STAND. COM. REP. NO. 987

Honolulu, Hawaii

March 13, 2009

RE: H.B. No. 200
H.D. 1

Honorable Calvin K.Y. Say
Speaker, House of Representatives
Twenty-Fifth State Legislature
Regular Session of 2009
State of Hawaii

Sir:

Your Committee on Finance, to which was referred H.B. No. 200 entitled:

"A BILL FOR AN ACT RELATING TO THE STATE BUDGET,"

begs leave to report as follows:

Introduction

The challenges currently facing Hawaii and this nation are unprecedented. When the 25th Legislature convened on Opening Day, our state faced a daunting $1,800,000,000 revenue shortfall over a three-year period. It quickly became apparent that this extraordinary challenge had no easy solution. Experts believe that both the local and national economies will remain in a downturn for a significant period. Indeed, economists agree that this downward trend shows no signs of slowing and may well persist long enough to affect budget decisions next session.

In crafting this Executive Biennium Budget, your Committee recognizes that the solution to our current problem must involve more than cutting programs and personnel. We must also take a hard look at the basic functions of government. After all, the needs and priorities of our communities have changed. The solution to our current problem must therefore be both systemic and sustainable. In short, this unprecedented challenge is an opportunity to re-evaluate the purposes and goals of certain functions of government so that fundamental change can occur to better meet the needs of our people. However, your Committee recognizes that discussions on making fundamental change will require more time, as the Administration apparently followed a narrow approach in crafting the budget it submitted to the Legislature. Nevertheless, your Committee has taken the initial steps to encourage the Administration to examine innovative ways to deliver and revamp 20th century programs and services in a 21st century world.

This Budget, therefore:

- Addresses the critical revenue shortfall by making difficult but necessary cuts to programs and personnel; and

- Requires the re-evaluation of the purposes and goals of certain functions of government.

Economic Outlook

In January 2009, the National Conference of State Legislatures (NCSL) released its *Update on State Budget Gaps: FY 2009 & FY 2010*. It states that the total budget gap for all states is $84,300,000,000. Thirty-four states project FY 2009-2010 gaps. Twenty-four of these states forecast gaps exceeding their general fund budgets by double-digits, with Hawaii, at 18 percent, forecasting the seventh largest gap.

Statistics released by the Department of Labor and Industrial Relations (DLIR) show that the jobless rate in Hawaii currently stands at 6.1 percent, the highest level for the state since April 1983. In January 2008, there were approximately 19,750 people unemployed. The unemployed population stood at 39,550 in January 2009, representing a 100 percent increase in the span of twelve months.

A March 12, 2009 article in the *Honolulu Star-Bulletin* reported that, "Hawaii climbed three notches to the No. 27 spot nationally in February" for foreclosures statewide. In February 2008, there were a total of 143 foreclosure actions taken. That number had risen to 537 by February 2009, an increase of 275 percent, according to data presented in the article.

In 2008 alone, the Bureau of Labor Statistics reported 88 mass layoffs in Hawaii including:

Company	Number of laid-off workers	Date of lay off
Weyerhaeuser	85	March 2008
Aloha Airlines	1,900	March 2008
Aloha Airlines Cargo Operations	300	March 2008
Molokai Properties Limited (Molokai Ranch)	120	March 2008
ATA Airlines	35	April 2008
Hawaii Medical Center	89	June 2008
Hawaii Health System Corporation (Kona Community Hospital)	54	July 2008
Maui Land & Pineapple	274	July 2008
Sea Life Park	44	August 2008
The Honolulu Advertiser	81	August 2008
Palama Meat Company	38	August 2008
Servco Pacific Incorporated	118	November 2008
Maui Land & Pineapple	98	February 2009
The Honolulu Star-Bulletin	17	March 2009

Budget Overview

The current bleak economic landscape requires that your Committee take several unpopular steps toward balancing the budget. This draft of the budget represents a general fund reduction in the Governor's budget equal to $235,819,465 for FY 2009-2010 and $170,532,170 for FY 2010-2011.

Part of this reduction results from layoffs. This draft of the budget eliminates 374 filled positions. Your Committee takes neither pride nor joy in recommending these lay-offs, but feels that it is prudent, responsible, and necessary to begin discussion in this direction. Indeed, any layoffs will occur only after all options and alternatives have been duly examined and considered.

In selecting positions to be eliminated, your Committee worked to, whenever possible:

- Avoid impact to front-line personnel delivering services and benefits to the general public;
- Cut excessive management and administrative layers (i.e. middle management); and
- Eliminate exempt positions not performing core government functions (e.g. public relations, special assistants, etc.).

In addition to these lay-offs, your Committee deleted funding for:

- Career Kokua in DLIR;
- The Disability and Communication Access Board in the Department of Health (DOH); and
- The State Health Planning and Development Agency (SHPDA) in DOH.

Your Committee found it particularly difficult to make reductions in human services, health, and education as reflected in this budget. But while these are essential services and affect our neediest, they also represent the largest portion of the State's budget. Certainly, it must be understood and emphasized that any layoffs will be the last option for consideration.

Department and Agency Highlights

Department of Human Services

Your Committee is quite concerned and alarmed by wasteful contracts currently administered by the Department of Human Services (DHS). The following two, in particular, stand out as examples of potentially egregious waste and questionable business practices:

- Benton and Associates has a $3,200,000 contract to integrate services and maximize federal revenue use within DHS. The scope of services indicates that Benton & Associates will "Develop and Implement an Integrated Human Services System." The contract was awarded in 2006 and has been renewed yearly, with annual contract increases. However, DHS staff can or should perform these services, particularly given that this staff is more knowledgeable about federal laws and department operations than hired outside consultants. The consultants' results also appear less than satisfactory.

- NorthStar, LLC, appears to have been engaging in suspect if not questionable business practices by receiving Temporary Assistance for Needy Families (TANF) funds to provide services with which they have no experience, a requirement for TANF-related contracts for services. NorthStar was initially contracted in 2006 to train and develop First-To-Work clients to ultimately become mortgage bankers. To date, none of their clients have advanced to that level, despite the fact that NorthStar has been paid $18,000 per First-To-Work client for this training. Moreover, this is only one of several questionable contracts between NorthStar and DHS.

Additionally, there are concerns that TANF-funded contracts are not serving TANF clients. Your Committee is alarmed that DHS retains these contracts at the expense of cutting other benefits and services to the poor and needy such as reducing general assistance payments, eliminating breast and cervical cancer treatment services, and reducing the number of social workers and eligibility workers, front-line staff who are delivering essential services to the public.

Your Committee is also concerned with the current state of the Office of Youth Services (OYS) and the Hawaii Youth

Correctional Facility (HYCF). In February 2006, HYCF entered into a Memorandum of Agreement (MOA) with the United States Department of Justice to improve conditions at the facility. This MOA outlined 53 areas of compliance for HYCF. Currently, HYCF is in full compliance in only 17 areas and has asked for a one year extension.

OYS and HYCF leadership has also been reluctant to provide information regarding purchase of service (POS) contracts. As all state contracts are public record, their reluctance to provide this information is troubling. Additionally, your Committee is concerned about the lack of recidivism studies for clients of OYS and HYCF as the last such study was done almost four years ago. These studies are imperative to any objective and meaningful evaluation into the effectiveness of programs and services.

Department of Health

Your Committee recognizes the hard work of DOH, which ensures that the State of Hawaii remains a healthy place to live and work while dealing with the harsh realities of an increasingly complex health care system.

Your Committee does not believe the reorganization plan proposed by DOH and the Governor will create either the necessary level of cost savings or increased efficiencies and, therefore, does not concur with the Governor's proposed reorganization plan. However, reconsideration of this decision may be warranted upon submission of compelling detailed analysis.

Likewise, while the reorganization plan acknowledges the critical statewide necessity of reliable and timely access to emergency medical services, your Committee believes that these medical services can be delivered in a more cost-efficient manner.

Finally, your Committee recognizes duplication of positions and management inefficiencies within DOH and has addressed these by reducing DOH general fund expenditures by $39,536,974 per year for each year of the biennium. This reduction of approximately four percent of the DOH's annual operating budget appears warranted as nearly one-third of DOH personnel do not provide direct services to the public. The reductions will be implemented by:

- Vacancy savings. Your Committee has eliminated 240.5 non-critical positions that have been vacant for one year or more, resulting in annual savings of $9,094,938;

- Excess filled positions. Your Committee has eliminated 298 filled positions found to be redundant management and administrative positions within DOH, resulting in annual savings of $13,208,372;

- Purchase-of-service contract rationalization. Your Committee finds that DOH can provide health services through POS contracts more efficiently by consolidating contracts with fewer providers, negotiating additional volume discounts for services, and replacing POS contracts with services provided by state employees. These policies will achieve annual savings of $15,481,775; and

- Other expenditures. Your Committee has scaled back miscellaneous expenditures within DOH, resulting in annual savings of $1,751,889.

Hawaii Health Systems Corporation

Your Committee remains concerned about the financial and operational management of the state hospital system. Accordingly, your Committee has:

- Separated programs and budgets for each of the five regions of the Hawaii Health Systems Corporation(HHSC) (Kauai, Oahu, Maui, West Hawaii, and East Hawaii); and

- Replaced the current senior management team of HHSC with a Deputy Director of Health. This Deputy Director, among other duties, will assess the condition of the hospital system and recommend improvements to its financial and operational capabilities.

Department of Education

Understanding the importance of public education under these difficult fiscal conditions, your Committee took great care to maintain funding at the school level for the Department of Education (DOE), and restricted reductions for School-Based

Budgeting to categorical programs, to avoid any reductions in funds for the Weighted Student Formula.

While reductions for the DOE in its entirety total over $31,000,000 in each of the fiscal years of the upcoming biennium, reductions for categorical programs amount to less than $4,000,000 of those amounts. Your Committee does not believe that these reductions will negatively affect the core mission of Hawaii's public schools.

Your Committee notes that these reductions are in addition to the Board of Education (Board), DOE, and the Governor's own reductions, some of which may ultimately eliminate 149 filled positions within the DOE. Restoration of these cuts was not requested by the Board or DOE, so your Committee accepted their decision and preference.

The Board took the responsible initiative to authorize reductions to the DOE, and your Committee applauds the Board's efforts to include input from the DOE budget office and school communities. However, your Committee does not support the Board's decision to use funds intended for school restructuring under the No Child Left Behind Act to restore cuts to unrelated programs. Even with all of the restructuring funds intact, the funding level would not be adequate for the number of schools that need restructuring, and your Committee fears a reduction in these funds will further hinder DOE's efforts to achieve progress toward its educational goals. The Board must be more conscientious when deciding to move funds from one area to another.

Your Committee is concerned by both recent audits of DOE's procurement procedures (*Procurement Audit of the Department of Education: Part 1 and Part 2,* Report Nos. 09-03 and 09-04, February 2009 by the Hawaii State Auditor). Disregard of the potential for financial mismanagement is never acceptable, and the current economic situation makes it intolerable. Credit should be given to the Superintendent for acknowledging current shortcomings and embarking upon addressing the weaknesses disclosed in the Audit. Your Committee will continue to monitor the progress of the DOE and work with the DOE to resolve these issues and adopt procurement best practices.

Given the State's current fiscal constraints, your Committee finds it troubling that charter schools continue to push for dramatic increases in funding, apparently believing themselves to be exempt from the financial hardships other state departments are forced to endure. Your Committee notes that charter schools were one of only two areas of state government that did not face any reductions in their budgets last year. Additionally, in their budget submittal for the upcoming biennium, charter schools ignored a directive from the Governor that all departments submit reduction scenarios and that no department was to request an increase in operating expenses. Rather, the charter schools proceeded to request additional amounts of $14 million for FY 2009-2010 and over $22 million for FY 2010-2011. Your Committee has denied those requests for additional funding based on the understanding that, during times of financial crisis, the burden of sacrifice must be shared by all.

University of Hawaii

The University of Hawaii System (UH System) plays a critical role in laying the foundation for the future of our State. Education is a powerful tool for all individuals to improve their situations and those of their families and their communities. Thus, continued support of the UH System will increase the growth and prosperity of the State.

Perhaps as a direct result of these difficult economic times, the UH System is experiencing record highs in enrollment. The largest increase is at the community college level, where enrollment has swelled by 9.4 percent. Across the entire UH System, enrollment has risen 5.6 percent. This enrollment surge, coupled with built-in annual tuition increases, should result in an influx of funds into the Tuition and Fees Special Fund. These increases will allow the UH system to offset a $35,000,000 reduction in general funds for each fiscal year. The ability of the UH System to absorb this amount of general fund savings has allowed it to become one of the leaders during these tough economic times.

Your Committee also recognizes the importance of educational programs that allow more of Hawaii's youth to remain in the islands to pursue their career goals. The College of Pharmacy at the University of Hawaii at Hilo is the only one of its kind in the state. Between 900 and 1,200 students apply for admission to that college each year, although only 90 are admitted per class. The College of Pharmacy is currently in the final stages of obtaining full accreditation. To support this effort for full accreditation for the college, your Committee has appropriated funding for fourteen positions and $2,083,136 in special funds for

FY2010, and funding for an additional sixteen positions and $2,187,609 in special funds for FY2011.

Department of Business, Economic Development, and Tourism

In an attempt to promote Hawaii's efforts to increase energy independence and alternative-energy programs, your Committee has provided DBEDT ample means and support over the years to formulate a strategic plan with key measurements. Despite this financial support, however, DBEDT has been unable to provide a clear plan with specific performance measures and goals. Therefore, the approval of any further funding for the Clean Energy Initiative as currently proposed would be irresponsible.

Furthermore, this prolonged ineffectiveness and lack of mission have prompted your Committee to reorganize DBEDT to ensure that specific current programs can continue to flourish under new direction more in line with its core goals and functions.

Your Committee made the following program transfers out of DBEDT:

- The Hawaii Housing Finance and Development Corporation back to DHS;

- The Small Business Regulatory Review Board, Research and Economic Analysis Division, and the High Technology Development Corporation to the Department of Commerce and Consumer Affairs (DCCA);

- The Foreign Trade Zone and Aloha Tower Development Corporation to the Department of Transportation's (DOT) Harbor Division;

- The Hawaii Community Development Authority and the Land Use Commission to the Department of Land and Natural Resources (DLNR); and

- The Creative Industries Division and the Hawaii Film Studio to the State Foundation on Culture and the Arts.

Department of Public Safety

Your Committee recognizes the importance of maintaining public safety and the difficulties currently facing the corrections industry. Over 2,000 of Hawaii's inmates remain incarcerated in mainland prisons at a total cost of $66,256,512 per year. Over the past few years, the Department of Public Safety (PSD) achieved a savings of $7,655,524 by using excess funds to purchase additional contracted bed space. Your Committee has identified this excess as a one-time savings for the general fund.

Your Committee was unwilling to remove funds from local prison systems beyond the reductions proposed by the Governor. However, excess administrative positions not located in individual prison systems were evaluated. In total, your Committee realized an additional reduction of eleven positions and $1,408,399 for FY 2009-2010 and $2,102,988 for FY 2010-2011.

Department of Land and Natural Resources

Your Committee understands the importance of conservation and the protection of Hawaii's unique natural resources. However, our current unfavorable fiscal conditions prevent many of the cuts proposed by the Governor from being restored. Specifically, funding for DLNR's Division of Conservation and Resources Enforcement, after being expanded by Legislative appropriation last year, must now be reduced by $1,325,801.

The Governor also reduced funding for the Parks Administration and Operation Program by $1,176,696, eliminating lifeguard services at Keawa'ula beach and Ka`ena Point State Park, and potentially forcing park closures statewide. Your Committee searched diligently for alternative sources of funding, but reluctantly agrees with the Governor's recommendations.

However, your Committee was able to restore the Governor's proposed cuts for the Aquatic Resources Program and water resources programs that combined to a total of $1,395,373. The areas restored include regional stream studies, bottomfish surveys, coral reef studies, coastal stock enhancement, and opae ula studies.

Department of Agriculture

In a year of fiscal hardship, your Committee recognizes the delicate balance required between budget reductions and maintenance of essential services to allow the agriculture industry to remain viable and continue to grow. The Governor's proposal cut the budget of the Department of Agriculture (DOA) by $2,000,000 through reductions in vacant positions and operating expenses.

Creativity and out-of-the-box thinking has allowed your Committee to help DOA to realize general fund savings with no impact to services. Because of the increase in the Pest Inspection, Quarantine, and Eradication Fund, the Plant Industry Division was able to retain staff and fund programs slated for cuts, including coqui frog eradication. Additionally, your Committee transferred the Division of Measurement Standards out of DOA to DCCA.

Department of Transportation

DOT provides essential services to the state including the maintenance and operation of Hawaii's public airports, commercial harbors, and highways - basic duties that a state must provide its residents. Because DOT is not funded by general funds, it is relatively easy to be unconcerned with its budget. However, while general funds are the primary focus of scrutiny during difficult economic times, it is important to realize that all budgets, including those funded by special funds, must be carefully reviewed. The taxpayers do not appreciate the technical distinction and all public funds should undergo equal scrutiny and oversight.

Specifically, your Committee finds it troubling that the Highways Division faces significant payroll shortfalls and herein request a better explanation and justification that heretofore has been proffered. With the amount of resources and number of personnel available to this division, there is no excuse for this mismanagement of payroll.

Department of Labor and Industrial Relations

Securing savings from the Department of Labor and Industrial Relations (DLIR) proved to be difficult. The majority of programs and services in DLIR are either fully or partially funded by federal dollars. As a result, many programs in DLIR must meet federal requirements, which is why your Committee has respectfully disagreed with the Governor's proposal to abolish positions from the Hawaii Occupational Safety and Health Division (HIOSH). To maintain the safety and well-being of our state's employees and residents, HIOSH must be able to operate effectively and efficiently to confirm the safety of elevators and boilers, and to ensure that workplace and construction sites are as safe as possible.

While potentially life-saving programs must be protected in these difficult times, redundant programs should be reduced or eliminated. Your Committee has eliminated the Career Kokua program, "Hawaii's Career Information Delivery System", which provides a database for career exploration and skill assessment. This function is mirrored by hirenethawaii.com, a job-seeker website service maintained by the Workforce Development Division in DLIR and supplemented by One-Stop Career Centers located throughout the islands.

Capital Improvement Project Program

In light of the economic downturn both statewide and nationwide, your Committee has remained mindful of the need to stimulate our economy through capital improvement projects (CIPs) while maintaining an affordable level of debt. Your Committee has crafted the Executive Biennium Budget to preserve future funding for infrastructure projects, programs, and services, while also alleviating the financial burden on future generations.

Your Committee approached the budget prudently, carefully assessing each project, cognizant of the need to produce a comprehensive budget to help generate economic growth and reduce debt service obligation. As a result, your Committee has appropriated funding not only for those projects that can be executed immediately, but also for those that have the most potential for substantial and diverse job creation. Your Committee has also taken into account the extent of each department's individual needs, considering their repair and maintenance backlogs while giving special consideration to those projects required for health, safety, and compliance requirements.

While anxiously anticipating federal funding through the American Recovery and Reinvestment Act of 2009 (ARRA), also known as the federal stimulus package, your Committee notes the uncertainty of specific funding mechanisms and allocations. As such, your Committee crafted a comprehensive CIP budget that will not only help spur our economy, but will be in a position to supplement and enhance the effectiveness of ARRA funding.

This year, the Administration requested a total of $955,155,000 in general obligation (G.O.) and general obligaton reimbursable (G.O.R.) bond-funded projects and a total of $2,952,862,000 for all means of financing. Given current economic conditions, your Committee has attempted to address debt service obligations by reducing the amount of G.O. and G.O.R. bonds appropriated, funding a total of $881,279,000 over the biennium. This reduction in G.O. and G.O.R. bond appropriations will result in general fund debt service savings. In all means of financing, your Committee has approved $3,361,412,000 over the biennium. While this is a slight increase from the amount requested in the Administration's budget, your Committee has dedicated these funds to crucial projects, with a large portion being provided to certain departments with the flexibility to seek alternative financing options which may, in turn, further reduce debt service obligations.

Despite challenging economic times, your Committee remains dedicated to the needs of our education system. Your Committee has funded those projects necessary for health, safety, and compliance requirements, as well as those most needed to address repair and maintenance backlogs. In addition, your Committee has funded large construction projects to ensure the future growth and prosperity of our schools. Your Committee has appropriated a total of $287,076,000 for various DOE school projects and whole school renovations. Also included is a $20,000,000 increase over the Administration's budget for repair and maintenance projects.

Similarly, your Committee has appropriated a total of $206,553,000 in G.O. and G.O.R. bond-funded projects for the UH System, including a $10,000,000 increase over the Administration's budget for repair and maintenance projects. The sum of $568,487,000 was also appropriated for projects financed with all means of financing, including $28,132,000 in revenue bonds and $12,660,000 in G.O. bonds for a long overdue Information Technology Center to serve not only the entire UH System, but potentially the State as well. Additionally, given the uncertainty of the credit market, your Committee has provided a $225,402,000 revenue bond authorization and appropriation to match a $10,900,000 federal fund appropriation for the Cancer Research

Center of Hawaii (CRCH), allowing the University to seek the most affordable financing options to ensure the future of CRCH.

In addition to education, your Committee has also attempted to address the need for affordable housing, appropriating $30,000,000 over the biennium for the Rental Housing Trust Fund and $20,000,000 for the Dwelling Unit Revolving Fund. Also included in the budget is $33,000,000 for a senior residence project to provide affordable rental units to our elderly community. Your Committee made further efforts to improve the condition of our affordable and public housing facilities, appropriating $10,000,000 for the Hawaii Public Housing Authority to help address its repair and maintenance backlog and provide additional affordable housing options for low income persons.

During these desperate economic times, perhaps the most important area in need of funding is health care. Thus, your Committee has provided $81,590,000 in all means of financing to address health care needs and facilities statewide. Of this total, nearly $40,000,000 has been provided to HHSC to assist in its efforts to improve our community hospitals and provide adequate health care to our entire state population.

Budget Timeline

On July 11, 2008, the Department of Taxation announced that "State Tax Revenues in Fiscal Year 2008 Reach All-Time High of $4.6 Billion." In a press release, the Governor declared that, "Hawai'i is fortunate that its fiscal picture continues to demonstrate growth, albeit less than the 3.3 percent growth projected by the Council on Revenues (Council) in late May." Unfortunately, not mentioned was the combined projected revenue shortfall for FY 2008-2009 and the upcoming biennium shortfall of nearly $1,000,000,000. The Administration's pronounced upbeat declarations belied the harsh fiscal reality facing the State and its citizens.

In preparing its budget submittal, the Administration distributed Finance Memorandum No. 08-09, issued on August 26, 2008, to its departments advising that:

> *"The focus should be determining the level of essential services and the core functions of your department. Programs with lower priority should be identified for*

possible reduction or elimination. Many programs have received substantial funding increases since FB 2005-07 during a period when revenue growth was robust. Critical review of these new or expanded programs is now necessary."

Pursuant to Article VII, Section 8 of the Hawaii State Constitution, the Governor submitted a budget and financial plan to the Legislature on December 22, 2008. This proposal was based on the October 2008 Council projection which predicted that general fund revenues for FY 2008-2009 would decrease by one-half percent, while increasing by three and one-half percent in FY 2009-2010 and by four and one-half percent in FY 2010-2011.

A review of this initial December plan and January's proposal reveals several glaring weaknesses:

- The budget did not include a projected increase of 29 percent, or $48,000,000 per year necessary to maintain health benefits for state employees and retirees at current levels;

- The Governor's financial plan submitted in December relied on transferring $36,000,000 to the general fund from the Beverage Container Deposit Special Fund, the state's recycling program (page vii, from *The FB 2009-11 Executive Biennium Budget - Budget in Brief* dated December 2008). However, the actual legislation submitted by the Governor in House Bill 1066 in January only identified $10,000,000;

- The Governor's proposed use of $75,000,000 from the Emergency and Budget Reserve Fund (EBRF) to balance the budget, even though these funds maintain the State's solid credit rating. In the "Comprehensive Annual Financial Report", the money in the EBRF and the Hawaii Hurricane Relief Fund is identified as "unreserved fund balances," or cash on hand available for any purpose;

- The Governor's financial plan relied on approximately $56,000,000 in revenue assumptions that include publishing the names of the "Top 50 Tax Scofflaws" and collecting money from the "cash economy" even though these enforcement activities are or should already be occurring; and

- The Governor's budget was based on cuts taken in the "discretionary budget" of Executive Branch agencies which includes only 20 percent of the entire Executive Branch budget, even though the Governor assumes that 100 percent of the budgets of the Judicial Branch, Legislative Branch, and Office of Hawaiian Affairs is "discretionary" for the purpose of cuts.

During the Administration's financial plan informational briefing on January 5, 2009, the Director of Finance was questioned by the Chairman whether the Administration expected the Council to lower its projections. The Director stated that the Administration had contingencies in case the Council revised its projection downward on January 9, 2009 and that she would be able to provide a revised financial plan on or about January 16, 2009.

On January 9, 2009, the Council did in fact lower its projections by three and one-half percent for FY 2008-2009, while predicting one percent growth for FY 2009-2010, and three and one-half percent growth for FY 2010-2011. This resulted in an additional projected revenue loss of approximately $150,000,000 for FY 2008-2009 and created a projected shortfall of approximately $1,300,000,000 for the upcoming biennium.

On January 21, 2009, your Committee held an informational briefing on the Administration's financial plan expecting to learn specifically how the Administration would deal with this revenue decrease. Instead, the Director of Finance merely suggested different options, stating that the Governor had made no commitments to any of the suggestions. In other words, the Administration presented the Committee a laundry list that included salary reductions, furloughs, tax code changes, Hawaii Hurricane Relief Fund transfers, special fund sweeps, legalized gambling proposals, and increasing taxes.

On January 27, 2009, your Committee received a memorandum from the Director of Budget and Finance that provided details on how the Administration would close the budget gap in FY 2008-2009, but there were no details for the upcoming fiscal biennium.

Despite assurances that the Administration was willing to work with the Legislature to address the additional shortfall, your Committee received no specific updates until the Governor unveiled a revised financial plan on March 4, 2009.

Unfortunately, elements of this plan proved to be even weaker and more unrealistic than elements of the financial plan submitted in December 2008.

In a press release on March 4, 2009, the Governor stated that she intends to balance the budget by:

- Using $320,000,000 in Federal Medical Assistance Percentage (FMAP) available through the ARRA;
- Redistributing a portion of the Tobacco Settlement funds (H.B. No. 1731);
- Transferring tobacco tax revenue to the general fund (H.B. No. 1732);
- Advancing the general excise tax filing date (H.B. No. 1735);
- Removing the exemption for central services and administrative fees for certain special funds (H.B. No. 1740);
- Transferring the interest earned on certain special funds to the general fund (H.B. No. 1733);
- Discontinuing employer-funded group life insurance;
- Seeking a $96,000,000 reduction to the Hawaii Employer - Union Health Benefits Trust Fund (EUTF) health benefits plan; and
- Reducing the high technology tax benefits in Act 221, SLH 2001, as amended, to 50 percent of their value.

Your Committee notes that:

- The actual amount of any FMAP increase is unclear, as unemployment adjustments seem to affect the totals. Additionally, preliminary estimates apportioned $360,000,000 to Hawaii, $40,000,000 more than the Governor's estimate;

- Several of the bills relied upon to increase revenue by $99,000,000 had public hearings, but were not passed out of committee. It's unclear how the Governor proposes to advance these bills without the amendment of numerous House and Senate rules, bringing into question the value of the current legislative process. The fact that none of the referenced House Bills were requested for introduction by the Governor suggest that those ideas were not a part of the Governor's initial or amended plans; and

- Your Committee finds that basing a financial plan on ongoing "negotiations," with respect to the proposed $96,000,000 cut in benefits via the EUTF, is a questionable approach to balancing a budget. The Legislature should not enter into the exclusive providence of the Executive branch.

It is unfortunate that the Governor has chosen to include over $200,000,000 in unrealistic revenue assumptions in her financial plan.

Your Committee has no desire to balance the budget on dead bills or dubious assumptions. While some of the resultant decisions are difficult and may be unpopular, your Committee feels that they represent an honest and prudent course of action.

Your Committee realizes that no one could have predicted the severity of the current economic crisis, but there were warning signs that the recent economic expansion was unsustainable. Your Committee openly spoke about moving ahead with caution and promoted the alignment of recurring revenue with recurring expenditures noting the structural deficits that could follow if these two were not aligned. Some in the Administration vehemently disagreed, with the Director of DBEDT saying in the *Honolulu Star-Bulletin* on July 22, 2007, that members of the Legislature were providing a "gloomy assertion." The Governor further claimed at a press conference on September 12, 2008, that the direction of the economy is "right on target". Yet the Council consistently revised its projections downward in 2008. Your Committee is encouraged that on March 4, 2009, the Governor finally acknowledged that, "We can't spend money we don't have."

Federal Stimulus Package

The federal American Recovery and Reinvestment Act will provide additional resources that will certainly help the State address its budgetary difficulties. While the exact amounts have yet to be determined, your Committee included amounts to the best of its understanding.

It is anticipated that the enhanced FMAP provided to the State's Medicaid program will increase the federal government's reimbursement by millions of dollars. Your Committee's latest estimates include approximately $136,000,000 for FY 2009-2010 and $68,000,000 for FY 2010-2011 in this area alone.

This funding has had a significant impact on retaining several programs that serve those in need, including the restoration of the following cuts made by the Governor in her budget submittal:

- Adult Dental Care (Act 160, SLH 2006)provides services to a monthly average of 15,000 adults and would no longer exist were it not for the federal Medicaid stimulus funds; and

- Keiki Care (Act 236, SLH 2008) provides gap insurance coverage for infants and children under age 19. Two positions slated for reduction were recovered because of ARRA money.

Also, the receipt of additional Medicaid reimbursements for the Developmental Disabilities Program in DOH will allow your Committee to reduce DOH's general fund expenditures by $12,852,955 in FY 2009-2010 and $6,426,478 in FY 2010-2011, while maintaining these vital services.

With a provision in ARRA for medical-records modernization, your Committee has provided HHSC with $5,000,000 for FY 2009-2010 and $2,500,000 in general funds for FY 2010-2011 to be matched by federal stimulus funds of $45,000,000 for FY 2009-2010 and $22,500,000 for FY 2010-2011. These funds should help automate medical records and modernize critical operational systems for HHSC.

Conclusion

It is important to realize that this House Draft of the Executive Biennium Budget represents one step in the deliberative legislative process. Given the current economic uncertainty, it is imperative to consider every available option, and your Committee hopes that, at the very least, the door has been opened for discussion on several of these difficult topics in the near future. The difficult decisions can only be delayed but cannot and will not be denied.

On March 12, 2009, the Council revised their forecast downward again, projecting another two percent decrease for FY 2008-2009, half percent decrease for FY 2009-2010, but an increase of one and a half percent for FY 2010-2011. These revised projections result in a revenue loss of approximately $90,000,000 for FY 2008-2009 and has increased the shortfall for the upcoming biennium by approximately $170,000,000.

Only a collaborative effort will pull the state out of these difficult times, and your Committee looks forward to working with the Senate and the Executive Branch to find a responsible and honest resolution to address economic realities and produce a balanced State biennium budget.

In total, this budget amounts to $5,125,494,687 in general funds and $10,310,629,181 in all means of financing for FY 2009-2010 and $5,293,484,531 in general funds and $10,432,342,376 in all means of financing for FY 2010-2011. As a point of reference, these amounts are each lower than the amount approved in the previous budget, Act 158, Session Laws of Hawaii 2008, which appropriated $5,318,212,647 in general funds for FY 2008-2009.

As affirmed by the record of votes of the members of your Committee on Finance that is attached to this report, your Committee is in accord with the intent and purpose of H.B. No. 200, as amended herein, and recommends that it pass Second Reading in the form attached hereto as H.B. No. 200, H.D. 1, and be placed on the calendar for Third Reading.

Respectfully submitted on
behalf of the members of the
Committee on Finance,

MARCUS R. OSHIRO, Chair

HSCR 987

State of Hawaii
House of Representatives
The Twenty-fifth Legislature

Record of Votes of the Committee on Finance

Bill/Resolution No.: HB 200	Committee Referral: FIN	Date: March 11, 2009

❑ The committee is reconsidering its previous decision on the measure.

The recommendation is to: ❑ Pass, unamended (as is) ☒ Pass, with amendments (HD) ❑ Hold
❑ Pass short form bill with HD to recommit for future public hearing (recommit)

FIN Members	Ayes	Ayes (WR)	Nays	Excused
1. OSHIRO, Marcus R. (C)	✓			
2. LEE, Marilyn B. (VC)	✓			
3. AQUINO, Henry J.C.	✓			
4. AWANA, Karen Leinani	✓			
5. BROWER, Tom	✓			
6. CHOY, Isaac W.	✓			
7. COFFMAN, Denny	✓			
8. HAR, Sharon E.	✓			
9. KEITH-AGARAN, Gilbert S.C.	✓			
10. LEE, Chris	✓			
11. NISHIMOTO, Scott Y.	✓			
12. SAGUM, Roland D., III	✓			
13. TOKIOKA, James Kunane	✓			
14. WOOLEY, Jessica	✓			
15. YAMASHITA, Kyle T.	✓			
16. PINE, Kymberly Marcos	✓			
17. WARD, Gene		✓		
TOTAL (17)	16	1	0	0

The recommendation is: ☒ Adopted ❑ Not Adopted
If joint referral, ______________ did not support recommendation.
committee acronym(s)

Vice Chair's or designee's signature: Marilyn B. Lee

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