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TO THE HOUSE COMMITTEE ON
CONSUMER PROTECTION AND COMMERCE

TWENTY-SIXTH LEGISLATURE
Regular Session of 2011

Monday, January 31, 2011
2:00 p.m.

TESTIMONY ON HOUSE BILL NO. 560
RELATING TO FINANCE.

TO THE HONORABLE ROBERT N. HERKES AND MEMBERS OF THE COMMITTEE:

My name is Keali'i S. Lopez, and I am the Interim Director of Commerce and Consumer Affairs ("DCCA" or the "Department"). The Department respectfully opposes H.B. No. 560.

The bill proposes to amend Section 26-9(o), Hawaii Revised Statutes, to require the DCCA to fund all interest payments on General Obligation ("GO") bonds issued on behalf of the DCCA and to annually collect funds from the Compliance Resolution Fund ("CRF") to pay the interest payments on the GO bonds beginning on July 1, 2011.

Since GO bonds were issued to pay for the King Kalakaua Building ("KKB"), which was purchased by the State in 2002, the Department assumes that the intent of H.B. No. 560 is to require the Department to be financially obligated to pay all the interest on the principal on the GO bonds issued for the purchase of KKB for the

Department. The Department further assumes that the rationale is based on the concept of self-funding as it applies to the capital expenditures as well as operational expenses of special-funded departments such as DCCA; that all costs should be funded exclusively through special funds.

While the Department agrees that it is reasonable, if the concept of self-funding is to be meaningful, that DCCA, in addition to operational costs, pays the capital costs associated with its operations, the department has two concerns with this particular proposal:

1. DCCA, arguably, has already paid for the KKB;
2. Even if DCCA did not already pay for the building, the Department has not budgeted funds for this purpose because this was not required of the Department when the expense was first incurred, and paying for it in the proposed manner will very seriously and adversely affect customer services and thereby undermine the Legislature's purpose in establishing the Department as a self-funded agency.

DCCA, arguably, has already paid for the building

By way of Act 177, SLH 2002 (CCA-191, item 2A), the Legislature appropriated $33 million for the acquisition and renovation of the old federal building (aka the United States Post Office Custom House and Court House), now known as the King Kalakaua Building. The means of financing was "C" funds (general obligation bond funds) rather than "D" funds (general obligation bond funds with debt service costs to be paid from special funds). KKB houses all but two of DCCA's divisions and the bulk of its employees.

H.B. No. 560 proposes to require DCCA to pay all the interest on the principal on the GO bonds issued for the purchase of the building. It is the DCCA's position that it has already reimbursed the general fund for the entire cost of the transaction, and that this proposal amounts to DCCA paying twice for the same thing.

DCCA's reimbursement arguably occurred when, simultaneous with the $33 million CIP appropriation for the building in 2002, the Legislature sought to transfer the same amount out of the CRF and into the general fund (Act 178, SLH 2002, section 39).

Governor Cayetano subsequently reduced the proposed amount to be transferred to $26 million. However, the next year, the Legislature was successful in requiring the Department to transfer another $15 million (Act 178, SLH 2003, section 28) out of the CRF. As a result, a total of $41 million was transferred from the CRF to the general fund in calendar year 2003.

While neither of the 2002 or 2003 transfer bills explicitly tied the CRF transfer to the building purchase, former DCCA director Lawrence Reifurth, in his 2009 testimony indicated that the subject of DCCA's intention to pay for the building purchase was discussed in letters from DCCA to legislative committees in 2001-02, and was mentioned later in legislative hearings. In addition, director Reifurth confirmed with former DCCA director Kathy Matayoshi (1994-2002) that DCCA intended, and understood that the Legislature intended, that the 2002 transfer was for the purpose of reimbursing the general fund for the cost of the KKB.

Even if it is legal for DCCA to pay this expense, DCCA has not budgeted to pay the expense and cannot readily afford to assume this responsibility without comprehensive planning.

The Department continues to experience reduced registration and license renewal revenues and expects that revenues will continue to fall for some time before they rise again. The Department's total revenues are projected to be $4 million less in FY 2011 compared to FY 2010.[1]

Whether or not DCCA paid for the KKB, if the Department is required to pay the estimated $11.5 million[2] for historic/current interest expenses as proposed in this measure, the Department will have an FY11 EOY cash balance of approximately $17 million, or approximately 5.2 months of reserve[3]. This is significantly below the 9-month cash reserve that the Department believes is the minimum needed in order to operate and provide the services the public needs.[4]

Additionally, if the Department pays $11.5 million for historic/current interest payments, it will likely not be in a position to assume additional future interest-related obligation. An $11.5 million transfer would leave the Department with less than $12 million (3.3 months) in cash reserves EOY FY12 and less than $6.5 million (1.8 months) in FY13.

In light of departmental cash flow needs, the Department could not assume this additional responsibility and keep services at existing levels.

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1 Based on the CRF Financial Plan numbers.
2 The Department's estimate is based on data provided by the Department of Budget and Finance in 2009 as current data is unavailable at this time.
3 Based on FY11 appropriation (Act 180, SLH 2010), which includes furlough restriction.
4 A 9-month cash reserve target was established by the Department which is significantly less than the 24-month and, the 18-month reserve targets adopted previously. The Department requires EOY cash reserves because it is responsible for addressing its own (1) cash flow, and (2) rainy day scenarios. Many of the Department's divisions do not receive any/significant revenues until well into the fiscal year (e.g., CATV: all revenues received in January/February; PVL/RICO: largest revenues received in December/June; DFI: revenues are not received until the end of the fiscal year; and INS: assessments are not usually received until the second half of the fiscal year). The 9-month reserve is reasonable. Any

Summary of the Department's position

The Department supports the principle of self-sufficiency which is the basis for the establishment of the CRF, and agrees that it is reasonable that the Department pay its own operation-related expenses. The Department is cognizant of the financial challenges facing our state, and is proactively taking steps to determine additional appropriate service payment options with other state departments for operations related services rendered to the DCCA. Additionally, the department has worked to right-size its fees over the past several years, which has resulted in reduced cash reserves. The department is concerned that the effect of this proposal would be to cause the Department to pay for KKB twice and result in significantly reducing the capacity and effectiveness of the Department to provide services.

We thank the House Committee on Consumer Protection and Commerce for the opportunity to present testimony on this matter and respectfully request that this bill be held in this Committee.

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reduction in cash reserves will require corresponding reduction in service and enforcement levels in order to bring expenses into alignment with impacted reserves.