

DEPT. COMM. NO. 340

March 17, 2017

HAND DELIVER

The Honorable Ronald Kouchi
Senate President
415 S. Beretania Street
State Capitol, Room 409
Honolulu, Hawaii 96813

Re: Audit of the Department of Transportation, Administration Division

Dear President Kouchi:

The financial audit report of the Department of Transportation, Administration Division for the fiscal year ending 2016 was issued on January 31, 2017. The Office of the Auditor retained Egami & Ichikawa, CPAs, Inc. to perform the financial audit. For your information, we are enclosing a copy of the two-page Auditor's Summary and the report.

The Auditor's Summary and report may be viewed electronically on our website at http://files.hawaii.gov/auditor/Reports/2016_Audit/DOT_Admin_Summary_2016.pdf and http://files.hawaii.gov/auditor/Reports/2016_Audit/DOT_Admin_2016.pdf.

If you have any questions about the report, please contact me.

Very truly yours,

Leslie H. Kondo
State Auditor

LHK:RTS:lfs

Enclosures

Auditor's Summary

Financial Audit of the Department of Transportation, Administration Division

Financial Statements, Fiscal Year Ended June 30, 2016



PHOTO: OFFICE OF THE AUDITOR

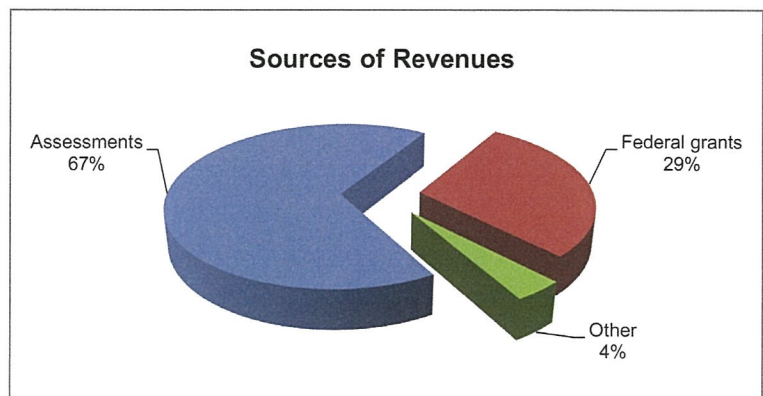
THE PRIMARY PURPOSE of the audit was to form an opinion on the fairness of the presentation of the financial statements for the Department of Transportation, Administration Division (DOT–Administration), as of and for the fiscal year ended June 30, 2016, and to comply with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance), which established audit requirements for state and local governmental units that receive federal awards. The audit was conducted by Egami & Ichikawa, Certified Public Accountants, Inc.

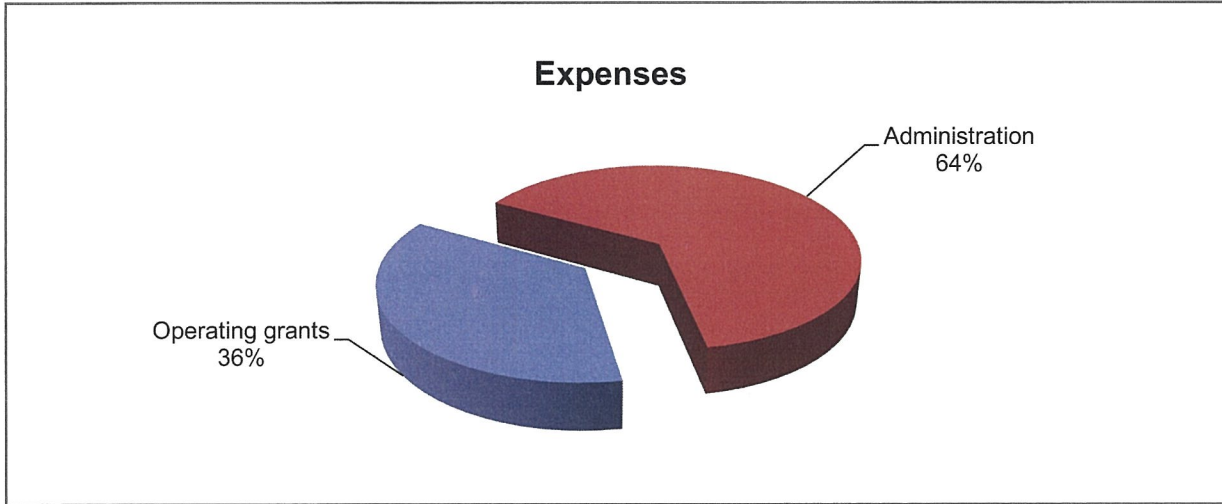
About the Division

DOT–ADMINISTRATION consists of the Office of the Director of Transportation, the Statewide Transportation Planning Office, and departmental staff services offices. Collectively, these offices provide the overall administrative support for the Department of Transportation (DOT). The Statewide Transportation Planning Office administers certain Federal Transit Administration and Federal Highway Administration grants. DOT–Administration financial statements reflect the financial activities of DOT–Administration and the Aloha Tower Development Corporation. DOT–Administration reports as assessment revenues a percentage of the Airports, Harbors, and Highways divisions' state allotted appropriations for the cost of the general administration expenses of DOT.

Financial Highlights

FOR THE FISCAL YEAR ended June 30, 2016, DOT–Administration reported total revenues of \$26.6 million, total expenses of \$22 million, and transfers to other DOT divisions of \$6.8 million resulting in a decrease in net position of \$2.2 million. The transfers related to unencumbered cash balances related to assessment revenues from those divisions. Revenues primarily consisted of \$17.7 million from assessments, \$7.7 million from federal grants, and \$1.2 million from other revenue sources.





As of June 30, 2016, total liabilities of \$18.9 million exceeded total assets of \$17.8 million, resulting in a deficit in net position of \$1.1 million. DOT–Administration has an unrestricted deficit of \$9.6 million. Total assets of \$17.8 million were comprised of cash of \$11.7 million, accounts receivable of \$5.2 million, and net capital assets of \$900,000. Liabilities totaled \$18.9 million, including a \$3.8 million Aloha Tower Development Corporation note payable to the Department of Transportation, Harbors Division.

Auditors' Opinions

DOT – ADMINISTRATION RECEIVED AN UNMODIFIED OPINION that the financial statements were presented fairly, in all material respects, in accordance with generally accepted accounting principles. DOT–Administration also received an unmodified opinion on its compliance with major federal programs in accordance with the *Uniform Guidance*.

Findings

THERE WERE NO REPORTED DEFICIENCIES in internal control over financial reporting that were considered to be material weaknesses and no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*. There were no findings that were considered material weaknesses in internal control over compliance in accordance with the *Uniform Guidance*.

For the complete report and financial statements visit our website at:
http://files.hawaii.gov/auditor/Reports/2016_Audit/DOT_Admin_2016.pdf

ORIGINAL

DEPT. COMM. NO. 340

State of Hawaii
Department of Transportation, Administration Division
Financial and Compliance Audit
June 30, 2016

Submitted By
Office of the Auditor
State of Hawaii

TABLE OF CONTENTS

| | <u>Page</u> |
|--|-------------|
| PART I - TRANSMITTAL | 1-2 |
| PART II - MANAGEMENT'S DISCUSSION AND ANALYSIS | 3-7 |
| PART III - FINANCIAL SECTION: | |
| Independent auditors' report | 8-10 |
| Financial statements | |
| Statement of Net Position - Governmental Activities | 11 |
| Statement of Activities | 12 |
| Balance Sheet - Governmental Funds | 13 |
| Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position | 14 |
| Statement of Revenues, Expenses, and Changes in Fund Balances - Governmental Funds | 15 |
| Reconciliation of the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balance to the Statement of Activities | 16 |
| Statement of Fiduciary Net Position | 17 |
| Notes to Financial Statements | 18-45 |
| Supplementary Financial Information | |
| Budgetary Comparison Statement (Non-GAAP Budgetary Basis) - Special Revenue Fund | 46 |
| Schedule of Expenditures of Federal Awards | 47-49 |
| Notes to Schedule of Expenditures of Federal Awards | 50-51 |
| PART IV - INTERNAL CONTROL AND COMPLIANCE SECTION: | |
| Reports on internal controls and compliance | |
| Report on Internal Control Over Financial Reporting and On Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i> | 52-53 |
| Independent Auditors' Report on Compliance For Each Major Program And on Internal Control Over Compliance Required by the Uniform Guidance | 54-56 |
| PART V - SCHEDULE OF FINDINGS AND QUESTIONED COSTS: | |
| Schedule of Prior Audit Findings and Questioned Costs | 57 |
| Schedule of Findings and Questioned Costs | 58-59 |
| PART VI - CORRECTIVE ACTION PLAN | 60 |

PART I
TRANSMITTAL

Office of the Auditor
State of Hawaii

We have completed our financial audit of State of Hawaii Department of Transportation, Administration Division (the "Division") as of and for the year ended June 30, 2016. The audit was performed in accordance with our agreement, dated April 21, 2016, with the Office of the Auditor, State of Hawaii.

OBJECTIVES

The primary purpose of our audit was to form an opinion on the fairness of the presentation of the Division's financial statements as of and for the fiscal year ended June 30, 2016, and to comply with the requirements of the Uniform Guidance. More specifically, the objectives of our audit were as follows:

1. To provide a basis for an opinion on the fairness of the financial statements of the Division.
2. To ascertain whether or not expenditures have been made and all revenues and other receipts to which the Division is entitled have been collected and accounted for in accordance with the laws, rules and regulations, and policies and procedures of the State of Hawaii and the federal government.
3. To ascertain the adequacy of the financial and other management information reports in providing officials at the different levels of the State and the Division the proper information to plan, evaluate, control, and correct program activities.
4. To evaluate the adequacy, effectiveness, and efficiency of the systems and procedures for financial accounting, reporting, operational and internal controls, and to recommend improvements to such systems and procedures.
5. To satisfy the audit requirements of the Federal grantor agency.

SCOPE OF THE AUDIT

Our audit was performed in accordance with auditing standards generally accepted in the United States of America as prescribed by the American Institute of Certified Public Accountants; the *Government Auditing Standards*, issued by the Comptroller General of the United States; and the provisions of the Uniform Guidance and *Audits of States, Local Governments, and Non-Profit Organizations*. The scope of our audit included an examination of the transactions and accounting records of the Division for the fiscal year ended June 30, 2016.

ORGANIZATION OF THE REPORT

This report is organized into six parts:

- PART I - Presents the transmittal letter.
- PART II - Presents management's discussion and analysis.
- PART III - Presents the financial section which includes the Division's financial statements and the auditors' report on such statements and supplementary financial information.
- PART IV - Contains the reports on internal controls over financial reporting and compliance.
- PART V - Presents the schedules of audit findings and questioned costs.
- PART VI - Contains the corrective action plan.

At this time, we wish to thank the personnel of the Administration Division and particular to the Business Management Office Staff for their cooperation and assistance extended to us. We will be happy to respond to any questions that you may have on this report.

Egami & Schuman CPAs Inc.

Honolulu, Hawaii
January 31, 2017

PART II

MANAGEMENT'S DISCUSSION AND ANALYSIS

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2016

This section of the annual financial report presents management's discussion and analysis of the Division's financial performance during the fiscal year ending June 30, 2016. It should be read in conjunction with the Division's financial statements which follows this section.

FINANCIAL HIGHLIGHTS

- The Division ended with a net position deficit of \$1,073,000 at June 30, 2016, which was a decrease of \$2,258,000 or 190.5% from the prior year. The decrease is primarily attributable to increase in operating grant expenses of \$955,000 and increase in transfers of \$1,555,000.
- The Division's current assets were \$16,895,000 which increased by \$2,673,000 or 18.8% from the prior year. The increase was primarily attributable to increases in grant related accounts receivable.
- The Division's investment in capital assets, net of depreciation were \$910,000 which increased by \$168,000 or 22.6% from the prior year. The increase is primarily attributable to addition of computer equipment.
- The Division's current liabilities were \$13,979,000 which increased by \$5,069,000 or 56.9% from the prior year. The increase is primarily attributable to increases in grant related accounts payable.
- The Division's total revenues were \$26,507,000 which was an increase of \$1,185,000 or 4.7% from the prior year. The increase was primarily attributable to increases in Federal grant revenues.

OVERVIEW OF FINANCIAL STATEMENTS

The financial statements consists of six parts: a transmittal, Management's discussion and analysis, which discusses the Division's financial performance during the fiscal year; a financial section which presents the Division's financial statements, notes to the financial statements and supplementary information; reports on internal controls and compliance; schedule of prior audit findings and questioned costs; schedules of findings and questioned costs; and the Division's corrective action plan. These components are described below:

Government-Wide Financial Statements

The government-wide financial statements reports information about the Division as a whole using accounting methods similar to those used by private sector companies. The *Statement of Net Position* provides both short-term and long-term information about the Division's financial position, which reflects the Division's financial condition at the end of the fiscal year.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
JUNE 30, 2016

OVERVIEW OF FINANCIAL STATEMENTS (Continued)

The *Statement of Net Position* presents the Division's assets and liabilities with the difference between the two reported as "net position". The *Statement of Activities* reflects the operations of the Division during the fiscal year and the resultant change in the net position. All of the current fiscal year's revenues and expenses are accounted for in the *Statement of Activities* on the accrual basis of accounting.

Fund Financial Statements

The fund financial statements provide detailed information about the Division's significant funds. A fund is a grouping of accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. Funds are either reported as a major fund or a non-major fund.

The Division has two types of funds:

- Governmental Funds:

Special Revenue Funds - The Special Revenue Funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specified purposes. The Special Revenue Funds were established to account for the contracts that the State entered into for the Division with the U.S. Department of Transportation, Federal Highway Administration (FHWA) and Federal Transit Administration (FTA). The Special Revenue Funds also include the transactions and balances of Aloha Tower Development Corporation (ATDC), a blended component unit.

- Fiduciary Funds:

Agency Fund - The Agency Fund is used to account for assets held by the Division in an agency capacity for other divisions of the Department of Transportation (DOT). These assets include receipts of bid deposits for contracts with the DOT. These assets can only be used or applied if certain requirements are met. The Division's fiduciary activities are reported in a separate "Statement of Fiduciary Net Position." These activities are excluded from the Division's basic financial statements because the Division cannot use these assets to finance its operations.

Notes to Financial Statements

The Notes to Financial Statements provide additional disclosures for the information reflected in the financial statements, which is essential to understanding the financial data provided in the government-wide fund financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
JUNE 30, 2016

OVERVIEW OF FINANCIAL STATEMENTS (Continued)

Other Reports

Following the Notes to Financial Statements and supplementary information are the Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards and a Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control over Compliance in Accordance with the Uniform Guidance. The schedules of prior and current findings and questioned cost and the Division's corrective action plan accompany these reports.

Government-wide Financial Analysis

The Statement of Net Position reflects the Division's financial condition at the end of the fiscal year. As of June 30, 2016, the Division's total net deficit was \$1,073,000.

The following presents a summarized comparison of net position and changes in net position for the fiscal years ended June 30, 2016 and 2015.

STATEMENT OF NET POSITION

June 30, 2016 and 2015

(Rounded to nearest \$1,000)

| | <u>2016</u> | <u>2015</u> |
|---|----------------------|----------------------|
| ASSETS | | |
| Current | \$ 16,895,000 | \$ 14,222,000 |
| Capital assets net of depreciation | <u>910,000</u> | <u>742,000</u> |
| Total assets | <u>\$ 17,805,000</u> | <u>\$ 14,964,000</u> |
| LIABILITIES | | |
| Current | \$ 13,979,000 | \$ 8,910,000 |
| Long-term | <u>4,899,000</u> | <u>4,869,000</u> |
| Total liabilities | <u>18,878,000</u> | <u>13,779,000</u> |
| NET POSITION DEFICIT | | |
| Invested in capital assets, net of related debt | 910,000 | 742,000 |
| Restricted for transportation projects | 7,598,000 | 6,870,000 |
| Unrestricted deficit | <u>(9,581,000)</u> | <u>(6,427,000)</u> |
| Total net position deficit | <u>(1,073,000)</u> | <u>1,185,000</u> |
| Total liabilities and net position | <u>\$ 17,805,000</u> | <u>\$ 14,964,000</u> |

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
JUNE 30, 2016

OVERVIEW OF FINANCIAL STATEMENTS (Continued)

Investment in capital assets (i.e. furniture and fixtures) and restricted funds for transportation projects, represent a large portion of the Division's net position. The Division uses these capital assets for the benefit and use by government agencies; consequently, these assets are not available for future spending and cannot be used to liquidate any liabilities. The remaining restricted assets of \$7,598,000 and \$6,870,000 at June 30, 2016 and 2015 represents resources that are subject to external restrictions or enabling legislation on how they may be used. Unrestricted deficits were \$9,581,000 and \$6,427,000 at June 30, 2016 and 2015, respectively.

The changes in net position reflect the Division's current fiscal year's revenues and expenses on the accrual basis of accounting.

CHANGES IN NET POSITION
For the Years Ended June 30, 2016 and 2015
(Rounded to nearest \$1,000)

| | <u>2016</u> | <u>2015</u> |
|-------------------------------------|-----------------------|---------------------|
| Revenues: | | |
| Assessments | \$ 17,669,000 | \$ 17,314,000 |
| Federal grant revenues | 7,652,000 | 6,922,000 |
| Other | <u>1,186,000</u> | <u>1,086,000</u> |
| Total revenues | <u>26,507,000</u> | <u>25,322,000</u> |
| Expenses: | | |
| Administration | 14,122,000 | 14,224,000 |
| Operating grants | <u>7,877,000</u> | <u>6,922,000</u> |
| Total expenses | <u>21,999,000</u> | <u>21,146,000</u> |
| Excess before transfers | 4,508,000 | 4,176,000 |
| Transfers | <u>(6,766,000)</u> | <u>(5,211,000)</u> |
| Change in net position | <u>(2,258,000)</u> | <u>(1,035,000)</u> |
| Net position, beginning of the year | <u>1,185,000</u> | <u>2,220,000</u> |
| Net position deficit, end of year | <u>\$ (1,073,000)</u> | <u>\$ 1,185,000</u> |

The Division's federal grant revenues increased by \$730,000 or 10.5% and total revenues increased by \$1,185,000 or 4.6% in 2016. Total expenses increased by \$853,000 or 4.0%. The significant changes in revenue and expenses during 2016 were attributed primarily to increases in grant revenues and related expenses.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
JUNE 30, 2016

SPECIAL FUND BUDGETARY ANALYSIS

The annual budget for the Division is based on assessments to the Harbors, Highways and Airport Divisions of the DOT, as detailed in the Notes to the Financial Statements. The significant differences between budgeted and actual revenues and expenditures in the Special Funds were primarily attributed to decreases in federal grant programs. Total revenues differed by \$22,610,000 or 50.1% below budget, and total expenditures were \$25,894,000 or 57.0% below budget.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

As of June 30, 2016 and 2015, the Division had \$910,000 and \$742,000, respectively, in capital assets, net of accumulated depreciation. The 2016 amount represents a net increase of \$168,000 or 22.6% from 2015. For the fiscal year ended June 30, 2016, there was \$384,000 in additions and transfers, which consisted primarily of computer hardware and software. Disposition of capital assets totaled \$1,523,000 for the fiscal year ended June 30, 2016.

Net capital assets (Rounded to nearest \$1,000) are as follows:

| | <u>2016</u> | <u>2015</u> |
|-------------------------------|-------------------|-------------------|
| Capital assets: | | |
| Furniture and equipment | \$ 3,559,000 | \$ 4,698,000 |
| Less accumulated depreciation | <u>2,649,000</u> | <u>3,956,000</u> |
| Total capital assets, net | <u>\$ 910,000</u> | <u>\$ 742,000</u> |

Debt Administration

As of June 30, 2016, the balance of a note payable to the Harbors Division (Harbors) approximated \$3,761,000. The note is an existing liability payable to Harbors by ATDC (a blended component unit). The Division did not have any debt financing for 2016 and 2015.

CURRENTLY KNOWN DECISIONS AND FACTS

None

PART III
FINANCIAL SECTION



INDEPENDENT AUDITORS' REPORT

Office of the Auditor
State of Hawaii

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of State of Hawaii Department of Transportation, Administration Division (the "Division") as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, based on our audit, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Division as of June 30, 2016, and the respective changes in financial position, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note 1, the financial statements present only the Division and do not purport to, and do not, present fairly the financial position of the State of Hawaii, or any other segment thereof, as of June 30, 2016, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 - 7 and 46 be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statement in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Division's basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, and is also not a required part of the basic financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 31, 2017, on our consideration of the Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.

This report is intended solely for the information and use of the Office of the Auditor, management of the Division, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Egami + Selman CPAs Inc.

Honolulu, Hawaii
January 31, 2017

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
STATEMENT OF NET POSITION - GOVERNMENTAL ACTIVITIES
June 30, 2016

| | |
|--|-----------------------|
| Current assets | |
| Cash and cash equivalents | \$ 11,674,103 |
| Accounts receivable | 5,220,529 |
| Total current assets | <u>16,894,632</u> |
| Capital assets, net of depreciation | <u>910,316</u> |
| Total assets | <u>17,804,948</u> |
| Current liabilities | |
| Accounts payable | 5,609,659 |
| Accrued payroll | 362,251 |
| Accrued vacation | 409,825 |
| Due to other divisions and funds | 7,597,507 |
| Total current liabilities | <u>13,979,242</u> |
| Long-term liabilities | |
| Due to general fund | 2,550 |
| Accrued vacation | 1,135,878 |
| Note payable to Department of Transportation, Harbors Division | 3,760,567 |
| Total long-term liabilities | <u>4,898,995</u> |
| Total liabilities | <u>18,878,237</u> |
| Net position deficit | |
| Invested in capital assets | 910,316 |
| Restricted for transportation projects | 7,597,507 |
| Unrestricted deficit | (9,581,112) |
| Total net position deficit | <u>\$ (1,073,289)</u> |

See accompanying notes to financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2016

| <u>Functions / Programs</u> | <u>Expenses</u> | <u>Program Revenues</u> | <u>Net (Expense) Revenue and Changes in Net Position</u> |
|---------------------------------------|----------------------|-----------------------------|--|
| Governmental activities: | | | |
| Administration | \$ 14,121,727 | \$ - | \$ (14,121,727) |
| Operating grants | <u>7,877,374</u> | <u>-</u> | <u>(7,877,374)</u> |
| Total governmental activities | <u>\$ 21,999,101</u> | <u>\$ -</u> | <u>(21,999,101)</u> |
| General revenues: | | | |
| Assessments | | | 17,668,916 |
| Federal grant revenues | | | 7,652,171 |
| Investment earnings | | | 80,224 |
| Miscellaneous | | | <u>1,106,040</u> |
| Total general revenues | | | <u>26,507,351</u> |
| Excess revenues over expenses | | | 4,508,250 |
| Other financing uses - transfers, net | | | <u>(6,766,154)</u> |
| Change in net position | | | (2,257,904) |
| Net position, beginning of the year | | | <u>1,184,615</u> |
| Net position deficit, end of year | | | <u>\$ (1,073,289)</u> |

See accompanying notes to financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
BALANCE SHEET - GOVERNMENTAL FUNDS

June 30, 2016

| | Restricted Funds | | | | Admin Fund | Other Govern- mental Funds | Total Govern- mental Funds |
|---|---------------------|------------------|------------------|------------------|---------------------|-------------------------------------|-------------------------------------|
| | S-213 | S-231/236 | S-255 | S-257 | | | |
| ASSETS | | | | | | | |
| Cash and cash equivalents | \$ 1,400,000 | \$ 34,924 | \$ 22,684 | \$ 97,630 | \$ 1,984,317 | \$ 1,463,279 | \$ 11,674,103 |
| Accounts receivable | 2,509,996 | - | 454 | - | 2,710,079 | - | 5,220,529 |
| TOTAL ASSETS | \$ 3,909,996 | \$ 34,924 | \$ 23,138 | \$ 97,630 | \$ 4,694,396 | \$ 1,463,279 | \$ 16,894,632 |
| LIABILITIES AND FUND BALANCES | | | | | | | |
| LIABILITIES | | | | | | | |
| Accounts payable | \$ 2,509,996 | \$ - | \$ 454 | \$ - | \$ 2,710,079 | \$ 389,130 | \$ 5,609,659 |
| Accrued payroll | - | - | - | - | - | 362,251 | 362,251 |
| Due to general funds | - | - | - | - | - | 2,550 | 2,550 |
| Note payable to Department of Transportation, Harbors Division | - | - | - | - | - | - | 3,760,567 |
| Due to other divisions and funds | - | - | - | - | - | 7,597,507 | 7,597,507 |
| Total liabilities | 2,509,996 | - | 454 | - | 2,710,079 | 8,351,438 | 17,332,534 |
| FUND BALANCES (DEFICITS) | | | | | | | |
| Assigned | 2,509,996 | - | - | - | - | 1,772,650 | 4,282,646 |
| Unassigned | (1,109,996) | 34,924 | 22,684 | 97,630 | 1,984,317 | (3,452,819) | (4,720,548) |
| Total fund balances (deficits) | 1,400,000 | 34,924 | 22,684 | 97,630 | 1,984,317 | (1,680,169) | (437,902) |
| TOTAL LIABILITIES AND FUND BALANCES | \$ 3,909,996 | \$ 34,924 | \$ 23,138 | \$ 97,630 | \$ 4,694,396 | \$ 6,671,269 | \$ 16,894,632 |

See accompanying notes to financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO THE STATEMENT OF NET POSITION
June 30, 2016

| | |
|--|------------------------------|
| Total fund balances - governmental funds | \$ (437,902) |
| Amounts reported for governmental activities that are different in the Statement of Net Position due to: | |
| Capital assets used in governmental activities are not financial resources and therefore not reported in the governmental funds | 910,316 |
| Accrued employee benefits payable not reported in the governmental funds | <u>(1,545,703)</u> |
| Total net position deficit - governmental activities | <u><u>\$ (1,073,289)</u></u> |

See accompanying notes to financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND
BALANCES - GOVERNMENTAL FUNDS

For the Year Ended June 30, 2016

| | Restricted Funds | | | | Admin Fund | Other Govern- mental Funds | Total Govern- mental Funds |
|---|---------------------|------------------|------------------|------------------|-----------------------|-------------------------------------|-------------------------------------|
| | <u>S-213</u> | <u>S-231/236</u> | <u>S-255</u> | <u>S-257</u> | | | |
| REVENUES | | | | | | | |
| Assessments | \$ - | \$ - | \$ - | \$ - | \$ 17,668,916 | \$ - | \$ 17,668,916 |
| Federal grant revenues | 3,508,683 | 242,663 | 454 | 9,354 | - | - | 7,652,171 |
| Other | - | - | - | - | 186,264 | 1,000,000 | 1,186,264 |
| | <u>3,508,683</u> | <u>242,663</u> | <u>454</u> | <u>9,354</u> | <u>17,855,180</u> | <u>1,000,000</u> | <u>26,507,351</u> |
| EXPENDITURES | | | | | | | |
| Personal services | - | - | - | 17,584 | 8,418,066 | - | 8,494,953 |
| Other | 3,508,683 | 242,663 | 454 | - | 5,836,915 | 226,597 | 13,684,441 |
| | <u>3,508,683</u> | <u>242,663</u> | <u>454</u> | <u>17,584</u> | <u>14,254,981</u> | <u>226,597</u> | <u>22,179,394</u> |
| EXCESS (DEFICIT) OF REVENUES OVER EXPENDITURES | - | - | - | (8,230) | 3,600,199 | 773,403 | 4,327,957 |
| OTHER FINANCING SOURCES (USES) | | | | | | | |
| Transfers in | 2,400,000 | - | - | - | 3,000,000 | 2,500 | 8,702,500 |
| Transfers out | (1,000,000) | - | - | - | (12,472,309) | - | (15,472,309) |
| Other | - | - | - | - | - | 3,655 | 3,655 |
| | <u>1,400,000</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>(9,472,309)</u> | <u>6,155</u> | <u>(6,766,154)</u> |
| NET CHANGE IN FUND BALANCES | 1,400,000 | - | - | (8,230) | (5,872,110) | 779,558 | (2,438,197) |
| Fund balances (deficits), beginning of year | - | 34,924 | 22,684 | 105,860 | 4,191,941 | (3,076,846) | 2,000,295 |
| Fund balances (deficits), end of year | <u>\$ 1,400,000</u> | <u>\$ 34,924</u> | <u>\$ 22,684</u> | <u>\$ 97,630</u> | <u>\$ (1,680,169)</u> | <u>\$ (2,297,288)</u> | <u>\$ (437,902)</u> |

See accompanying notes to financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT
OF REVENUES, EXPENDITURES, AND CHANGES IN FUND
BALANCES TO THE STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2016

| | | |
|---|------------------|---------------------------|
| Total net change in fund balances - governmental funds | \$ | (2,131,594) |
| Amounts reported for governmental activities that are different in the Statement of Net Assets due to: | | |
| Capital asset outlays, net transfers and disposals | \$ 379,906 | |
| Depreciation expense | <u>(211,170)</u> | |
| Excess of capital asset outlays over depreciation expense | | 168,736 |
| The net change in obligations for accrued vested vacation benefits is reported in the Statement of Activities, but is not reported as an expenditure in the governmental funds as it does not require the use of current financial resources. | | |
| | | <u>11,557</u> |
| Change in net position of governmental activities | \$ | <u><u>(1,951,301)</u></u> |

See accompanying notes to the financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
STATEMENT OF FIDUCIARY NET POSITION
June 30, 2016

ASSETS

Cash and cash equivalents \$ 10,400

Total assets \$ 10,400

LIABILITIES

Bid bond payable \$ 7,400

Other Payable 3,000

Total liabilities \$ 10,400

See accompanying notes to financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Department of Transportation of the State of Hawaii was formed shortly after Hawaii became a State in 1959. It has three divisions, Airports, Harbors and Highways, which are supported by 10 departmental staff offices. The State of Hawaii Department of Transportation, Administration Division (Division) consists of the Office of the Director of Transportation, Departmental Staff Services Offices, and the Statewide Transportation Planning Office. Collectively, these offices provide the overall administrative support of the Department of Transportation.

The Statewide Transportation Planning (STP) Office is responsible for the administration of certain Federal Transit Administration (FTA) and Federal Highway Administration (FHWA) federal grants awarded to the Department of Transportation.

The Division's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for State and Local Governments through its pronouncements (Statements and Interpretations). The more significant accounting policies established in GAAP and used by the Division is discussed below.

Reporting entity - The financial statements reflect only the Division's financial activities as well as the financial activities of Aloha Tower Development Corporation (ATDC), a blended component unit of the Division. The State Comptroller maintains the central accounts for all State funds and publishes financial statements for the State of Hawaii (State) annually, which includes the Division's financial activities.

Government-Wide and Fund Financial Statements - (the statement of net position and the statement of activities) report information of all of the nonfiduciary activities of the Division. In general, the effect of interfund activity has been removed from these government-wide statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges to customers who purchase, use or directly benefit from goods or services provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items not properly included among

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues. The Division does not allocate general government (indirect) expenses to other functions.

Net position components are classified restricted when legally enforceable enabling legislation places restrictions or are externally imposed by citizens and/or public interest groups. Additionally, restricted net position are re-evaluated if any of the resources raised by the enabling legislation are used for a purpose not specified by the enabling legislation or if the government has other cause for reconsideration. Internally imposed designations of resources are not presented as restricted components of net position. When both restricted and unrestricted resources are available for use, generally it is the Division's policy to use restricted resources first, then unrestricted resources as they are needed.

Separate financial statements are provided for Governmental Funds and Fiduciary Funds. However, the Fiduciary Funds are not included in the government-wide financial statements. Major Governmental Funds are reported as separate columns in the fund financial statements.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

Government Wide Financial Statements - are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

Governmental Funds Financial Statements - are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Division considers revenues other than federal grants and assistance awards to be available if they are collected within 60 days of the end of the fiscal year.

Federal grants and assistance awards made on the basis of entitlement periods are recorded as revenues when available and entitlement occurs which is generally within 12 months of the end of the current fiscal year. All other federal reimbursement-type grants are recorded as intergovernmental receivables and revenues when the related expenditures or expenses are incurred and funds are available.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Expenditures are generally recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Encumbrances are recorded obligations in the form of purchase orders or contracts. The Division records encumbrances at the time purchase orders or contracts are awarded and executed. Encumbrances outstanding at fiscal year-end are reported as restrictions, assignments, or commitments (no commitments in 2016) of fund balances since they do not constitute expenditures or liabilities.

Fiduciary Fund - financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide financial statements described above. Agency Funds do not have a measurement focus, and report only assets and liabilities.

Fund Accounting - The financial statements of the Division are recorded in individual funds, each of which is deemed to be a separate accounting entity. The division uses fund accounting to report on its financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.

The financial activities of the Division that are reported in the accompanying fund financial statements have been classified into the following major Governmental Fund. In addition, a description of the Fiduciary Fund follows.

Governmental Fund Type

The Division reports the following major Governmental Fund:

Special Revenue Fund - are used to account for the proceeds of specific revenue sources that are restricted to expenditures for specified purposes. The Special Revenue Funds were established to account for the contracts that the State entered into for the Division with the U.S. Department of Transportation, Federal Highways Administration (FHWA), Federal Transit Administration (FTA) and those between the Division and FTA prior to enactment of the Intermodal Surface Transportation Efficiency Act of 1991. The special revenue funds also includes the transactions and balances of ATDC, a blended component unit.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Fiduciary Fund Type

The Division reports the following Fiduciary Fund:

Agency Fund - is used to account for assets held by the Division in an agency capacity. These assets include the receipt of bid deposits for contracts with the Department of Transportation (DOT) in accordance with the Taxpayer Relief Act of 1997. These assets can only be used or applied if certain requirements are met. The Division's fiduciary activities are reported in a separate Statement of Fiduciary Net Position. These activities are excluded from the Division's basic financial statements because the Division cannot use these assets to finance its operations.

Net Position - In the government wide financial statements, net position is reported in three categories: net investment in capital assets, net of related debt; if any; restricted; and unrestricted. Restricted components are restricted by parties outside of the State (such as citizens, public interest groups or the judiciary) or imposed by law through enabling legislation.

Fund Balance Reporting - In the fund financial statements, Governmental Funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

In accordance with GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, the Division classifies fund balances based primarily on the extent to which it is bound to follow constraints on how resources can be spent. Classifications used by the Division are:

Restricted - Represents resources that are restricted to specific purposes usually imposed by external parties such as creditors, grantors, or other governments.

Committed - Represents resources that can only be used for specific purposes pursuant to formal action of the Legislature.

Assigned - Represents resources that are constrained by management's intent to be used for specific purposes, but are neither restricted nor committed.

Unassigned - Represents residual balances that are neither nonspendable, restricted, committed or assigned.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Encumbrance balances at year-end are reflected as assigned. The Division's Special Funds consist of specific revenue sources restricted or committed to expenditure for specific purposes other than debt service or capital projects. Restricted and committed revenues are expected to comprise a substantial portion of the fund inflows. Funds not meeting these criteria are reported in the general fund. The spending policy of the Division's Special Funds is, in order of priority, restricted, committed, and then assigned. The Division's classification of Special Fund inflows are restricted (federal grants), program revenues (committed), transfers from other funds (assigned), investment income (assigned unless restricted), and miscellaneous revenues (assigned). The Division's Special Funds are not encumbered.

Assessment Revenues - In accordance with Section 30, Chapter 36, of the Hawaii Revised Statutes (HRS), the Division reports as assessment revenues a percentage of the Airports, Harbors, and Highways Divisions' State allotted appropriations for the cost of the general administration expenses of the DOT.

On a quarterly basis, the divisions of DOT transfer their pro-rata share of their budgetary appropriation to cover their share of the operation expenses incurred by the Division. The unencumbered cash balances at the end of each fiscal year are transferred back to the respective divisions in accordance with their pro-rata share percentage. *Due to Other Divisions and Funds* as of June 30, 2016 was \$7,597,507. The \$6,766,154 reflected as *Other financing sources - Transfers, net* is the amount of unencumbered cash balances transferred back to the other divisions and other funds during 2016. The net transfers during the year ended June 30, 2016 contributed to the net position deficit of \$1,073,289 as of June 30, 2016.

Risk Management - The Division is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; and workers' compensation. The Division is insured under the State of Hawaii (the State) as follows: The State generally retains the first \$1,000,000 per occurrence of property losses, the first \$4,000,000 with respect to general liability claims, and the first \$500,000 of losses due to crime. Losses in excess of those retention amounts are insured with commercial insurance carriers. The limit per occurrence for property losses is \$200,000,000, except for terrorism, which is \$50,000,000 per occurrence. The annual aggregate for general liability losses is \$5,000,000 per occurrence and for crime losses, the limit per occurrence is \$10,000,000 with no aggregate limit. The State is generally self-insured for workers' compensation and automobile claims.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The estimated reserve for losses and loss adjustment costs includes the accumulation of estimates for losses and claims reported prior to fiscal year-end, nonincremental estimates (based on projections of historical developments) of claims incurred but not reported, and nonincremental estimates of costs for investigating and adjusting all incurred and unadjusted claims. Amounts reported are subject to the impact of future changes in economic and social conditions. The State believes that, given the inherent variability in any such estimates, the reserves are within a reasonable and acceptable range of adequacy. Reserves are continually monitored and reviewed, and as settlements are made and reserves adjusted, the differences are reported in current operations. A liability for a claim is established if information indicates that it is probable that a liability has been incurred at the date of the basic financial statements and the amount of the loss is reasonably estimable.

Interfund and Intrafund Transfers - Significant transfers of financial resources between activities within the same fund are offset within that fund. Transfers of revenues from funds authorized to receive them to funds authorized to expend them are recorded as operating transfers in the financial statements.

Compensated Absences - The Division's policy to permit employees to accumulate earned but unused vacation and sick leave benefits. There is no liability for unpaid accumulated sick leave since sick leave is not convertible to pay upon termination of employment. All vacation pay is accrued when incurred. A liability for these amounts is reported only if they have matured, for example, as a result of employee resignations and retirements.

Deferred Compensation Plan - The Division offers its employees a deferred compensation plan (Plan) created in accordance with Internal Revenue Code Section 457. The Plan, available to all Division employees, permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

All Plan assets are held in a trust fund to protect them from claims of general creditors. The Division has no responsibility for loss due to the investment or failure of investment of funds and assets in the Plan, but does have the duty of due care that would be required of an ordinary prudent investor. Accordingly, the assets and liabilities of the Division's deferred compensation plan are not reported in the accompanying basic financial statements.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Cash and Cash Equivalents - Cash and cash equivalents include all cash, repurchase agreements, U.S. government securities and time certificates of deposits with original maturities of three months or less.

Investments - The State's investments are reported at fair value within the fair value hierarchy established by generally accepted accounting principles. Investments in mutual funds are reported at fair value based on quoted market prices. Investments in U.S. government obligations are reported at fair value based on quoted prices or other observable inputs, including pricing matrices. Investments in certificates of deposit and repurchase agreements are reported at fair value using cost-based measures due to the nonparticipating nature of these securities.

Fair Value Measurements - The State measures the fair value of assets and liabilities as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants at the measurement date. The fair value hierarchy distinguishes between independent observable inputs and unobservable inputs used to measure fair value, as follows:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 - Inputs other than quoted market prices included in Level 1 that are observable for an asset or liability, either directly or indirectly.
- Level 3 - Unobservable inputs for an asset or liability reflecting the reporting entity's own assumptions. Level 3 inputs are used to measure fair value to the extent that observable Level 1 or 2 inputs are not available.

Capital Assets - Capital assets of the Division include furniture and equipment with estimated useful lives greater than one year and acquisition costs greater than the following amounts:

| | |
|-------------------------|---------|
| Furniture and equipment | \$5,000 |
|-------------------------|---------|

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at their estimated fair market value at the date of donation. Transfers are recorded at cost, net of the depreciation which would have been charged had the asset been directly acquired by the Division. Major outlays for capital assets and improvements are capitalized as projects are constructed to the extent the State's capitalization thresholds are met. Interest incurred during the construction phase of the capital assets is reflected in the capitalized value of the asset constructed, net of interest earned, on the invested proceeds over the same period. Maintenance and repairs are charged to operations when incurred. Betterments and major improvements which significantly increase values, change capacities, or extend useful lives are capitalized. Upon sale or retirement of capital assets, the cost and the related accumulated depreciation, as applicable, are removed from the respective accounts, and any resulting gain or loss is recognized in the statement of activities.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

| | <u>Useful Lives</u> |
|-------------------------|---------------------|
| Furniture and equipment | 5 - 7 years |

Use of Estimates - The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the basic financial statements and accompanying notes. Actual results could differ from those estimates.

Pensions - For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Employees' Retirement System (ERS) and additions to/deductions from the ERS's fiduciary net position have been determined on the same basis as they are reported by the ERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with benefit terms. Investments are reported at their fair value.

Grants - Revenues for all federal reimbursement-type grants are recorded as receivables when costs are incurred.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

2. BUDGETING AND BUDGETARY CONTROL

The Division's budget is established through the State of Hawaii's (State) budgetary process.

The budget of the State is a detailed operating plan identifying estimated costs and results in relation to estimated revenues. The budget includes (1) the programs, services, and activities to be provided during the fiscal year; (2) the estimated revenues available to finance the operating plan; and (3) the estimated spending requirements of the operating plan. The budget represents a process through which policy decisions are made, implemented, and controlled. Revenue estimates are provided to the State legislature at the time of budget consideration and are revised and updated periodically during the fiscal year. Amounts reflected as budgeted revenues in the general fund statement of revenues and expenditures - budget and actual (budgetary basis) are those estimates as compiled by the Council on Revenues and the Director of Finance. Budgeted expenditures are derived primarily from the General Appropriations Act, Supplemental Appropriations Act, and from other authorizations contained in the State Constitution, the Hawaii Revised Statutes, and other specific appropriations acts in various State Legislative Hearings.

All expenditures of appropriated funds are made pursuant to the appropriations in the biennial budget.

The General Fund and Special Revenue Funds have legally appropriated annual budgets. The Capital Projects Fund's appropriated budgets are for projects that may extend over several fiscal years.

The final legally adopted budget in the accompanying general fund statement of revenues and expenditures - budget and actual (budgetary basis) represents the original appropriations, transfers, and other legally authorized legislative and executive changes.

The legal level of budgetary control is maintained at the appropriation line item level by department, program, and source of funds as established in the appropriations acts. The Governor is authorized to transfer appropriations between programs within the same department and source of funds; however, transfers of appropriations between departments generally require legislative authorization. Records and reports reflecting the detail level of control are maintained by and are available at the Department of Accounting and General Services.

To the extent not expended or encumbered, the General Fund's appropriations generally lapse at the end of the fiscal year for which the appropriations are made. The State Legislature specifies the lapse dates and any other contingencies which may terminate the authorizations for other appropriations.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

2. BUDGETING AND BUDGETARY CONTROL (Continued)

Budgets adopted by the State Legislature for the General Fund are presented in the general fund statement of revenues and expenditures - budget and actual (budgetary basis). The State's annual budget is prepared on the modified-accrual basis of accounting with several differences, acquired through long-term financing (basis difference) and (2) the accounting for transfers of principally related to (1) the encumbrance of purchase order and contract obligations and equipment debt service payments through the General Fund (perspective difference), which represent departures from GAAP.

Adjustments necessary to convert the results of operations and fund balances for the year ended June 30, 2016 from the GAAP basis to the budget basis are as follows:

| | |
|---|-----------------------|
| Excess of expenditures over revenues and transfers, GAAP basis | \$ (2,438,197) |
| Increase (decrease) in revenues: | |
| Current year receivables | (5,220,529) |
| Prior year receivables | <u>1,188,635</u> |
| | <u>(4,031,894)</u> |
| Increase (decrease) in expenditures: | |
| Current year accrued liabilities | (5,974,460) |
| Prior year accrued liabilities | 1,593,624 |
| Current year encumbrances, net of adjustments | 3,552,741 |
| Prior year encumbrances | <u>(1,787,608)</u> |
| | <u>(2,615,703)</u> |
| Excess of expenditures over revenues and transfers, budgetary basis | \$ <u>(3,854,388)</u> |

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS

The Director of Finance is responsible for the safekeeping of all monies deposited into the State Treasury. The Director of Finance pools and invests any monies of the State, which in the Director of Finance's judgment, are in excess of the amounts necessary for meeting the specific requirements of the State. Investment earnings are allocated to the Division based on its equity interest in the pooled monies. Legally authorized investments include obligations of or guaranteed by the U.S. government, obligations of the State, federally-insured savings and checking accounts, time certificates of deposit, auction rate securities, and repurchase agreements with federally-insured financial institutions.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

4. CAPITAL ASSETS

Capital assets activities for the governmental activities of the Division for the year ended June 30, 2016, were as follows:

| | <u>Beginning Balance</u> | <u>Increases</u> | <u>Decreases</u> | <u>Ending Balance</u> |
|--|------------------------------|-------------------|------------------|---------------------------|
| <u>Capital assets:</u> | | | | |
| Furniture & equipment | \$4,698,381 | \$ 383,978 | \$1,523,008 | \$3,559,351 |
| Less accumulated depreciation | <u>3,956,801</u> | <u>211,170</u> | <u>1,518,936</u> | <u>2,649,035</u> |
| Capital assets, net of depreciation | <u>\$ 741,580</u> | <u>\$ 172,808</u> | <u>\$ 4,072</u> | <u>\$ 910,316</u> |

5. ACCRUED VACATION

Accrued vacation consists of the following:

| | |
|-----------------------------------|--------------------|
| Balance at June 30, 2015 | \$1,557,259 |
| Increases | <u>(11,556)</u> |
| Balance at June 30, 2016 | 1,545,703 |
| Less current portion | <u>(409,825)</u> |
| Total accrued vacation, long-term | <u>\$1,135,878</u> |

6. CHANGES IN LONG-TERM LIABILITIES

Changes in non-current liabilities were as follows:

| | <u>Beginning Balance</u> | <u>Increases</u> | <u>Decreases</u> | <u>Ending Balance</u> | <u>Due within one year</u> |
|-------------------------|------------------------------|-------------------|-------------------|---------------------------|--------------------------------|
| Due to general fund | \$ 2,550 | \$ - | \$ - | \$ 2,550 | \$ - |
| Accrued vacation | 1,106,175 | 480,788 | 451,085 | 1,135,878 | 409,825 |
| Note payable-DOT Harbor | <u>3,760,567</u> | <u>-</u> | <u>-</u> | <u>3,760,567</u> | <u>-</u> |
| | <u>\$4,869,292</u> | <u>\$ 480,788</u> | <u>\$ 451,085</u> | <u>\$4,898,995</u> | <u>\$ 409,825</u> |

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS

Pension Plan

Plan Description

Generally, all full-time employees of the State and counties are required to be members of the ERS, a cost sharing multiple-employer defined benefit pension plan administered by the State's pension benefits program. Benefits, eligibility, and contribution requirements are governed by HRS Chapter 88 and can be amended through legislation. The ERS issues a publicly available financial report that can be obtained at ERS's website: <http://www.ers.ehawaii.gov/>.

Benefits provided

The ERS Pension Trust is comprised of three pension classes for membership purposes and considered to be a single plan for accounting purposes since all assets of the ERS may legally be used to pay the benefits of any of the ERS members or beneficiaries. The ERS provides retirement, disability, and death benefits with three membership classes known as the noncontributory, contributory and hybrid retirement classes. The three classes provide a monthly retirement allowance equal to the benefit multiplier (generally 1.25% or 2%) multiplied by the average final compensation multiplied by years of credited service. Average final compensation for members hired prior to July 1, 2012 is an average of the highest salaries during any three years of credited service, excluding any salary paid in lieu of vacation for members hired January 1, 1971 or later and the average of the highest salaries during any five years of credited service including any salary paid in lieu of vacation for members hired prior to January 1, 1971. For members hired after June 30, 2012, average final compensation is an average of the highest salaries during any five years of credited service excluding any salary paid in lieu of vacation.

Each retiree's original retirement allowance is increased on each July 1 beginning the calendar year after retirement. Retirees first hired as members prior to July 1, 2012 receive a 2.5% increase each year of their original retirement allowance without a ceiling. Retirees first hired as members after June 30, 2012 receive a 1.5% increase each year of their original retirement allowance without a ceiling. The annual increase is not compounded.

The following summarizes the provisions relevant to the largest employee groups of the respective membership class.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

Noncontributory Class

- Retirement Benefits - General employees' retirement benefits are determined as 1.25% of average final compensation multiplied by the years of credited service. Employees with ten years of credited service are eligible to retire at age 62. Employees with 30 years of credited service are eligible to retire at age 55.
- Disability Benefits - Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 35% of their average final compensation. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined in the same manner as retirement benefits but are payable immediately, without an actuarial reduction, and at a minimum of 12.5% of average final compensation.
- Death Benefits - For service-connected deaths, the surviving spouse/reciprocal beneficiary receives a monthly benefit of 30% of the average final compensation until remarriage or re-entry into a new reciprocal beneficiary relationship. Additional benefits are payable to surviving dependent children up to age 18. If there is no spouse/reciprocal beneficiary or dependent children, no benefit is payable.

Ordinary death benefits are available to employees who were active at time of death with at least ten years of credited service. The surviving spouse/reciprocal beneficiary (until remarriage/reentry into a new reciprocal beneficiary relationship) and dependent children (up to age 18) receive a benefit equal to a percentage of member's accrued maximum allowance unreduced for age or, if the member was eligible for retirement at the time of death, the surviving spouse/reciprocal beneficiary receives 100% joint and survivor lifetime pension and the dependent children receive a percentage of the member's accrued maximum allowance unreduced for age.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

Contributory Class for Members Hired prior to July 1, 2012

- Retirement Benefits - General employees' retirement benefits are determined as 2% of average final compensation multiplied by the years of credited service. General employees with five years of credited service are eligible to retire at age 55.
- Disability Benefits - Members are eligible for service-related disability benefits regardless of length of service and receive a one-time payment of the member's contributions and accrued interest plus a lifetime pension of 50% of their average final compensation. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined as 1.75% of average final compensation multiplied by the years of credited service but are payable immediately, without an actuarial reduction, and at a minimum of 30% of average final compensation.
- Death Benefits - For service-connected deaths, the surviving spouse/reciprocal beneficiary receives a lump sum payment of the member's contributions and accrued interest plus a monthly benefit of 50% of the average final compensation until remarriage or re-entry into a new reciprocal beneficiary relationship. If there is no surviving spouse/reciprocal beneficiary, surviving children (up to age 18) or dependent parents are eligible for the monthly benefit. If there is no spouse/reciprocal beneficiary or dependent children/parents, the ordinary death benefit is payable to the designated beneficiary.

Ordinary death benefits are available to employees who were active at time of death with at least one year of service. Ordinary death benefits consist of a lump sum payment of the member's contributions and accrued interest plus a percentage of the salary earned in the 12 months preceding death, or 50% Joint and Survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% Joint and Survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

Contributory Class for Members Hired After June 30, 2012

- Retirement Benefits - General employees' retirement benefits are determined as 1.75% of average final compensation multiplied by the years of credited service. General employees with ten years of credited service are eligible to retire at age 60.
- Disability and Death Benefits - Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 50% of their average final compensation plus refund of contributions and accrued interest. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are 3.0% of average final compensation for each year of service for judges and elected officers and 1.75% of average final compensation for each year of services for police and firefighters and are payable immediately, without an actuarial reduction, at a minimum of 30% of average final compensation.

Death benefits for contributory plan members hired after June 30, 2012 are generally the same as those for contributory plan members hired June 30, 2012 and prior.

Hybrid Class for Members Hired Prior to July 1, 2012

- Retirement Benefits - General employees' retirement benefits are determined as 2% of average final compensation multiplied by the years of credited service. General employees with five years of credited service are eligible to retire at age 62. General employees with 30 years of credited service are eligible to retire at age 55.
- Disability Benefits - Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 35% of their average final compensation plus refund of their contributions and accrued interest. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined in the same manner as retirement benefits but are payable immediately, without an actuarial reduction, and at a minimum of 25% of average final compensation.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

- Death Benefits - For service-connected deaths, the surviving spouse/reciprocal beneficiary receives a lump sum payment of the member's contributions and accrued interest plus a monthly benefit of 50% of the average final compensation until remarriage or re-entry into a new reciprocal beneficiary relationship. If there is no surviving spouse/reciprocal beneficiary, surviving children (up to age 18) or dependent parents are eligible for the monthly benefit. If there is no spouse/reciprocal beneficiary or dependent children/parents, the death benefit is payable to the designated beneficiary.

Ordinary death benefits are available to employees who were active at time of death with at least five years of service. Ordinary death benefits consist of a lump sum payment of the member's contributions and accrued interest plus a percentage multiplied by 150%, or 50% Joint and Survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% Joint and Survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary.

Hybrid Class for Members Hired After June 30, 2012

- Retirement Benefits - General employees' retirement benefits are determined as 1.75% of average final compensation multiplied by the years of credited service. General employees with ten years of credited service are eligible to retire at age 65. Employees with 30 years of credited service are eligible to retire at age 60.
- Disability and Death Benefits - Provisions for disability and death benefits generally remain the same except for ordinary death benefits. Ordinary death benefits are available to employees who were active at time of death with at least ten years of service. Ordinary death benefits consist of a lump sum payment of the member's contributions and accrued interest, or 50% Joint and Survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% Joint and Survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

Contributions

Contributions are governed by HRS Chapter 88 and may be amended through legislation. The employer rate is set by statute based on the recommendations of the ERS actuary resulting from an experience study conducted every five years. Since July 1, 2005, the employer contribution rate is a fixed percentage of compensation, including the normal cost plus amounts required to pay for the unfunded actuarial accrued liabilities. The contribution rates for fiscal year 2016 were 17.00%. Contributions to the pension plan from the State was \$373,881,000 for the fiscal year ended June 30, 2016, of which the Division's share was \$2,014,190.

The employer is required to make all contributions for noncontributory members. Contributory members hired prior to July 1, 2012 are required to contribute 7.8% of their salary. Hybrid members hired prior July 1, 2012 are required to contribute 6.0% of their salary. Hybrid members hired after June 30, 2012 are required to contribute 8.0% of their salary.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At June 30, 2016, the State reported a liability of approximately \$4.3 billion for its proportionate share of net pension liability, of which the Division's share was \$11,360,958. The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The State's proportion of the net pension liability was based on a projection of the State's long-term share of contributions to the pension plan relative to projected contributions of all participants, actuarially determined. At June 30, 2015, the State's proportion was 57.2380% which was a decrease of 1.2455% from its proportion measured as of June 30, 2014.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

There were no changes in other assumptions and inputs that affected the measurement of the total pension liability since the prior measurement date other than the investment return assumption. Fiscal year 2016 was the first year of the three-year phase-in of the investment return assumption. The investment return rate decreased beginning in fiscal year 2016 to 7.65% and will continue to decrease to 7.55% in fiscal year 2017 and to 7.50% in fiscal year 2018, and will remain at 7.50% thereafter. There were no changes between the measurement date, June 30, 2015, and the reporting date, June 30, 2016, that are expected to have a significant effect on the proportionate share of the net pension liability.

For the year ended June 30, 2016, the State recognized pension expense of approximately \$354,299,000, of which the Division's share was \$1,020,330. At June 30, 2016, the State reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources (amounts expressed in thousands):

| | <u>Deferred Outflows of Resources</u> | <u>Deferred Inflows of Resources</u> |
|--|---|--|
| Differences between expected and actual experience | \$ 41,650 | \$ (121,021) |
| Changes of assumptions | 102,682 | - |
| Net difference between projected and actual earnings on pension plan investments | 204,549 | (351,490) |
| Changes in proportion and differences between State contributions and proportionate share of contributions | 5,804 | (26,929) |
| State contributions subsequent to the measurement date | 476,076 | - |
| Total | <u>\$ 830,761</u> | <u>\$ (499,440)</u> |

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

The \$476,076,000 reported as deferred outflows of resources related to pensions resulting from State contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows (amounts expressed in thousands):

| Year ended June 30: | |
|---------------------|---------------------|
| 2017 | \$ (64,048) |
| 2018 | (64,048) |
| 2019 | (64,048) |
| 2020 | 52,228 |
| 2121 | (4,839) |
| | <u>\$ (144,755)</u> |

Actuarial Assumptions

The total pension liability in the June 30, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

| | |
|---------------------------|---|
| Inflation | 3.00% |
| Payroll growth rate | 3.50% |
| Investment rate of return | 7.65% per year, compounded annual including inflation |

The same rates were applied to all periods. There were no changes to ad hoc postemployment benefits including COLA.

Post-retirement mortality rates are based on Client Specific Tables and the 1994 US Group Annuity Mortality Statistic Tables. Pre-retirement mortality rates are based on the RP-2000 tables.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

The actuarial assumptions used in the June 30, 2015 valuation were based on the most recent experience study dated December 20, 2010. Between experience studies, the Board of Trustees of the Employees' Retirement System of the State of Hawaii elected to lower the investment return assumption effective with the June 30, 2015 valuation.

The long-term expected rate of return on pension plan investments was determined using a "top down approach" of the Bespoke Client-Constrained Simulation-based Optimization Model (a statistical technique known as "re-sampling with replacement" that directly keys in on specific plan-level risk factors as stipulated by the ERS Board) in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

| <u>Asset Class</u> | <u>Target Allocation</u> | <u>Long-Term Expected Real Rate of Return</u> |
|-----------------------|--------------------------|---|
| Domestic equity | 30.0% | 8.5% |
| International equity | 26.0% | 9.3% |
| Total Fixed-income | 20.0% | 3.1% |
| Real Estate | 7.0% * | 9.2% |
| Private Equity | 7.0% * | 11.9% |
| Real Return | 5.0% * | 6.7% |
| Covered Calls | <u>5.0%</u> | 7.7% |
| Total Investments | <u>100.0%</u> | |

*The real estate, private equity, and real return targets will be the percentage actually invested up to 7.0%, 7.0%, and 5.0%, respectively of the total fund. Changes in the real estate, private equity, and real return targets will be offset by an equal percentage change in the large cap domestic equity target.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

Discount Rate

The discount rate used to measure the net pension liability was 7.65%, a decrease from the 7.75% rate used at the prior measurement date. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that contributions from the State will be made at statutorily required rates, actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all period of projected benefit payments to determine the total pension liability.

Sensitivity of the State's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate

The following presents the State's proportionate share of the net pension liability calculated using the discount rate of 7.65%, as well as what the State's proportionate share of the net pension liability would be if it were calculated using a discount rate that is one percentage point lower (6.65%) or one percentage point higher (8.65%) than the current rate:

| | 1% Decrease (6.65%) | Discount Rate (7.65%) | 1% Increase (8.65%) |
|---|---------------------------|-----------------------------|---------------------------|
| State's proportionate share of the net pension liability | \$ 5,465,016 | \$ 4,314,246 | \$ 3,213,481 |

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

Pension Plan Fiduciary Net Position

The pension plan's fiduciary net position is determined on the same basis used by the pension plan. The ERS financial statements are prepared using the accrual basis of accounting under which expenses are recorded when the liability is incurred, and revenues are recorded in the accounting period in which they are earned and become measurable. Employer and member contributions are recognized in the period in which the contributions are due. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. Investment purchases and sales are recorded as of their trade date. Administrative expenses are financed exclusively with investment income.

There were no significant changes after the report measurement date. Detailed information about the pension plan's fiduciary net position is available in the separately issued ERS financial report. ERS's complete financial statements are available at <http://www.ers.ehawaii.gov>.

Payables to the Pension Plan

At June 30, 2016, the amount payable to the ERS was \$21,256,000.

Post-Retirement Health Care and Life Insurance Benefits

Plan Descriptions

The State provides certain health care and life insurance benefits to all qualified employees. Pursuant to Act 88, SLH of 2001, the State contributes to the EUTF, agent multiple-employer defined benefit plan that replaced the Hawaii Public Employees Health Fund effective July 1, 2003. The EUTF was established to provide a single delivery system of health benefits for state and county workers, retirees, and their dependents. The EUTF issues an annual financial report that is available to the public. That report may be obtained by writing to the EUTF at PO Box 2121, Honolulu, Hawaii 96805-2121.

For employees hired before July 1, 1996, the State pays the entire monthly contribution for employees retiring with ten years or more of credited service, and 50% of the base monthly contribution for employees retiring with fewer than ten years of credited service. A retiree can elect a family plan to cover dependents.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

For employees hired after June 30, 1996 but before July 1, 2001, and who retire with less than ten years of service, the State makes no contributions. For those retiring with at least ten years but fewer than 15 years of service, the State pays 50% of the base monthly contribution. For those retiring with at least 15 years but fewer than 25 years of service, the State pays 75% of the base monthly contribution. For those employees retiring with at least 25 years of service, the State pays 100% of the base monthly contribution. Retirees in this category can elect a family plan to cover dependents.

For employees hired on or after July 1, 2001, and who retire with less than ten years of service, the State makes no contributions. For those retiring with at least ten years but fewer than 15 years of service, the State pays 50% of the base monthly contribution. For those retiring with at least 15 years but fewer than 25 years of service, the State pays 75% of the base monthly contribution. For those employees retiring with at least 25 years of service, the State pays 100% of the base monthly contribution. Only single plan coverage is provided for retirees in this category. Retirees can elect family coverage but must pay the difference.

Cost

Effective July 1, 2006, the State implemented GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other than Pensions*. Statement No. 43 establishes accounting and financial reporting standards for plans that provide other postemployment benefits (OPEB) other than pensions. Statement No. 43 requires defined benefit OPEB plans that are administered as a trust or equivalent arrangements to prepare a statement of plan assets and a statement of changes in plan assets.

The reporting of active and retiree (including their respective beneficiaries) healthcare benefits provided through the same plan should separate those benefits for accounting purposes between active and retiree healthcare benefits. Accordingly, the State reports the retiree healthcare benefits as OPEB in conformity with Statement No. 43 and the active employee healthcare benefits as risk financing in conformity with GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, as amended.

The State is required by GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, to obtain an actuarial valuation every other year. Therefore, an actuarial valuation was performed for July 1, 2015.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

The State's base contribution levels to EUTF are established by statutes and the retiree is responsible to pay the difference if the base contribution is less than the cost of the monthly premium.

Prior to fiscal year 2014, the State's base contribution levels were tied to the pay-as you-go amounts necessary to provide current benefits to retirees. In fiscal year 2016, the State contributed \$249,827,000 in addition to amounts necessary to provide current benefits to retirees.

The State's annual OPEB cost for each plan is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters in Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

The actuarial methods and assumptions used to compute the ARC is disclosed in the notes to the financial statements of the State of Hawaii's comprehensive annual financial report. The Division's contribution for the years ended June 30, 2016, 2015, and 2014 were \$683,101, \$571,000 and \$554,000 respectively.

For the year ended June 30, 2016, total annual required contribution of \$698,051,000 was recognized for post-retirement health care and life insurance benefits by the State of which \$419,600,000 was paid in 2016 and a net OPEB obligation of \$4,335,863,574 remained as of June 30, 2016. The Division's share of the total annual required contribution was \$1,347,976, of which \$683,101 was paid in 2016. The estimated amounts were provided to the Division by the State of Hawaii Department of Accounting and General Services. The final amounts for post-retirement health care and life insurance benefits for the year ended June 30, 2016, for the annual required contribution, the annual contribution paid, and the net OPEB obligation remaining, are included in the State of Hawaii's Comprehensive Annual Financial Report.

On July 3, 2013, the Governor signed into law Act 268, SLH of 2013. Act 268 requires the EUTF to establish and administer separate accounts for each public employer for the purpose of receiving irrevocable employer contributions to prefund post-employment health and other benefit costs for retirees and their beneficiaries. It establishes the Hawaii EUTF Trust Fund Task Force to examine further steps to address the unfunded liability and requires all public employers to make annual required public employer contributions effective fiscal year 2014. Commencing fiscal year 2019, the annual public employer contributions shall be equal to the annual required

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

7. RETIREMENT BENEFITS (Continued)

Employees' Retirement System (Continued)

contribution, as determined by an actuary retained by the EUTF board. In any fiscal year, should an employer's contribution be less than the annual required public employer contribution, the difference shall be transferred to the appropriate trust account from a portion of all general excise tax revenues, for the State, or transient accommodations tax revenues, for the counties.

8. COMMITMENTS AND CONTINGENCIES

Accumulated Sick Leave Pay

Sick leave accumulates at the rate of one and three-quarters working days for each month of service without limit, but may be taken only in the event of illness and is not convertible to pay upon termination of employment. However, a state employee who retires or leaves government service in good standing with 60 days or more of unused sick leave is entitled to additional service credit in the ERS. The Division's accumulated sick leave as of June 30, 2016, was approximately \$4,057,000.

General Contingencies

The Division operates throughout the State of Hawaii. National and international events can have severe, adverse effects on economic conditions in Hawaii. The effects on the financial statements of the Division, from such changes in economic conditions, if any, are not presently determinable.

9. BLENDED COMPONENT UNIT - ALOHA TOWER DEVELOPMENT CORPORATION

Aloha Tower Development Corporation (ATDC), a blended component unit of the Division, is a state agency established under HRS Chapter 206J, primarily to redevelop the Aloha Tower complex in Honolulu. The complex encompasses Piers 5 to 23 of Honolulu Harbor. In September 1993, the State of Hawaii, Department of Transportation, Harbors Division (Harbors), entered into a lease with the ATDC which grants a leasehold interest in portions of the Aloha Tower complex to ATDC. ATDC is required annually to reimburse Harbors for any losses in revenue during the term of the lease caused by any action of ATDC or the developer of the

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

9. BLENDED COMPONENT UNIT - ALOHA TOWER DEVELOPMENT CORPORATION
(Continued)

Aloha Tower complex and to provide replacement facilities for maritime activities at no cost to Harbors.

ATDC subleased lands surrounded by Piers 8 and 9 and a portion of land surrounded by Pier 10 to a developer and entered into a capital improvements, maintenance, operations, and securities agreement with the developer and Harbors. Harbors continues to operate the harbor facilities at Piers 8, 9, and 10.

The sublease between the ATDC and the developer requires the developer to construct, at the developer's cost, various facilities as designated in the developer's proposal, including a Marketplace, and to reimburse Harbors for all losses in revenue and increased expenses which may be incurred by Harbors. The lease was subsequently amended and requires ATDC to pay \$225,000 each year to Harbors as a minimum base payment for losses in revenue related to fiscal years beginning July 1, 2005, that, subject to approval, may be reduced for certain expenses incurred by ATDC. The Amendment also requires an equity participation payment to be made in an amount of 50% of the difference between the total revenues and total operating expenses of ATDC for a fiscal year (the equity payment), provided that if the equity payment exceeds two and one-half times the actual operating expenses of ATDC for such fiscal year, ATDC must make a supplemental payment equal to 75% of the difference between the equity payment and the product of two and one-half times the actual operating expenses of ATDC. These payments were to be applied to reduce the amount owed to the Harbors for losses in revenue by ATDC prior to July 1, 2004. During the year ended June 30, 2016, there were no equity payments made.

During the year ended June 30, 2015, the State of Hawaii entered into a successor memorandum of understanding with ATDC and Hawaii Lifestyle Retail Properties, LLC (HLRP) whereby ATDC agreed to abate rent in the amount of \$1 million under the lease between ATDC and HLRP for the period retroactive to July 1, 2014 to June 30, 2015 in consideration for the construction of HLRP improvements at Aloha Tower Marketplace to create student and faculty residences and various university spaces for Hawaii Pacific University and to memorialize the understanding of the parties with respect to various aspects of its agreement. ATDC did not receive any rent revenue during this period and was unable to make any equity participation payments to Harbors. Rent collection resumed for the year ended June 30, 2016, resulting in collections of \$1 million for the year.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

9. BLENDED COMPONENT UNIT - ALOHA TOWER DEVELOPMENT CORPORATION
(Continued)

The successor memorandum of understanding also amended the obligations owed to Harbors, which arose from the original Aloha Tower Marketplace construction. The obligations are valued at \$3.5 million, depending upon when actual payments are made by the operator of Aloha Tower Marketplace within a six year timeframe ending June 2016. The amendment provides that in consideration of ATDC's issuance of any renewed leases, HLRP shall pay the Harbors Division the sum of \$1,750,000 on or before December 31, 2021.

At June 30, 2016, future minimum lease rent receipts approximate the following:

Years ending June 30,:

| | |
|-----------|----------------------|
| 2017 | \$ 1,000,000 |
| 2018 | 1,000,000 |
| 2019 | 1,000,000 |
| 2020 | 1,000,000 |
| 2021-2025 | 5,000,000 |
| 2026-2030 | 5,000,000 |
| 2031-2035 | 5,000,000 |
| 2036-2040 | 5,000,000 |
| 2041-2045 | 5,000,000 |
| 2046-2050 | 5,000,000 |
| 2051-2055 | 5,000,000 |
| 2056-2060 | <u>3,250,000</u> |
| Total | <u>\$ 42,250,000</u> |

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE FINANCIAL STATEMENTS (Continued)
JUNE 30, 2016

10. NOTE PAYABLE TO DEPARTMENT OF TRANSPORTATION, HARBORS DIVISION

During the year ended June 30, 2012, the administration of ATDC was assigned to the Department of Transportation by Act 152, Session Laws of Hawaii (SLH) 2011. Accordingly, the balance of an outstanding note payable from ATDC to Harbors of \$4,923,067 was recognized as a transfer to the Division during the year ended June 30, 2012 (See Note 9). During the year ended June 30, 2016, no payments were made on the balances of the outstanding note. As of June 30, 2016, the balance of the note amounted to \$3,760,567. The note does not require specific payments of interest. Supplemental payments to Harbors are required under an amendment to the sublease agreement between ATDC and the developer of land surrounded by Pier 10, which reduce the amount owed to the Harbors Division for losses in revenue by ATDC prior to July 1, 2004 (see Note 9).

**SUPPLEMENTARY FINANCIAL
INFORMATION**

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
BUDGETARY COMPARISON STATEMENT (NON-GAAP
BUDGETARY BASIS) - SPECIAL REVENUE FUND
For the Year Ended June 30, 2016

| | Budget | Actual | Variance - Favorable (Unfavorable) |
|--|---------------|----------------|--|
| Revenues | | | |
| Assessments | \$ 17,620,532 | \$ 17,668,916 | \$ 48,384 |
| Federal grant revenues | 25,625,696 | 3,620,277 | (22,005,419) |
| Other | 1,839,565 | 1,186,264 | (653,301) |
| Total revenues | 45,085,793 | 22,475,457 | (22,610,336) |
| Expenditures | | | |
| Personal services | 10,915,468 | 8,475,203 | 2,440,265 |
| Other | 34,542,209 | 11,088,488 | 23,453,721 |
| Total expenditures | 45,457,677 | 19,563,691 | 25,893,986 |
| Excess (deficiency) of Revenues over expenditures | (371,884) | 2,911,766 | 3,283,650 |
| Transfers to others | 371,884 | (6,766,154) | (7,138,038) |
| Excess (deficiency) of revenues Over expenditures and transfers | \$ - | \$ (3,854,388) | \$ (3,854,388) |

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended June 30, 2016

| Federal Grantor/Pass-Through Grantor Program Title | Federal CFDA Number | Grant Number | Program or Award Amount | Current Year Expenditure Amount |
|--|---------------------------|-----------------|-------------------------------|---------------------------------------|
| <u>Federal Transit Administration:</u> | | | | |
| Federal Transit - Capital Investment Grants: | | | | |
| Capital improvement grant to assist in financing the acquisition, construction, reconstruction, and improvement of facilities, rolling stock and equipment for use in mass transportation in urban areas | | | | |
| | 20.500 | | | |
| 10/01/13-09/30/14 | | HI-03-0038 | \$ 40,034,267 | \$ 3,863,847 |
| 10/01/09-09/30/10 | | HI-04-0004 | 5,699,400 | 541 |
| 10/01/11-09/30/12 | | HI-04-0009 | 3,955,000 | 1,315,000 |
| 10/01/11-09/30/12 | | HI-04-0010 | 233,129 | 7,841 |
| 10/01/12-09/30/13 | | HI-04-0013 | 3,440,000 | 1,240,000 |
| | | | <u>53,361,796</u> | <u>6,427,229</u> |
| | | | * | * |
| Formula Grants for Rural Areas: | | | | |
| Financial, operating, and technical assistance in providing public transportation services in non-urbanized areas | | | | |
| | 20.509 | | | |
| 10/01/11-09/30/12 | | HI-18-X030 | 2,127,899 | 12,583 |
| 10/01/12-09/30/13 | | HI-18-X031 | 2,675,805 | 723,630 |
| 10/01/14-09/30/15 | | HI-18-X032 | 1,737,944 | 242,663 |
| | | | <u>6,541,648</u> | <u>978,876</u> |
| | | | * | * |

* Denotes major program expenditures

(Continued)

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (Continued)
For the Year Ended June 30, 2016

| Federal Grantor/Pass-Through Grantor Program Title | Federal CFDA Number | Grant Number | Program or Award Amount | Current Year Expenditure Amount |
|--|---------------------------|-----------------|-------------------------------|---------------------------------------|
| <u>Federal Transit Administration (Continued):</u> | | | | |
| Enhanced Mobility of Seniors and Individuals with Disabilities: | | | | |
| Capital assistance grant to assist in providing transportation services for elderly and the handicapped | 20.513 | | | |
| 10/01/11-09/30/12 | | HI-16-0037 | \$ 892,501 | \$ 8,344 |
| | | | <u>892,501</u> | <u>8,344</u> |
| Job Access and Reverse Commute Program: | | | | |
| Capital planning and operating expenses for projects that transport low income individuals to and from jobs and activities related to employment, and for reverse commute projects | 20.516 | | | |
| 10/01/11-09/30/12 | | HI-37-X008 | 353,164 | 194 |
| | | | <u>353,164</u> | <u>194</u> |
| Metropolitan Transportation Planning and State and Non-Metropolitan Planning and Research | | | | |
| To assist in development of metropolitan and state transportation improvement programs, long-range transportation plans, and other technical studies in a program for a unified and officially coordinated Statewide Transportation system and Metropolitan Transportation system(s). | 20.505 | | | |
| 10/01/13-09/30/14 | | HI-80-0021 | 605,588 | 82,889 |
| | | | <u>605,588</u> | <u>82,889</u> |

* Denotes major program expenditures

(Continued)

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (Continued)
For the Year Ended June 30, 2016

| Federal Grantor/Pass-Through Grantor Program Title | Federal CFDA Number | Grant Number | Program or Award Amount | Current Year Expenditure Amount |
|--|---------------------------|-----------------|-------------------------------|---------------------------------------|
| <u>Federal Transit Administration (Continued):</u> | | | | |
| Bus and Bus Facilities Formula Program: | | | | |
| Provides capital funding to replace, rehabilitate and purchase buses and related equipment and to construct bus-related facilities | | | | |
| 10/01/13-09/30/14 | 20.526 | HI-34-0001 | \$ 815,833 | \$ 154,185 |
| | | | <u>815,833</u> | <u>154,185</u> |
| Total Federal Transit Administration | | | <u>62,570,530</u> | <u>7,651,717</u> |
| <u>Federal Highway Administration:</u> | | | | |
| Highway Planning and Construction: | | | | |
| Grant to assist in the development of an integrated, interconnected transportation system | | | | |
| 10/01/14-09/30/15 | 20.205 | SPR-0010(37) | 71,200 | 263 |
| 10/01/15-09/30/16 | | SPR-0010(38) | 431,200 | 191 |
| | | | <u>502,400</u> | <u>454</u> |
| Total Federal Highway Administration | | | <u>502,400</u> | <u>454</u> |
| Total Federal Financial Assistance | | | <u>\$ 63,072,930</u> | <u>\$ 7,652,171</u> |

* Denotes major program expenditures

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
JUNE 30, 2016

NOTE A - BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards (Schedule) includes the federal grant activity of the Department of Transportation, Administration Division and is presented on the accrual basis of accounting. The information in this Schedule is presented in accordance with the requirements of the Uniform Guidance. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the general purpose financial statements.

*Denotes major program expenditures, comprising 96% of total expenditure of federal awards of a low-risk auditee.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. In addition, pass-through entity identifying numbers are presented where available.

Of the federal expenditures presented in the Schedule, sub-recipients were provided federal awards as follows:

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (Continued)
For the Year Ended June 30, 2016

| Federal Grantor/Pass-Through Grantor Program Title | Federal CFDA Number | Agency or Pass-Through Number | Federal Expenditures Passed-Through |
|--|---------------------------|-------------------------------------|---|
| <u>Federal Transit Administration:</u> | | | |
| Federal Transit - Capital Investment Grants: | 20.500 | HI-03-0038 | \$ 3,863,847 |
| Capital improvement grant to assist in financing the | | HI-04-0004 | 541 |
| acquisition, construction, reconstruction, and improvement of | | HI-04-0009 | 1,315,000 |
| facilities, rolling stock and equipment for use in mass | | HI-04-0010 | 7,841 |
| transportation in urban areas | | HI-04-0013 | 1,240,000 |
| | | | * <u>6,427,229</u> |
| Formula Grants for Rural Areas: | | | |
| Financial, operating, and technical assistance in providing | 20.509 | HI-18-X030 | 5,000 |
| public transportation services in non-urbanized areas | | HI-18-X031 | 698,952 |
| | | HI-18-X032 | 242,663 |
| | | | * <u>946,615</u> |
| Metropolitan Transportation Planning and State and Non-Metropolitan Planning and Research | 20.505 | HI-80-0021 | <u>82,889</u> |
| To assist in development of metropolitan and State transportation improvement programs, long-range transportation plans, and other technical studies in a program for unified and officially coordinated Statewide Transportation system and Metropolitan Transportation system(s). Metropolitan Transportation system(s) | | | |
| Bus and Bus Facilities Formula Program: | | | |
| Provides capital funding to replace, rehabilitate and | 20.526 | HI-34-0001 | <u>154,185</u> |
| purchase buses and related equipment and to construct bus-related facilities | | | |
| Total pass-through of federal financial assistance | | | \$ <u><u>7,610,918</u></u> |

* Denotes major program expenditures

PART IV

INTERNAL CONTROL AND COMPLIANCE SECTION

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING
STANDARDS*

Office of the Auditor
State of Hawaii

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of State of Hawaii Department of Transportation, Administration Division (the “Division”) as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Division’s basic financial statements, and have issued our report thereon dated, January 31, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Division’s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Division’s internal control. Accordingly, we do not express an opinion on the effectiveness of the Division’s internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Division's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, including applicable provisions of the Hawaii Public Procurement Code (Chapter 103D of the Hawaii Revised Statutes) and procurement rules, directives and circulars, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance.

This report is intended solely for the information and use of the Office of the Auditor, management of the Division, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Eganis + Okun CPA's Inc.

Honolulu, Hawaii
January 31, 2017



INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

Office of the Auditor
State of Hawaii

Report on Compliance for Each Major Federal Program

We have audited the State of Hawaii Department of Transportation, Administration Division's (the "Division") compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Division's major federal programs for the year ended June 30, 2016. The Division's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Division's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Division's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Division's compliance.

Opinion on Each Major Federal Program

In our opinion, the Division complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2016.

Report on Internal Control over Compliance

Management of the Division, is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Division's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Division's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

This report is intended solely for the information and use of the Office of the Auditor, management of the Division, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Eganis + Kluenn CPAs Inc.

Honolulu, Hawaii
January 31, 2017

PART V

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
SCHEDULE OF PRIOR AUDIT FINDINGS AND QUESTIONED COSTS
For the Year Ended June 30, 2016

Status of Prior Year Comments

FINANCIAL STATEMENT FINDINGS

No matters were reported.

FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

No matters were reported.

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended June 30, 2016

SECTION I - SUMMARY OF AUDITORS' RESULTS

FINANCIAL STATEMENTS:

| | |
|---|----------------------|
| Type of auditors' report issued: | <u>Unmodified</u> |
| 1. Internal control over financial reporting: | |
| 2. Material weaknesses identified? | <u>No</u> |
| Reportable condition identified that is not considered to be material weakness | <u>None reported</u> |
| 3. Noncompliance material to financial statements noted? | <u>No</u> |

FEDERAL AWARDS:

| | |
|--|----------------------|
| 1. Internal control over major program: Material weaknesses identified? | <u>No</u> |
| Reportable condition identified that is not considered to be material weakness | <u>None reported</u> |
| 2. Type of auditors' report issued on compliance for major program: | <u>Unmodified</u> |
| 3. Any audit findings disclosed that are required to be reported in accordance with Uniform Guidance? | <u>None reported</u> |
| 4. Identification of major program: | |
| a. Federal Transit Cluster: CFDA No. 20.500 - Capital Investment Grants: Capital improvement grant to assist in financing the acquisition, construction, reconstruction, and improvement of facilities, rolling stock and equipment for use in mass transportation in urban areas and CFDA No. 20.509 - Formula Grants for Rural Areas: Financial, operating, and technical assistance in providing public transportation services to non- urbanized areas. | |
| b. Dollar threshold used to distinguish between type A and type B programs: | <u>\$750,000</u> |
| c. Auditee qualified as low-risk auditee? | <u>Yes</u> |

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)
For the Year Ended June 30, 2016

SECTION II - FINANCIAL STATEMENT FINDINGS

No matters were reported.

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

No matters were reported.

PART VI
CORRECTIVE ACTION PLAN

STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION, ADMINISTRATION DIVISION
CORRECTIVE ACTION PLAN
For the Year Ended June 30, 2016

A corrective action plan is not required since there were no audit findings and questioned costs reported for the year ended June 30, 2016.