting an EPA-developed information system or implementing an alternative integrated information system; and

- g. Conducts timely quality assurance of all paper and electronic data, and reprograms existing databases to prevent default entry of extraneous data.

The director of health in cooperation with the Board of Certification of Operating Personnel in Water Treatment Plants should continue to ensure that all water treatment plant operators are appropriately certified.

The department should continue to address violations in a timely manner and ensure that the public remains informed of all safe drinking water violations.

ACTIONS REPORTED

The branch technical staff attended a 4-day training on new sanitary survey requirements conducted by trainers for EPA's Drinking Water Academy in December 2000. The Program is committed to meeting minimum numbers of sanitary surveys called for in current and future regulations.

Rules are being developed that make failure to correct "significant deficiencies" as defined a violation. The branch anticipates holding public hearings on these requirements in May 2002, with final promulgation of these rules projected for December 2002. Procedures for follow-up for correction of deficiencies that do not meet the "significant deficiency" definition have already been implemented by staff.

The 2001 Legislature approved a revolving fund position for a DPSA IV in the branch. This position, once established, will address this issue promptly.

The branch reports that these actions will also be the responsibility of the new DPSA IV position. A verification audit of branch data was conducted by an EPA contractor in May 2001. This audit consisted of the examination of a statistically representative number of randomly selected water system files and data. The audit report is dated September 19, 2001 and was received by the branch on October 25, 2001. In its transmittal letter, EPA stated that no major problems with either data discrepancies or compliance determinations were noted. The report does recommend several areas of improvement. These activities will be reviewed and implemented as appropriate.

The branch reports that this program was recently expanded (through the revision of Chapter 11-25 effective January 2001) to require operators of drinking water distribution systems to receive similar certification. At the present time, there are approximately 140 treatment plant operators and over 280 distribution system operators certified in Hawaii. This program will be maintained.

The branch continues to notify public water systems of violations upon their determination and of the applicable public notification and other requirements as well as potential rectification actions. This practice will be continued.

RECOMMENDATIONS

The department should exercise greater vigilance in bringing significant noncompliers back into compliance by ensuring that the Safe Drinking Water Branch:

- a. Initiates enforcement action in a more timely manner with the assistance of the attorney general's office;
- b. Routinely reminds systems on compliance schedules to submit status reports; and
- c. Exercises its penalty powers on systems that exhibit a lack of commitment to resolving noncompliance.

The department should maximize the use of available resources to protect drinking water supplies by:

- a. Working with public water systems with high priority projects to ensure that they will be ready to apply for assistance;
- b. Continuously evaluating whether the Drinking Water Treatment Revolving Loan Fund program is adequately staffed; and
- c. Developing a long-term integrated expenditure plan for all funds available to the safe drinking water program.

ACTIONS REPORTED

The branch continues to fund an additional deputy attorney general position that has greatly improved our ability to address significant noncompliers.

All systems on compliance schedules receive quarterly letters of violation. The Compliance Section now includes information on the current status of each compliance order in our letters of violation sent each quarter. This information includes penalties received and remaining to be paid as well as due dates for reports and upcoming milestone dates.

The branch reports that it has and will continue to exercise the use of penalty powers against deficient water systems that demonstrate lack of resolve to improve compliance.

The branch has initiated a 2-year, \$100,000 contract to review and assist the five public water systems in greatest need to improve their technical, managerial and financial capacity. One objective of this contract is to assist these systems improve their capability to qualify for DWSRF loans.

The branch reports that this is an ongoing process. The branch has initiated a request to fill the remaining engineering position in this program.

The branch is currently working with the US EPA in the execution of a contract to develop a 10-year resource needs plan. This work was originally scheduled for completion in 2001. However, due to the schedule of the EPA contractor, the Cadmus Group, it appears that this work will begin in January 2002. This contract will involve reviewing current and future staffing and funding level needs, including consideration of existing and future regulations, assessing current and future funding sources, and recommending actions to assure the continued viability of the program.

RECOMMENDATIONS

The Legislature should consider establishing a statutory working definition for special education eligibility

The Departments of Education and Health should adopt a best practices approach for designing and funding programs.

The State of Hawaii should establish a credible and independent capacity to evaluate services and programs provided to the children of Hawaii. Such a capacity should be mandated by legislation.

The Departments of Education and Health should assess the feasibility of providing service vouchers to parents of children in the *Felix* class.

An independent evaluator, such as the Center for Service and Program Evaluation, proposed above, should assess the use of service vouchers, and the service voucher program should be established using a random assignment procedure, so that appropriate evaluations can be carried out.

ACTIONS REPORTED

No legislation was enacted.

The department of education reports that it is aware of and utilizes the principles inherent in established practices for designing and funding educational and human service programs.

Staffing requests for School-based Behavioral Health Services in the *Felix* Response Plan and FY02 budget are based upon national professional staffing guidelines. Adjustments in the FY03 budget requests based on operational realities unique to the State underscore the limitations of adopting a "best practice" identified somewhere else.

No legislation was enacted.

The department notes that while attractive at one level, this approach is not feasible for the following reasons:

- 1) The State is ultimately responsible for the provision of a free and appropriate public education. This includes monitoring the provision of services and guarantees of child and parental rights. Simply put parents cannot waive the State's federal obligations.
- 2) The use of educational vouchers for a selected and protected student population creates an intricate set of dynamics with far reaching public policy ramifications.
- 3) The constitutional issues raised previously have yet to be adequately addressed.

The department commented that while the Center for Service and Program Evaluation suggests a reasonable plan for evaluating any service provision design, the aforementioned problems with the use of service vouchers, not used in the provision of IDEA-required services elsewhere, makes this an academic question as it would be inappropriate to experiment with untried methods for delivering statutorily mandated services and supports to students with disabilities. In addition, it would be unwise to proceed until all legal/constitutional issues related to this matter are resolved.

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RECOMMENDATIONS

The Departments of Education and Health should collaborate with the University of Hawaii to address the personnel needs required to provide adequate and effective services to children in the *Felix Class*.

The Departments of Education and Health must develop mechanisms that will ensure that coordination and cooperation take place at the state and local levels with other entities such as the Hawaii Office of Youth Services, the Department of Human Services and the Judiciary (e.g. Family Court). The same is true at the individual case level.

ACTIONS REPORTED

The department does collaborate with the University of Hawaii and other institutions of higher learning to address personnel needs associated with providing services to children in the *Felix Class*. Collaborative agreements exist with the College of Education and the School of Medicine.

The department works with the College of Education through 1) supplying incentives for mentors and cooperative teachers providing necessary field experience to university students, 2) funding coursework for students enrolled at UH who are committed to working as Special Education teachers for three years in the DOE, 3) funding prerequisite coursework, and 4) supporting UH in creating an additional Cohort in Bachelor's in Education Dual Preparation Program.

The department also has a memorandum of agreement with UH School of Medicine to support training of speech pathologists.

The department develops joint operating procedures with the Department of Health (DOH) to ensure coordination and cooperation between the departments at all levels. The DOE and DOH hold weekly operational planning meetings to address policy, operational procedures, and training. Department of Human Services personnel representing the multi-agency case coordinators also attend this meeting.

At a broader level the departments participate in the monthly Multi-Agency Children's Committee meetings that address all services to children, *Felix* and non-*Felix*.

Most recently the department is a full participant in the DOH-led initiative to attend the Third Annual Policy Academy. This is an opportunity to coordinate children's mental health policy across the broad array of child serving agencies such as the Hawaii Office of Youth Services, the Department of Human Services and the Judiciary (e.g. Family Court).

RECOMMENDATIONS

The Legislature should consider establishing a statutory working definition for special education eligibility.

The Departments of Education and Health should adopt a best practices approach for designing and funding programs.

The State of Hawaii should establish a credible and independent capacity to evaluate services and programs provided to children in Hawaii. Such a capacity should be mandated by legislation.

The Departments of Education and Health should assess the feasibility of providing service vouchers to parents of children in the *Felix* class.

An independent evaluator, such as the Center for Service and Program Evaluation, proposed above, should assess the use of service vouchers, and the service voucher program should be established using a random assignment procedure, so that appropriate evaluations can be carried out.

The Departments of Education and Health should collaborate with the University of Hawaii to address the personnel needs required to provide adequate and effective services to children in the *Felix* class.

ACTIONS REPORTED

No legislation was enacted.

The department of health agrees with this recommendation. For the past one and a half to two years, the Child and Adolescent Mental Health Division (CAMHD) has focused on making sure that the services provided are making a difference in the lives of children and families. The department, in collaboration with professionals from the University of Hawaii, continues the development of "best practices" based on evaluated outcomes. CAMHD recently produced practice guidelines in collaboration with the Department of Education.

No legislation was enacted.

The department reports that consultants do not provide specific information to adequately evaluate this recommendation. However, the department is not averse to considering such an evaluation if the Legislature were to provide the funds. The department indicated that it would not support moving forward with a voucher system without first conducting a thorough evaluation.

The department is not averse to the idea, but would require the Legislature to provide additional funds for the evaluation process.

The department reports that it is collaborating with the John A. Burns School of Medicine (JABSOM), and the Schools of Psychology and Social Work. The department and the University of Hawaii collaborate on the academic and clinical training of psychiatry residents, psychology interns, and graduate level social work students. The department and JABSOM ensure adequate and effective clinical direction of all psychiatric and medical services provided to

RECOMMENDATIONS

The Departments of Education and Health must develop mechanisms that will ensure that coordination and cooperation take place at the state and local levels with other entities such as the Hawaii Office of Youth Services, the Department of Human Services and the Judiciary (e.g. Family Court). The same is true at the individual case level.

ACTIONS REPORTED

Felix class youth through the joint appointment of qualified psychiatrists at the department's Family Guidance Centers.

The department noted that the collaboration between the department and the university is unique in that the schools provide multi-disciplinary services and diverse training programs. For example, the School of Psychology and the department are also collaborating on a program aimed at the dissemination of cognitive behavioral therapy for youth diagnosed with anxiety and depression disorders.

The department agrees with consultants that agency coordination and collaboration is critical. All child-serving agencies are asked to participate in the child-specific coordinated service planning meetings and the State has made significant improvements in multi-agency participation. CAMHD participates in the Multi-Agency Children's Council (MACC). All child-servicing agencies are involved and policy issues are addressed.

Report Title: **Allocation to New Century Charter Schools Project – FY2000-01**
 Report No.: 01-01

RECOMMENDATIONS

No recommendations.

ACTIONS REPORTED

Report Title: **Sunset Evaluation of Barbering and Beauty Culture**
 Report No.: 01-02

RECOMMENDATIONS

Chapters 438 and 439, HRS, should be repealed.

ACTIONS REPORTED

Legislation was not enacted to repeal Chapters 438 and 439, HRS.

Report Title: **Audit of the Workers' Compensation Payment Process in State Agencies**
 Report No.: 01-03 (Department of Human Resources Development response)

RECOMMENDATIONS

To ensure the timely payment of benefits to injured state employees we recommend that workers' compensation managers in the

ACTIONS REPORTED

RECOMMENDATIONS

Department of Human Resources Development, Department of Education, University of Hawaii, Judiciary, and other state agencies:

- a. Ensure that reports of industrial injury (WC-1) are submitted within the seven working day timeframe;

- b. Improve efforts to conduct claim investigations in a more timely manner and comply with the 30-day requirement for filing denial reports. Requests for extensions should be properly obtained prior to the end of the 30-day requirement;

- c. Ensure that payments for disabilities are made in a timely manner and in accordance with Section 386-31, HRS;

- d. Improve efforts to submit WC-3 reports in a more timely manner and in accordance with Section 386-95, HRS; and

- e. Ensure that final reports for claims are filed within 30 days after final payments for compensation have been made.

We recommend that state workers' compensation managers in the Department of Human Resources Development, Department of Education, University of Hawaii, Judiciary, and other state agencies improve efforts to pay benefits accurately and on time by:

ACTIONS REPORTED

The department of human resources development's State Workers Compensation Division (SWCD) reports that its chief met with the personnel officers of all departments, except DOE and Judiciary to explain the findings of the audit. The SWCD stressed the DLIR requirement to submit claims on the WC-1 in a timely manner and emphasized that pursuant to chapter 386-95, HRS, there is a penalty for failing to comply.

The department reports that the SWCD division managers met with professional staff to develop a system that automatically generates a request for extension if an investigation will take more than 30 days to complete. If a denial is appropriate and based upon a legal issue, a denial letter will be generated immediately. This milestone objective will be measured through the SWCD employee performance appraisal system.

The department's SWCD division chief met with departmental personnel officers to inform them that they must expedite the process of reconciling an employee's leave credits during a disability from work.

The department's SWCD established a policy to stop the collection of financial data for the current calendar year on November 30, 2001. This new internal deadline will permit the department to complete the required WC-3's by December 31st. This milestone performance goal will a part of the SWCD employee's performance measurement.

The department reports that in order to insure compliance with the filing deadlines, SWCD claims managers will have this performance objective included in the performance appraisal system.

RECOMMENDATIONS

- a. Tracking and monitoring open claims and ensuring that payments are processed in a timely manner. This should include any follow-up with departmental payroll offices to verify that disability payments have been processed;
- b. Ensuring the accuracy of disability compensation calculations by documenting the calculation of the claimant's average weekly wage through the use of the WC-14 report; and
- c. Improving the review of medical bills to ensure that payments do not exceed allowable amounts and that the payments are warranted and are adequately supported.

ACTIONS REPORTED

The department's SWCD developed an improved tracking report to include all relevant data and deadlines. To increase the awareness of this finding in SWCD, support staff are being cross-trained to make timely payment of invoices. The department's SWCD will monitor payments with departmental payroll offices to verify timely payments if disability worksheets are not received by SWCD after benefits have been approved.

The department notes that during the briefing of the departmental personnel officers, SWCD distributed blank forms (WC-14) and reviewed the completion of the form. SWCD agreed to accept a different format if it was already being used and met the requirements of §386-51, HRS.

The director pursued contracting an internal auditor with DAGS audit division without success. While the department awaits further information on the financial outlook for FY02 and beyond, SWCD is conducting an on-going process of review at its monthly staff meetings.

Report Title: **Audit of the Workers' Compensation Payment Process in State Agencies**

Report No.: 01-03 (Department of Education Response)

RECOMMENDATIONS

To ensure the timely payment of benefits to injured state employees we recommend that workers' compensation managers in the Department of Human Resources Development, Department of Education, University of Hawaii, Judiciary, and other state agencies:

- a. Ensure that reports of industrial injury (WC-1) are submitted within the seven working day timeframe;

ACTIONS REPORTED

The department of education reports that the instructional packet for all workers' compensation forms was revised on August 1, 2001. Representatives of the department's Workers' Compensation Section conducted annual training for the Hawaii State Public Library System, department schools, district and state officials. Emphasis focused on accurate completion and timely submission of the Employer's Report of Industrial Injury (WC-1).

On a monthly basis, a report of delinquent WC-1 reports is compiled and forwarded for dissemination to administrators responsible for ensuring the completion of the WC-1.

RECOMMENDATIONS

- b. Improve efforts to conduct claim investigations in a more timely manner and comply with the 30-day requirement for filing denial reports. Requests for extensions should be properly obtained prior to the end of the 30-day requirement;

- c. Ensure that payments for disabilities are made in a timely manner and in accordance with Section 386-31, HRS;

ACTIONS REPORTED

The Workers' Compensation office continues to contact all delinquent schools and sites when the department's workers compensation office receives medical reports and invoices for which the record shows no WC-1.

The department explained that existing procedural instructions are reviewed and updated to attain procedures that are consistent and practical, whenever time and resources permit. A formal procedures manual is still a goal to achieving consistent and efficient operations.

Electronic claims reporting is pending availability of computer manpower and resources.

The department advised that a report of denied claims is compiled on a monthly basis. The supervisor is provided a copy and inquires with the claims manager as to the status of the claim. The conference yields improved claims management through the exchange of ideas between supervisor and claims manager and consequently leads to more timely resolution of denied claims. Requests for extension are more timely. The Department of Labor and Industrial Relations, Disability Compensation Division (DLIR/DCD) was contacted to determine how the department was complying with obtaining extensions where needed. The DLIR/DCD reported no known delinquencies.

The department reports that existing procedures are reviewed with the goal toward developing a formal procedures manual. The department's workers compensation section and payroll section have met to discuss methods for improvement.

The department's workers' compensation section was invited to review the time and attendance program project scheduled for implementation in 2002. Suggestions were presented for implementation and are expected to improve accuracy and timeliness of disability payments.

The department's payroll staff strives to make payments in a timely manner. However, the limitations imposed by having payments issued only twice a month due to the semi-monthly payroll system may delay some payments.

RECOMMENDATIONS

- d. Improve efforts to submit WC-3 reports in a more timely manner and in accordance with Section 386-95, HRS; and
- e. Ensure that final reports for claims are filed within 30 days after final payments for compensation have been made.

We recommend that state workers' compensation managers in the Department of Human Resources Development, Department of Education, University of Hawaii, Judiciary, and other state agencies improve efforts to pay benefits accurately and on time by:

- a. Tracking and monitoring open claims and ensuring that payments are processed in a timely manner. This should include any follow-up with departmental payroll offices to verify that disability payments have been processed;
- b. Ensuring the accuracy of disability compensation calculations by documenting the calculation of the claimant's average weekly wage through the use of the WC-14 report; and
- c. Improving the review of medical bills to ensure that payments do not exceed allowable amounts and that the payments are warranted and are adequately supported.

ACTIONS REPORTED

The department noted that it remains steadfast in its support of an amendment to section 386-95, HRS, to allow WC-3 reports to be filed by January 31 of the following year.

The department reports that the purchase of enhanced equipment has been completed and is awaiting installation. The improved technology will enable the workers' compensation section to upgrade its risk management program and improve the process to move claims quickly and accurately to claim closure.

The payroll section has been working on a procedure to improve timely benefit reconciliation to facilitate timely claims closure.

The department reports that beginning December 2001, the DOE Payroll Section will begin tracking the date disability payment authorization is received and the date payment is made. Microsoft Access database software will be used to manage the tracking system.

The department reports that since September 2001, the payroll section affixes a calculator tape to the Form WC-14 documenting how the average weekly wage was computed.

The department's workers compensation section contracts a 100% FTE in-house bill auditor. The auditor employs the CR Links program to perform bill audits. The CR Links program is reviewed and updated by the program owner.

Report Title: **Audit of the Workers' Compensation Payment Process in State Agencies**
 Report No.: 01-03 (The University of Hawaii Response)

RECOMMENDATIONS

To ensure the timely payment of benefits to injured state employees we recommend that workers' compensation managers in the Department of Human Resources Development, Department of Education, University of Hawaii, Judiciary, and other state agencies:

ACTIONS REPORTED

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RECOMMENDATIONS

- a. Ensure that reports of industrial injury (WC-1) are submitted within the seven working day timeframe;

- b. Improve efforts to conduct claim investigations in a more timely manner and comply with the 30-day requirement for filing denial reports. Requests for extensions should be properly obtained prior to the end of the 30-day requirement;

- c. Ensure that payments for disabilities are made in a timely manner and in accordance with Section 386-31, HRS;

- d. Improve efforts to submit WC-3 reports in a more timely manner and in accordance with Section 386-95, HRS; and

- e. Ensure that final reports for claims are filed within 30 days after final payments for compensation have been made.

We recommend that state workers' compensation managers in the Department of Human Resources Development, Department of Education, University of Hawaii, Judiciary, and other state agencies improve efforts to pay benefits accurately and on time by:

ACTIONS REPORTED

The University of Hawaii is continuing to train its supervisors and managers on the importance of timely action. While the university provides an internal reporting form for its employees and supervisors, it is for convenience purposes to capture pertinent data. Employees and supervisors are encouraged to report all work related injuries and illnesses in any manner – telephonic, e-mail, written report, face to face, etc. – to the responsible agent as soon as possible to permit the timely reporting to the Department of Labor and Industrial Relations (DLIR).

The university reports that a third-party administrator contracted by the university has conducted its investigations in a timely manner. All requests for extensions beyond the required 30-day timeframe have been submitted to DLIR in a timely manner. All investigations of claims initially denied pending investigation are completed within the authorized extended timeframes.

The university reports that unlike other State agencies, the university, with few exceptions, effects payment of wage replacement benefits outside the state payroll system to avoid the delays inherent in early payroll deadlines. However, there are still instances wherein the wage replacement benefits are made beyond the required ten days. In these cases, the claimant suffers no loss of wages inasmuch as regular salary or wages continue to be paid.

The university notes that because this is the first year of services provided by a third-party administrator to the university, there is no established record of timely or late submissions of WC-3 reports relative to University claimants. However, the third-party administrator reports that it submits all WC-3 reports by the deadline specified by DLIR.

The university reports that its contracted third-party administrator files final reports within ten days of the final payment of all benefits.

RECOMMENDATIONS

- a. Tracking and monitoring open claims and ensuring that payments are processed in a timely manner. This should include any follow-up with departmental payroll offices to verify that disability payments have been processed;

- b. Ensuring the accuracy of disability compensation calculations by documenting the calculation of the claimant's average weekly wage through the use of the WC-14 report; and

- c. Improving the review of medical bills to ensure that payments do not exceed allowable amounts and that the payments are warranted and are adequately supported.

ACTIONS REPORTED

The university reports that its third-party administrator makes all payments on behalf of the university, inclusive of wage replacement, medical treatments, vocational rehabilitation, rating examinations, etc. Because wage replacement benefits are not tied to state payroll deadlines, these benefits are more timely paid. The third-party administrator and the university conduct quarterly open claims reviews to ensure progress of the case and appropriate benefit payments, as well as to report on the status of open claims.

The university reports that it utilizes its own form, which is more user friendly, to expedite information and to prevent misreporting of information. This form captures the same data as that of the WC-14. The third-party administrator utilizes this data to ensure accuracy of disability compensation calculations. In an internal audit of such calculations, it has been determined that the third party administrator has been accurate in its calculations.

The university reports that its third-party administrator monitors, audits and adjusts medical bills to ensure that payments do not exceed the allowable amounts and that the services for which payment is requested are authorized. The university conducts a post-audit of reported payments.

Report Title: **Audit of the Workers' Compensation Payment Process in State Agencies**
 Report No.: 01-03 (Judiciary Response)

RECOMMENDATIONS

To ensure the timely payment of benefits to injured state employees we recommend that workers' compensation managers in the Department of Human Resources Development, Department of Education, University of Hawaii, Judiciary, and other state agencies:

- a. Ensure that reports of industrial injury (WC-1) are submitted within the seven working day timeframe;

ACTIONS REPORTED

The Judiciary reports that it has amended its personnel manual to improve timeliness and ensure that WC-1 reports are submitted within the required seven working day timeframe.

RECOMMENDATIONS

- b. Improve efforts to conduct claim investigations in a more timely manner and comply with the 30-day requirement for filing denial reports. Requests for extensions should be properly obtained prior to the end of the 30-day requirement;
- c. Ensure that payments for disabilities are made in a timely manner and in accordance with Section 386-31, HRS;
- d. Improve efforts to submit WC-3 reports in a more timely manner and in accordance with Section 386-95, HRS; and
- e. Ensure that final reports for claims are filed within 30 days after final payments for compensation have been made.

We recommend that state workers' compensation managers in the Department of Human Resources Development, Department of Education, University of Hawaii, Judiciary, and other state agencies improve efforts to pay benefits accurately and on time by:

- a. Tracking and monitoring open claims and ensuring that payments are processed in a timely manner. This should include any follow-up with departmental payroll offices to verify that disability payments have been processed;
- b. Ensuring the accuracy of disability compensation calculations by documenting the calculation of the claimant's average weekly wage through the use of the WC-14 report; and
- c. Improving the review of medical bills to ensure that payments do not exceed allowable amounts and that the payments are warranted and are adequately supported.

ACTIONS REPORTED

The Judiciary continues to make every effort to investigate claims and conclude the investigations as quickly as possible so as to meet the 30-day requirement for filing denial reports. The need to file any requests for extension is now monitored more closely to ensure that such requests are submitted prior to the end of the 30-day requirement.

The Judiciary continues to process disability payments as soon as possible within the constraints of the state's semi-monthly payroll system. There have been no complaints about any late payments.

The Judiciary notes that the Department of Labor and Industrial Relations (DLIR) has recognized the need to amend HRS 386-95 to change the due date from December 31 to January 31. The Judiciary is in compliance with the DLIR memo which establishes the January 31 due date.

The Judiciary reports that once it has determined that any payment was "final," the applicable cases have all been closed with the 30 days and will continue to be so.

The Judiciary reports that it has developed an internal procedure, which, along with continued contact with the payroll office, helps to ensure the timely processing of disability payment.

The Judiciary has procedures in place to ensure the accuracy of its workers' compensation calculations. This includes a double-check of the average weekly wage, one by payroll and one by the workers' compensation branch.

The Judiciary has obtained proposals from two vendors and is now in the process of selecting one to audit all medical bills on a trial basis for an eight-month period. At the conclusion of the trial period, the Judiciary will analyze the results and determine whether it should continue to outsource the auditing function of all medical bills.

RECOMMENDATIONS

The Department of Labor and Industrial Relations should address delays in processing workers' compensation payments by:

- a. Reducing the amount of time it takes to schedule hearings including time limits for medical evaluations. It should also ensure that once a hearing is conducted, decisions are issued in a timely manner and in accordance with Section 386-86, HRS;

- b. Seeking an amendment to Section 386-95, HRS, to require WC-3 annual reports to be filed by January 31 of the next year after the calendar year has ended; and

- c. Establishing a system to identify violations of Chapter 386, HRS, and monitor and assess related penalties to ensure compliance with the law.

ACTIONS REPORTED

The department is reviewing its procedures to include prioritizing hearings according to issues (compensability, medical treatment denial, termination of temporary total disability, etc.) so that certain types of hearings can be heard in less than three months after request. The department considers the minimum time required to conduct a hearing to be three months after a request is received. Requests for medical evaluations are being processed pursuant to section 12-10-75, Workers' Compensation Administrative Rules.

The department has implemented a computer program to track individual hearings officers/hearings/decision due.

The department reports that as recommended by the auditor, an amendment to section 386-95, HRS, is being proposed during the next legislative session to adjust the filing date from December 31 to January 31, which is a more reasonable requirement.

The department reports that it currently uses a delinquent employer run to identify delinquent employers. Investigators pursue delinquent employers to bring them into compliance. Penalties are assessed if the employer fails to obtain insurance coverage.

Penalties for untimely or underpaid benefits (section 386-92) are assessed based upon complaint investigations, audit of annual cost reports submitted by carriers and audit of insurance carriers and adjustors.

The department also notes that section 386-95 requires employers/carriers to report payments to claimants annually. Requiring more frequent reports would require DCIS program modifications and additional department staffing. The department currently processes approximately 60,000 WC-3 cost reports annually. The volume of work would increase exponentially based upon frequency of reports. Additional funding would be required to modify the computer system and add staff. The

RECOMMENDATIONS

ACTIONS REPORTED

department recommends an alternative that would incorporate an initial payment feature into the new Lotus Notes data warehouse environment upon receipt of funding to move the cost reporting function into this new environment. The department predicts that this process would minimize additional staffing requirements since it will be done electronically. The department advised that a report to identify untimely reporting of injuries is being developed in the new Lotus Notes system.

The department notes that complaints against health care providers are adjudicated upon receipt of complaints pursuant to Section 386-27, HRS.

The department reports that penalties from fraud are assessed after filing of a complaint and conduct of a hearing to consider arguments of parties in the complaint pursuant to section 386-98, HRS. Penalties are logged by the Enforcement Branch and transmitted to the Fiscal Office upon collection.

Report Title: A Review and Identification of Fiscally Related Powers Conferred Upon or Assumed by the Executive Branch

Report No.: 01-04

RECOMMENDATIONS

No recommendations.

ACTIONS REPORTED

Report Title: Audit of the Department of Human Services' Information System

Report No.: 01-05

RECOMMENDATIONS

The director of human services should ensure that a departmental *Distributed Information Processing and Information Resource Management* (DIPIRM) plan that reflects the department's overall automation plan is completed and that projects are consistent with the DIPIRM.

ACTIONS REPORTED

The department reports that the source documents that are required to complete the DIPIRM are in the process of being updated by the divisions and staff offices of the department. These documents referred to as Project Valuation Assessments (PVAs) are created by the organization requesting or requiring information technology needs. Once the PVAs are received by the office of information technology, they will be consolidated and submitted to the Department of Accounting and General Services (DAGS), Information and Communication Services Division (ICSD) for review and retention.

RECOMMENDATIONS

The Department of Human Services should ensure its Information Technology Steering Committee is in accord with the State's System Development Methodology. The committee should be chaired by the deputy director and be comprised of administrators from each division. The Information Systems Office administrator should be a non-voting member and provide advisory assistance.

The department should redesign the social services computer system to better meet user needs and incorporate necessary interfaces. In redesigning the system, the department should consider pursuing federal SACWIS funding.

ACTIONS REPORTED

The department reports that its ITSC was established in 2000. Since August 2001, the ITSC has met at least monthly. Committee members are comprised of administrators from each division, staff office, and Office of Youth Services. The committee is chaired by the department's deputy director.

The department has pursued funding requests in the biennium and supplemental budgets. However, the department notes that the Legislature has not appropriated additional general funds to pursue redesigning or replacing the Child Protective Services System (CPSS). The department is currently looking into improving interfaces and the more efficient methodology of integration as measures to improve data integrity and consistency between the various federal and state programs administered by the department.

Report Title: **Audit of the Office of Hawaiian Affairs**
Report No.: 01-06

RECOMMENDATIONS

The Board of Trustees should direct its immediate attention towards identifying OHA's role in improving the condition of all Hawaiians. Specifically, the trustees should:

Identify and prioritize goals and objectives for the Office of Hawaiian Affairs. These goals and objectives should be developed within the context of a comprehensive master plan that clearly identifies OHA's role in relation to other agencies providing services to Hawaiians; (1.1)

Update OHA's master and functional plans and ensure that these plans account for increased revenues that should be used to expand services to Hawaiians, while at the same time preserving the corpus for future generations. The trustees should also coordinate these key planning documents with OHA's spending and investment plans; and (1.2)

ACTIONS REPORTED

1.1 The board reports that the office of Hawaiian affairs (OHA) has embarked on a multiyear plan to respond to these recommendations. The board began with the implementation of a strategic planning process in February 2001. An OHA vision statement, mission and trustee priorities were developed in the first phase. These were shared at 15 community meetings statewide. The office is currently in Phase IV of V. The completed strategic plan document was scheduled for Dec. 31, 2001.

1.2 The board reports that it adopted 10 strategic plan goals in January 2002. The strategic plan is one of several preparations for the update of the OHA Master Plan. The development of a Native Hawaiian Well-Being Paradigm began in 2000. This provides the basis for determining what the conditions are for Hawaiians that need improvement. Several native Hawaiian research projects are being prepared for the master plan revisit.

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RECOMMENDATIONS

ACTIONS REPORTED

The board reports that the strategic plan will also focus on determining the indicators needed to measure or compare effectiveness of OHA programs. Long-term tracking of these indicators will be needed for the results-based methodology that will be employed.

The board notes that §10-6, HRS, calls for the development “of a comprehensive master plan for native Hawaiians and Hawaiians.” The Native Hawaiian Comprehensive Master Plan (NHCMP) is a combined effort of all public and private agencies and organizations that advocate for, provide services to, and assist Hawaiians in any way. In the last two years a number of the Hawaiian agencies have renewed their strategic and/or master plans. The current progress of the NHCMP work group is in three areas:

1. The compilation and analysis of programs available to Hawaiians.
2. The establishment of an Intranet between service providers requires a commitment by all parties. Collaboration and sharing of data, financial and human resources and other information to improve services to the beneficiaries is key to this phase. An external website for the general public on program availability will be a product of this collaboration.
3. A plan to assure efficient ancestry verification is being developed as a result of the Department of Health’s new procedure for vital statistic documents. Hawaiians are required to show proof of ancestry in order to receive certain benefits. The inaccessibility and cost of these documents led to an interagency collaboration.

The board reports that this is also a link to the identification of OHA beneficiaries. OHA’s role in this process has been one of facilitation and documentation. The success of these three initiatives will determine the schedule for the completion of a Native Hawaiian Comprehensive Master Plan.

RECOMMENDATIONS

Prepare a budget that reflects the board's priorities as established in OHA's master plan, and limits expenditures to budgeted programs and services. Cash reserves set aside in money market accounts should be limited to quarterly budgets and emergency appropriations. An appropriation that would cause OHA to exceed its expenditure ceiling should be justified and reported to the Legislature within 20 days prior to the commencement of each legislative session. (1.3)

The board should fulfill its fiduciary duties and improve its management of OHA's investments by:

Complying with policies regarding the use of expense, protocol, and petty cash funds. The fiscal staff should audit these records and refer all incidents of gross misuse to the attorney general for further review; (2.1)

ACTIONS REPORTED

1.3 The board reports that the OHA budgetary process has recently undergone a series of major changes with the adoption of a total operating budget approach, the development of a spending policy, and the incorporation of spending policy restrictions upon the FY02 and FY03 total operating budget. The next phase being developed by staff for consideration by administration and the board is the adoption of a Performance & Program Budgeting Process (PPBP).

PPBP promotes efficiency and effectiveness because it defines and links the results of expenditures with the amounts appropriated by the board for a given purpose through the budget for that year. The PPBP requires the establishment of program priorities (linked directly with the results of OHA's strategic planning efforts and ultimately OHA's master plan).

Regarding cash reserves held in OHA's money market account, OHA's existing cash management policies already prevent OHA from holding more than an estimated quarterly amount within OHA's Operating Budget Money Market account. This cash management practice was adopted with the creation of the money market account and serves to address the concerns of the auditor.

The board reports that in regards to the issue of OHA exceeding its expenditure ceiling, OHA's spending policy would require significant external and internal due diligence in order to justify breaching the expenditure ceiling. If OHA did exceed its spending policy, this fact would be readily apparent and could easily be reported to the Legislature as a part of its legislative briefing and submitted in the December preceding the start of the Legislature in January of the following year.

2.1 The board reports that on March 30, 2001, the committee on policy and planning entertained an action item recommending the approval of a system wherein funds would be disbursed on an actual expenditure reimbursable basis in lieu of the existing method of prepayment.

RECOMMENDATIONS

Disbursing trustee expense funds on a cash reimbursable basis; (2.2)

Ensuring compliance with OHA's investment policy; (2.3)

ACTIONS REPORTED

The measure failed to pass out of committee. The committee did not feel that a reimbursement procedure was feasible given the amount of the trustees' salaries and the delays that occur between expending funding and having reimbursements processed.

The board notes that on July 13, 2001 the committee on Policy and Planning was presented with an action item that recommended elimination of the requirement that trustees file quarterly expenditure reports with the chairperson. Reports would continue to be filed with the administrator and the chief financial officer.

The measure passed out of committee on July 13, 2001.

The Board of Trustees approved the measure on Aug. 2, 2001.

The Board of Trustees approved a second reading of the measure on Aug. 30, 2001.

2.2 The board reports that OHA's administration is currently seeking alternative disbursement solutions for trustee expense funds (e.g., trustee allowances) after efforts to introduce a cash reimbursable policy failed at the committee on policy and planning level. Interim measures taken by administration entail requiring trustees to certify that their expenses are in accordance with the intent to develop and maintain an ongoing communication network with beneficiaries, promote an understanding of Hawaiian issues, and encourage participation in resolution of these issues. This certification shall be required for the December 2001 quarterly report.

2.3 The board notes that an overview of OHA's current treasury business cycle addresses this issue. As allowed by the Hawai'i Revised Statutes, section 10-5, OHA's trustees are authorized to invest funds derived from any source including monies from the public land trust.

Included within this review is an overall policy benchmark index (*composed of 40% S&P500, 15% Russell 2000, and 10% MSEA-FE-Net, 35% LB Int Govt/Credit Bonds*) matched with the performance of OHA's Native Hawaiian Trust Fund (entire fund).

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RECOMMENDATIONS

Carefully considering the recommendations of OHA's investment consultants and documenting in public record the reason for choosing not to implement any of these recommendations; (2.4)

Adopting quarterly benchmarks for each money manager and requiring OHA's investment consultants to compare each manager's quarterly performance to these benchmarks in order to improve the timeliness in identifying under-performing managers. Similarly, the board should require that OHA's investment consultants annually report the data needed to identify whether each money manager complied with market cycle performance measures; (2.5)

Terminating under-performing money managers in a timely manner; and (2.6)

Immediately contracting for bank custodian services for OHA's investments. (2.7)

ACTIONS REPORTED

The board reports that on a monthly basis, First Hawaiian Bank (FHB) sends a statement to each investment manager detailing the current month's transactions. The investment manager then reconciles the statement to his/her records. FHB does not reconcile its records to the broker's records. In addition, FHB sends statements to the investment consultant and OHA.

2.4 The board reports that in an effort to facilitate investment decisions, OHA hired Salomon Smith Barney, Inc. (SSB), as a consultant for investment related matters. The budget and finance committee meets with an SSB representative on a quarterly basis (public record) and is presented with the results of the quarter for the various investment portfolios for each of the investment managers.

As requested, SSB fields questions and offers advice to the committee. In addition, SSB also presents significant changes to the board at the board meeting. The board then acts accordingly based on this advice. Currently, OHA invests the public land trust funds in various marketable equity and debt securities.

2.5 The board notes that the budget and finance committee meets with an SSB representative on a quarterly basis (public record) and is presented with the results of the quarter for the various investment portfolios for each of the investment managers.

In addition, a detailed comparative analysis of OHA's equity managers, small cap growth, international equity, and fixed income along with their respective benchmarks are provided.

2.6 The board reports that the investment managers must comply with the mix of investments per the Investment Policy, which was amended by the board on August 1, 2000. For FY02, Salomon Smith Barney presented its July-September 2001 quarterly report to the budget and finance committee on October 12, 2001.

2.7 OHA contract no. 1542 with FHB for custodial services is in effect as of March 31, 2001.

RECOMMENDATIONS

The board should clarify its bylaws to require the board chair to place all items on the board agenda within a reasonable number of days once a committee recommendation is received. (3.1)

OHA should improve the management of its grants program by:

Improving its oversight of grant awards. Grant monitors should verify whether the grantees meet performance measures prior to disbursing quarterly payments to the grantees; (4.1)

Developing policies and procedures for awarding subsidies and purchase of services in accordance with board priorities. The practice of using the grant program to fund these services should be discontinued immediately and necessary health care services should be identified and procured in accordance with the competitive purchase of service process established in Chapter 103F; and (4.2)

ACTIONS REPORTED

3.1 The board responded that on Feb. 22, 2001, an action item was presented to the committee on policy and planning, which recommended an amendment to the OHA bylaws. This amendment would mandate that the chairperson of the OHA board place any committee recommendation on a board agenda no later than thirty (30) calendar days after receipt of the recommendation.

The Board approved the measure on March 15, 2001.

The Board approved the bylaw amendment on second reading on April 19, 2001.

4.1 The board reports that OHA program monitors review progress reports and gather data as necessary to ensure that the activities of the contractor/grantee meet the agreed scope of services as specified in the contract agreement. Upon reviewing reports and data, the monitors focus on the scope of activities/services written in the contract. Procedures now in place ensure the scope of activities/services is clear and measurable along the timeline stated in the contract. Measurement of activities will provide an overview on how the program is running and if it is meeting its target.

The board also notes that monitors now identify whether the contractor/grantee has fulfilled the scope of activities/services in the contract agreement and draft a report of their findings to the administrator. Furthermore, OHA tracks all grants in a database to certify uniformity.

4.2 The board reports that OHA's grants program has developed policies and procedures establishing priority areas on which the board shall base its funding decisions. Currently, this policy is under review by the committee on policy and planning, and will be moved to board upon approval.

RECOMMENDATIONS

Ensuring that services are provided and tax clearances received from grant recipients prior to disbursing any grant funds. (4.3)

OHA should reduce the financial losses incurred by the Native Hawaiian Revolving Loan Fund (NHRLF) by:

Completing loan applicant credit reviews and analyzing each applicant's market and financial plan prior to OHA's approval of loan requests, (5.1)

ACTIONS REPORTED

On July 5, 2001, the board approved a request for a legal opinion from the Attorney General on the laws applicable to OHA's grants and subsidies program. The Attorney General issued an opinion dated September 25, 2001, stating that OHA does not appear to have the authority to make grants pursuant to existing standards provided by law.

As such, the board notes that OHA's grants program has been halted until this issue can be resolved and/or proper accommodations are made relative to the procurement law. OHA's legislative and government affairs (LAGA) committee will be discussing various legislative amendments to the state procurement statutes to address the Attorney General's opinion.

OHA is currently considering utilizing grant monies allocated by the board to fund community organizations in compliance with the State's procurement process. The board's attorney is currently reviewing this matter.

4.3 The board reports that to address concerns regarding tax clearance submittals, all grant recipients are required to submit a tax clearance form prior to disbursement of grant funds, and upon closure of the grant agreement. OHA will not fund any contract without first receiving a tax clearance.

5.1 The board reports that a credit report review is the initial step in the application process and is done by the assigned loan officer, for every applicant coming into the NHRLF program. An internal file review process has been implemented. This current file review process ensures that the credit report is included in each new loan file. A business plan (which includes market and financial plans) is also required for each loan being processed through the NHRLF program. The loan officer analyzes the business plan and utilizes this information to prepare a loan write-up for presentation to the NHRLF Board for consideration of loan approval. This file review process currently in effect, ensures that the approved loan write-up and business plan are included in each new loan file.

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RECOMMENDATIONS

Disbursing loan funds only after receiving all required loan-closing documents; (5.2)

Developing clear guidelines for determining when collateral is a loan condition. Furthermore, OHA should take possession of secured collateral when accounts are past 90 days due and other collection efforts have been unsuccessful; (5.3)

Improving collection efforts by notifying borrowers in writing of outstanding monthly payments and consequences of failure to pay. Late fees should be assessed as authorized by the Native Hawaiian and Revolving Loan Fund Operation Manual; (5.4)

ACTIONS REPORTED

5.2 The board reports that an internal review process has been implemented wherein the manager or designee will review the file or verify with the loan officer to ensure that any conditions for disbursement placed upon the loan have been met prior to transmittal of the check to the loan officer for disbursement. The current procedure calls for the loan officer to schedule a loan-closing meeting with the borrower at which time required loan-closing documents are signed and a bank account is established into which loan funds are deposited. To monitor that the funds are being used as intended, the loan officer's signature is required for the borrower to draw from the account. After the documents are signed, the manager or designee reviews the file for completeness.

5.3 The board notes that the Federal Register indicates that "collateral is not required by statute for each loan made, but the loan administrator may require collateral if he deems it necessary to secure the loan". Loan officers are required to work closely with their delinquent borrowers. When all efforts are exhausted on their level, the loan is sent to OHA's credit and collections specialist for further collection efforts. The decision by the credit and collections specialist to repossess collateral occurs on a case-by-case basis. Efforts are made to avoid closing a business, which would extinguish any chance of repayment. A report documenting the decision to take or not to take, legal action or repossess collateral for seriously delinquent loans is included in the loan file.

5.4 The board reports that the software module to generate monthly late notices has been installed and set up in the new loan servicing application. Monthly late notices have been sent out on time since March 2001. Based on prior experience and the unique portfolio of loans, NHRLF feels that 30 days is too soon to send a letter regarding collection procedures and are proposing a revision to the policies that will make this notification requirement more feasible at 60 days. The revised operations manual that updates these policies and procedures was approved by the NHRLF board of directors and was approved by the board on Oct. 10, 2001. The manual now awaits formal approval by the Administration for Native Americans (ANA).

RECOMMENDATIONS

Promptly notifying the Administration for Native Americans (ANA) of all loans 90 days in arrears. Notification to the ANA should include OHA's recommendations for further action as required by Title 45, Section 1336.68 of the Code of Federal Regulations; and (5.5)

Ensuring that monthly delinquency loan reports are accurate. (5.6)

The board should adopt clear policies and procedures for effecting organizational change that require careful planning prior to actual implementation of any change. These policies should require the following:

An assessment of the current organization's strengths and weaknesses. The purpose of a reorganization being considered by the board or administrator should be clearly documented and available for public review; (6.1)

A detailed timeframe for implementation; (6.2)

A revised organization chart (to be reviewed and approved by the board) that identifies all position titles and position numbers; and (6.3)

ACTIONS REPORTED

The board also advised that the NHRLF has analyzed the feasibility of implementing the imposition of late fees on past due accounts. The board explained that the problem in the past was that although the assessment of late fees was authorized in the operations manual, the loan-closing documents did not contain the language to enforce it. Therefore, in January 2000 the loan-closing documents were revised to include the language for subsequently closed loans. The NHRLF has begun implementation of late fees, effective October 2001.

5.5 The board reported that delinquency reports identifying all loans in arrears and the status of the collection efforts have resumed as part of the quarterly reporting to ANA effective with March 2001. The original federal regulations called for ANA to be advised on all actions to be taken on accounts over 90 days delinquent. This proved to be a hindrance to collection efforts as valuable time was lost waiting for an ANA response.

5.6 The board noted that the delinquency reports are reviewed and discussed by NHRLF staff and reported to the Advisory Board of Directors monthly. The loan servicing software installed in early 2000 has been helpful in providing the data needed to prepare these reports accurately.

6.1 The board reported that an administrator's directive on organizational change was formulated to provide internal flexibility and efficiency in effecting functional and structural changes to the organization. The directive also established relevant guidelines that recognize the unique nature and changing needs of the agency, as described in Hawai'i Revised Statutes, Chapter 10. As these procedures guide the internal process of effecting organizational change, this directive was developed with respect to the auditor's concerns over the agency's ability to effectively manage its programs and human resources.

6.2 See Paragraph 6.1.

6.3 The board reported that OHA human resources staff is compiling all formally approved position titles and numbers for publication.

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RECOMMENDATIONS

Accurate position descriptions and qualification statements for each position prepared by OHA's personnel office. (6.4)

The administrator should immediately develop an employee grievance process for board review and approval. Once adopted, copies of the policy should be distributed to all employees. (7.1)

ACTIONS REPORTED

6.4 The board reported that OHA administration has directed all departments to examine their mission and functional duties. Division managers have been tasked with providing accurate position titles that represent all staff at OHA. As of Oct 1, 2001, this process has yielded a clear portrayal of position titles and numbers, eventually all approved by OHA's current administrator.

7.1 The board reported that a written grievance procedure or similar process will raise the expectation of both the managers and staff that a potential new right or privilege is being created. Hawaii Revised Statutes states that officers and employees of OHA may be hired without regard to Chapters 76 and 77, and shall serve at the pleasure of the administrator.

The principal policy that provides a process of investigation and recommendation is OHA's policy against sexual and other forms of harassment.

The principal recommendation made in lieu of a grievance procedure or complaint process was that managers should be trained in the "at-will" employment condition, rights accorded to employees by federal and state statutes, effective investigation and documentation methods and practices, applicable internal policies and procedures, and other management practices.

An additional recommendation is that the staff be educated on their "at-will" employment condition, their rights under federal and state statutes, applicable internal policies and procedures, chain of command, and other related guidelines.

The board noted that a training module for managers and staff respectively covering the areas noted above is being developed for implementation. This training module will also discuss the "chain of command" concept in addressing concerns, which employees may have regarding their employment with OHA.

The board reported that the administrator will meet with staff to emphasize the nature of the "at-will" condition of employment.

**OFFICE OF THE AUDITOR
 APPROPRIATIONS AND EXPENDITURES ON A BUDGETARY BASIS
 FOR THE FISCAL YEAR ENDED JUNE 30, 2001**

APPROPRIATIONS

Act 1, SLH 2000 (operations)	\$ 2,019,850
Act 138, SLH 1999 (operations - salary adjustments)	52,593
Act 1, SLH 2000 (special studies)	150,000
Act 125, SLH 2000 (public land trust study)	250,000
Act 180, SLH 2000 (additional studies)	125,000
Act 1, SLH 2001 (<i>Felix</i> related work)	500,000
	<u>\$ 3,097,443</u>

EXPENDITURES

Staff salaries	\$ 1,369,843
Contractual services	349,995
Other expenses	174,130
Special studies	624,036
Excess of appropriations over expenditures	\$ 2,518,004
	<u>\$ 579,439</u>

EXCESS OF APPROPRIATIONS OVER EXPENDITURES

Act 1, SLH 2000 (operations)	\$ 178,475
Act 138, SLH 1999 (operations- salary adjustments)	0
Act 1, SLH 2000 (special studies)	115,038
Act 125, SLH 2000 (public land trust study)	159,883
Act 180, SLH 2000 (additional studies)	0
Act 1, SLH 2001 (<i>Felix</i> related work)	126,043
	<u>\$ 579,439</u>

The Office of the Auditor

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.

To carry out its mission, 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 operational 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 the schedule and 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 reports* include studies and audits relating to the State's procurement of goods, services, and construction.
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.

THE AUDITOR

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