

TESTIMONY BY KALBERT K. YOUNG
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE HOUSE COMMITTEE ON FINANCE
ON
SENATE BILL NO. 1285, S.D. 2

March 23, 2011

RELATING TO CAPITAL INVESTMENTS

Senate Bill No. 1285, S.D. 2, proposes to amend Chapter 37, Hawaii Revised Statutes, to include agency-wide technology or computer systems with an estimated useful life of over seven years to be considered capital investments and financed by bond funds.

We support this Administration measure.

We note, however, that under applicable federal law, the weighted economic lives of bond-financed capital improvements multiplied by 1.2 may not be less than the weighted average maturity of the bond issuance. The weighted economic lives will be determined using the anticipated life of each bond-financed capital improvement (including technology and computer system projects and all other projects) funded by the affected bond issuance. Because projects can be funded by more than one bond issuance based on expenditures, it will be necessary to continually monitor the amount of technology and computer system expenditures affecting our bond issuances.

NEIL ABERCROMBIE
GOVERNOR



BRUCE A. COPPA
Comptroller

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TESTIMONY
OF
BRUCE A. COPPA, COMPTROLLER
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES
TO THE
HOUSE COMMITTEE
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S.B. 1285, S.D. 2

RELATING TO CAPITAL INVESTMENTS

Chair Oshiro and members of the Committee, thank you for the opportunity to submit testimony on S.B. 1285, S.D. 2.

The Department of Accounting and General Services (DAGS) strongly supports S.B. 1285, S.D. 2.

DAGS has an immediate and pressing need to upgrade its legacy systems and hardware to ensure reliable, efficient, and effective technology solutions for State agencies and to our citizens through transparency in the access to government records and services. To accomplish this upgrade, millions of dollars are needed and the traditional financing source of general fund appropriations are unrealistic and archaic in today's environments.

Currently, the State's accounting platform, the Financial Accounting Management Information System (FAMIS) is over 25 years old. Replacement of it has been estimated at \$50

million. Another alternative would be to implement an Enterprise Resource Planning (ERP) integrated system to provide interfaces between all programs such as budget, general ledger, personnel, and payroll to eliminate the redundancy of data that now exists with our incompatible systems. The ERP solution will cost in the millions to purchase and implement and perhaps be equal to or greater than the FAMIS replacement cost of \$50 million. With the State facing an \$800 million deficit in the upcoming biennium, the funding for these system replacements cannot be from general funds. The only viable alternative would be to treat it as a capital project and utilize general obligation bond financing.

Is this approach reasonable? Yes and it is the current practice in private industry where legacy system implementation is treated as a capital project for three reasons. First, the life of the asset or system. Because of the extensive effort required to develop and implement legacy applications included changes in corporate culture (doing things differently), corporations utilize these systems for a minimum of 10 years. Secondly, because of its life, it is treated as depreciable asset, like a building. Lastly, these projects are funded with long term borrowings or possibly equity capital.

In the long term, we must begin to think about how the CIO will implement the IT strategic plan. It would be tragic to see the demise of the implementation of the IT strategic plan and the CIO by the CIO's failure to implement the IT strategic plan because the required funding to purchase the hardware, software, and other resources (i.e. consultants) were not available. That will happen like the countless other general funded IT initiatives (i.e. alternate data center) which have failed due to a lack of funding. S.B. 1285, S.D. 2, is the financing vehicle to overcome the funding road blocks and elevate the State's IT capacity.

Thank you for the opportunity to submit testimony on this matter.

Date: 03/23/2011

Committee: House Finance

Department: Education

Person Testifying: Kathryn S. Matayoshi, Superintendent of Education

Title of Bill: SB 1285,SD2(sscr602) RELATING TO CAPITAL INVESTMENTS.

Purpose of Bill: Amends chapter 37, Hawaii Revised Statutes, to include agency-wide technology and computer systems with an estimated useful life of greater than seven years as capital investments to allow all costs to be financed with bond funds and depreciated as capital investments.

Department's Position: The Department **supports** this bill. Passage of this measure would clarify the Legislature's support of the concept of bond financing of large technology and computer system projects and advance discussion on the need to replace the Department's Financial Management System (FMS). The Department needs to upgrade, improve, or replace its technology and computer systems infrastructure to become more efficient and productive. However, the cost of large-scale new technology or computer systems is prohibitively expensive when trying to budget for the project within a biennium budget, even with phased implementation. A large-scale project designed to have a useful life of multiple years should be able to be funded as a capital investment over a longer period of time. For example, the Department of Accounting and General Services (DAGS) uses FAMIS, which is approximately 20 years old. The DOE is currently using FMS, which is also approximately 20 years old, and other systems that are based on antiquated technologies. Replacement of these systems would result in improved efficiencies, greater accountability and transparency in the use of public funds, and improved reporting for decision makers and stakeholders at all levels.

The development and implementation of large information systems is costly but essential to provide efficient and accurate program execution. Allowing the cost of such systems to be classified as capital investment

costs is realistic and recognizes their long-term importance to state agencies. The Department has been pro-active in planning for the replacement of its financial management systems, and now has a request for proposal (RFP) ready to proceed. However, the main road block to proceeding is funding.

It should be noted that this concept was supported in the January 2010 report of the Task Force on Reinventing Government, which stated on page 12, "We do strongly recommend, however, that investments in technology should be considered as capital improvements by the executive and legislative branches. The corporate sector regularly capitalizes such purchases, and government would do well to do the same."

It should be further noted that the effective date of SD2 is July 1, 2050 and that the Department requests an effective date of July 1, 2011.