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TESTIMONY
OF
AARON S. FUJIOKA
ADMINISTRATOR
STATE PROCUREMENT OFFICE

TO THE
HOUSE COMMITTEE
ON
FINANCE

February 27, 2009

2:00 PM

HB 1372

RELATING TO THE TRANSITIONING OF THE REGIONS AND FACILITIES OF HAWAII HEALTH SYSTEMS CORPORATION.

Chair Oshiro, Vice-Chair Lee and committee members, thank you for the opportunity to testify on HB 1372.

The State Procurement Office (SPO) opposes the amendment in SECTION 4, which exempts from HRS chapter 103D, the Hawaii Health Systems Corporation (HHSC).

Statutory exemptions for specific agencies are contrary to the Hawaii Public Procurement Code (Code), section 103D-102, HRS, on the applicability of the chapter that states in part ". . . shall apply to all procurement contracts made by governmental bodies whether the consideration for the contract is cash, revenues, realizations, receipts, or earnings, . . ." Any governmental agency with the authority to expend funds should be in compliance with chapter 103D, which promotes the policy of fair and equitable treatment of all persons who deal with the procurement system; fosters effective broad-based competition; and increases public confidence in public procurement.

The SPO is against statutorily exempting specific agencies from the Code, as it is not in the best interest of government, the business community, and the general public. The Code establishes a time-tested, fair, and reliable set of rules and processes for award of contracts. The competitive procurement processes of the Code are to insure that all potential providers are afforded the opportunity to compete for the required services. To the extent agencies may need specific purchases to be exempted from Code requirements, the Code provides an exemption process.

The Code should not be viewed as an obstacle to a purchasing agency's mission, but rather as the single source of public procurement policy to be applied equally and uniformly. It was the legislature's intent for the Code to be a single source of public procurement policy. If individual agencies are exempted and allowed to develop their own individual processes, it becomes problematic and confusing to vendors, contractors and service providers that must comply with a variety of different processes and standards. Fairness, open competition, a level playing field, and government disclosure and transparency in the procurement and contracting process are vital to good government. For this to be accomplished, we must participate in the process with one set of statutes and rules.

If the Legislature believes that the policy and procedures as used by the HHSC, is a better policy than the one currently used by all 20 jurisdictions pursuant to section 103D-203, then the Code should be rewritten to reflect HHSC's policy and procedures for all purchasing jurisdictions to follow, rather than having multiple policies.

There needs to be one single source of public procurement policy.

Thank you.

HAWAII GOVERNMENT EMPLOYEES ASSOCIATION
AFSCME Local 152, AFL-CIO

AFSCME
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The Twenty-Fifth Legislature, State of Hawaii
Hawaii State House of Representatives
Committee on Finance

Testimony by
Hawaii Government Employees Association
February 27, 2009

<u>H.B. 1372 – RELATING TO THE HAWAII HEALTH SYSTEMS CORPORATION</u>

The Hawaii Government Employees Association supports the general purpose and intent of H.B. 1372. We concur that the Hawaii Health Systems Corporation (HHSC) provides vital health care safety net services to communities throughout the State that must not be lost. The continued financial challenges faced by HHSC and the State pose a risk to the public health services it offers while also hindering efforts to improve the quality of health care delivered to patients.

It is evident that decisive action is needed to ensure that HHSC remains a viable health care system. We recognize that some type of comprehensive restructuring may be required to achieve this important objective. H.B. 1372, although still a work in progress, offers the opportunity for developing a new organizational structure that will improve operations and achieve greater efficiencies.

H.B. 1372 still permits any of the regional systems or individual facilities to transition into a new legal entity, including but not limited to, a non-profit corporation, for-profit corporation, municipal facility, public benefit corporation, or any two or more combinations of these options.

However, to preserve the safety net, we believe there must be a system intact to ensure the availability of core health services to all Hawaii residents. If the current HHSC regions choose various modes of operation, there must be continuity of a system to address quality health care. The HGEA is committed to improving the bill as it moves through the legislative process.

Thank you for the opportunity to testify in support of H.B. 1372.

Respectfully submitted,

Nora A. Nomura
Deputy Executive Director

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OUR UNION OUR FAMILY
UPW
AFSCME LOCAL 646 AFL-CIO

The House of Representatives
The Twenty-Fifth Legislature
Regular Session of 2009

Committee on Finance
Rep. Marcus R. Oshiro, Chair
Rep. Marilyn B. Lee, Vice Chair

DATE: Friday, February 27, 2009
TIME: 2:00 p.m.
PLACE: Conference Room 308
State Capitol
415 South Beretania Street

TESTIMONY OF THE UNITED PUBLIC WORKERS, AFSCME, LOCAL 646, AFL-CIO ON H.B. 1372 RELATING TO HAWAII HEALTH SYSTEMS CORPORATION

My name is Dayton M. Nakanelua, and I am the state director of the United Public Workers, AFSCME, Local 646, AFL-CIO (UPW). In behalf of approximately 500 blue collar, non-supervisory employees from bargaining unit 1 and 1,000 institutional, health, and correctional workers from bargaining unit 10 who are currently employed by the Hawaii Health Systems Corporation (HHSC), the UPW opposes House Bill No. 1372 which gives to HHSC the authority for the formation of a new transition entity through the sale, lease, or transfer of the various assets or facilities of the State by the corporate board or regional system (in section 2), and to broadly grant contracting out authority to the corporate or regional system boards (in Section 5). The union submits that granting further authority and autonomy to HHSC and its regional system board,

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and transferring State facilities and assets will not work. It is time to hold top managers of HHSC accountable for the budget deficits and fiscal crisis, and to give serious consideration to restoring our community hospital system (under the State of Hawaii) which existed prior to 1996.

As you know, when HHSC was established in 1996 (through chapter 323F) there was great hope and promise that through restructuring the State of Hawaii's community hospital system, and granting autonomy to "an independent agency of the state" there would be improvements in the quality and affordability of health care for the people. See Haw. Sess. L. Act 262, § 2 at 595. It was thought that "appropriate flexibility and autonomy was needed for the community hospitals to compete and remain viable." Id. Instead each year the legislature is asked to pay more and more. As you know, the estimated HHSC shortfall for fiscal year 2008-2009 is $40,000,000 and the projected deficit for fiscal year 2009-2010 is $62,000,000. Meanwhile, the top executives of HHSC receive compensation which exceeds three (3) times what is paid to the heads of state departments and executive agencies and are given long term contracts with lucrative severance and housing allowances and exclusive incentive payments. See The Legislative Auditor's Report No. 08-08 (April 2008), at pp. 36-37 (attached).

We do not agree with the proponents of this measure that HHSC and its regional boards should be authorized to form a new entity, including a "for profit corporation" and to sell and transfer State assets as provided in the measure. (See Section 2). State "assets" and facilities should not be encumbered or transferred at the behest of any particular regional board or even by decision of the board of directors of HHSC for "profit."

We also oppose authorizing provisions which grant HHSC and its regional boards the authority to contract out operations with other entities under section 5. Under these provisions a regional board can advance its own interest by entering into a joint venture (for profit) which benefits one facility directly, but which could be detrimental to the interest of the remaining hospitals and facilities. Allowing fragmentation of the system in this manner is contrary to the public interest and to the statewide health care interest of the people of Hawaii.

We urge you to carefully examine what has happened under HHSC administration since 1996, and give serious consideration to restore health care to the State of Hawaii, Department of Health.

Financial Review of the Hawaii Health Systems Corporation

A Report to the Governor and the Legislature of the State of Hawai'i

Report No. 08-08
April 2008

THE AUDITOR
STATE OF HAWAI'I

OVERVIEW

Financial Review of the Hawaii Health Systems Corporation

Report No. 08-08, April 2008

Summary

The Office of the Auditor and the certified public accounting (CPA) firm of Accuity LLP conducted a financial review of the Hawaii Health Systems Corporation, a public body corporate and politic and an instrumentality and agency of the State of Hawai'i, for the fiscal year July 1, 2005 to June 30, 2006. The review included inquiry and analytical procedures, as well as examining the reports, records, and other relevant documents to assess the corporation's compliance with state procurement laws and to determine whether the corporation's financial statements are presented in conformity with applicable accounting principles. We also performed procedures focused on the corporation's procurement policies, compliance with the state procurement laws, lease financing arrangements, information systems, the patient billing cycle, safeguarding of capital assets, and management of conflicts of interest.

The firm was unable to render a review opinion on the corporation's financial statements as corporation management refused to sign a representation letter acknowledging its responsibility for the fair presentation of its own financial statements. Despite this being a standard review procedure, the corporation repeatedly refused to sign the representation letter unless it was first allowed to review information that is unrelated to the representations being made. The corporation also did not provide adequate responses to several analytical inquiries that were material to its financial statements, further preventing the firm from completing its review procedures. These problems resulted in significant delays in the completion of the engagement, and prevented the firm from opining on the corporation's financial statements and including those statements in this report.

With respect to the corporation's internal control over financial reporting and operations, we found three material weaknesses. First, we found that the corporation's procurement and asset management policies and practices do not comply with applicable state laws. The corporation's original exemption from the Hawai'i Public Procurement Code was repealed prior to FY2005-06, the period under review; however, the corporation did not revise its internal policies to comply with state laws. For example, the corporation continued to use $100,000 as its threshold for small purchases, while state laws applicable at the time set this threshold at $25,000. Further, the corporation claimed its procurement code exemption was reinstated by the Legislature subsequent to the period under review; however, a review of the related legislation supported no such claim and current laws specifically state that the corporation shall be subject to the procurement code. The corporation also unilaterally determined it has always been exempt from Chapter 103F, Hawai'i Revised Statutes (HRS), *Purchases of Health and Human Services*. However, the related documents provided by the corporation do not support such claims. As a result, we found several specific violations of the state laws governing procurement and asset management.

The second material weakness is that the corporation's inattention to information technology (IT) management exposes its sensitive information to unnecessary risk. The corporation has outsourced a majority of its core IT activities to third party vendors and has placed significant reliance on these vendors to ensure that the corporation's systems and applications are secure and operating properly without the corporation having an adequate system to monitor vendor activity. The third material weakness is that not all of the corporation's facilities have, or adhere to, established billings, collections, and receivables policies. An example of a negative result of this was the corporation's loss of approximately $204,000 it was due from Medicare and Medicaid because the related claims at various corporation facilities had not been submitted within the required 365 day timeframe.

During our review, we also encountered several other reportable matters. First, as previously mentioned, a general lack of management cooperation resulted in the delayed completion of the engagement and inability for us to opine on the corporation's financial statements. Second, the corporation's June 30, 2006 financial statements excluded $4 million in bond fund appropriations. Third, the corporation's compensation structure is not comparable to other state agencies. For example, compensation packages for the corporation's top executives include housing allowances, retention bonuses, severance packages (up to 200 percent of base salary plus housing allowance), and salaries that are two to three times that of other state department heads.

Recommendations and Response

We made several recommendations regarding the corporation's operations. Among these, we recommended that the corporation revise its current procurement policies and practices to comply with applicable state laws; commit adequate resource to its information technology practices; and establish and enforce consistent customer billing procedures. We also made a number of recommendations to Hawaii Health Systems Corporation's management and corporate board of directors.

In its response to our draft report, the Hawaii Health Systems Corporation was extremely critical of our overall engagement approach, and claimed our process and identified material weaknesses did not meet applicable attestation standards. The corporation also disputed nearly all of our individual findings.

Our contracted CPA firm, Accuity LLP, spent considerable time inspecting documents; conducting interviews; and reviewing the corporation's processes over procurement and asset management, customer billing, information technology, and conflicts of interest. We believe the report presents an accurate and balanced analysis of the corporation.

Marion M. Higa
State Auditor
State of Hawai'i

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Financial Review of the Hawaii Health Systems Corporation

A Report to the Governor and the Legislature of the State of Hawai'i

Conducted by

The Auditor
State of Hawai'i
and
Accuity LLP

Submitted by

THE AUDITOR
STATE OF HAWAI'I

Report No. 08-08
April 2008

The Corporation's Compensation Structure Is Not Comparable to Other State Agencies

The corporation was established as an instrumentality and agency of the State, and is therefore subject to state laws and regulations unless specifically exempted. Section 323F-8, HRS, allows the corporation to hire a chief executive officer and up to 18 additional employees exempt from the salaries recommended in Section 26-52, HRS. We found that the exempt salaries of corporation executives include retention incentives and severance packages not comparable to other state officials' and may have long-term consequences for the State.

We noted that the base salaries of the corporation's chief executive officer (CEO) and COO/CFO were more than the salaries recommended by the State Executive Salary Commission (Commission). In its *2004 Report of the Executive Salary Commission*, the Commission recommended that compensation for department heads fall within a range of $93,636 to $104,040 for FY2006, based on the size of the department. The reason for the higher compensation levels for corporation executives was due to an exemption under Section 323F-8, HRS, which allows the corporation's board of directors to establish the CEO's compensation, and also provides for the CEO to appoint up to 18 other personnel also exempt from the commission's recommended salary ranges.

In his most recent appointment, the corporation's president and CEO was appointed to a seven-year term, January 1, 2005 – December 31, 2011. After December 31, 2011, the CEO's employment automatically renews for three-year terms, unless one of the parties wishes to terminate the agreement. The CEO receives a base salary of $255,000 per year, and the base salary increases on August 1st of each year by the cost of living increase for the state as determined by the U.S. Department of Labor. The CEO also receives a housing allowance of $45,000 per year. If the CEO completes the seven-year term, the corporation will pay a retention incentive of one year's current salary plus housing allowance. Additionally, the corporation will pay a retention incentive of one-half year's current annual salary plus one-half year's annual housing allowance after the completion of each three-year term subsequent to the first seven-year term. In the event the CEO is terminated, he will receive a severance package equal to 24 months of his current base salary and housing allowance, exclusive of any incentive payments. The CEO is also a participant in the State's Employees' Retirement System. Salary and years of service are among the factors in the calculation of State retiree benefits.

The corporation's COO/CFO was appointed to a six-year term, August 1, 2005 – July 31, 2011. After July 31, 2011, the COO/CFO's employment automatically renews for three-year terms, unless one of the parties wishes to terminate the agreement. The COO/CFO receives a base salary of $217,800 per year. If the COO/CFO completes the six-year term, the corporation will pay a retention incentive of one year's current salary. Additionally, the corporation will pay a retention incentive of one-half year's current annual salary after the completion of each three-year term subsequent to the first six-year term. In the event the COO/CFO is terminated, he will receive a severance package equal to 12 months of his current base salary, exclusive of any incentive payments. The COO/CFO is also a participant in the State's Employees' Retirement System.

The corporation claims that executive compensation is commensurate with the compensation packages of executives at organizations of similar size and stature. In 2004, the corporation's board of directors performed a study on executive compensation among other healthcare organizations in the State, which revealed the following:

Organization	Base Salary (2002)	Total Cash Compensation (2002)
Hawaii Pacific Health	$575,667	$725,076
Queen's Medical Center	$398,160	$480,629
Castle Medical Center	$321,711	$421,518
Rehabilitation Hospital of the Pacific	$686,371	$697,965
Kuakini Medical Center	$218,513	$230,758

While the corporation's executive total compensation appears to be in line with if not lower than its counterparts in the private sector, it is nearly three times the salary of department heads of other executive agencies. Additionally, state department heads are employed at-will and can be dismissed without any severance benefits, and they do not receive any housing allowances.

Recommendation

We recommend that the HHSC Corporate Board review the compensation packages of its executives. While not bound by state salary schedules, the board should evaluate the aptness of executives' compensation in comparison with other healthcare, insurance, and non-profit organizations, and/or other state agencies, as deemed appropriate. In evaluating executive compensation, the board should consider total compensation and benefits, including the amount or necessity of housing allowances, bonuses, retirement benefits, and severance packages.

Faxed Testimony: 2 copies + original to Room 306
FIN Hearing
2:00 p.m., Friday, February 27, 2009
HB 1372

Hawai'i Primary Care Association

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To: **The House Committee on Finance**
The Hon. Marcus R. Oshiro, Chair
The Hon. Marilyn B. Lee, Vice Chair

Testimony in Support of House Bill 1372

Relating to the Transitioning of the Regions and Facilities of Hawaii Health Systems Corporation

Submitted by Beth Giesting, CEO

February 27, 2009, 2:00 p.m. agenda, Room 308

The Hawaii Primary Care Association supports the section of this bill that requires collaboration between HHSC and community health centers. As noted in §323F, community health centers, also known as Federally Qualified Health Centers or FQHCs, are ideal partners as bring to the community the benefits of enhanced Medicaid and Medicare reimbursement, stable federal funding with periodic opportunities for enhancement, state grants, federal tort claims coverage that relieves them of malpractice costs, and qualify for National Health Service Corps and other loan repayment programs to enhance recruitment and retention. In addition, the health centers have a clinically and economically effective model of comprehensive primary care, systems of quality assurance, electronic medical records systems, VTC systems, and other operational advantages.

Thank you for your consideration of this measure and for the opportunity to present our support.