Department of Health
State of Hawaii

Financial Statements
June 30, 2018
Together with Independent Auditor's Report

Submitted by

THE AUDITOR
STATE OF HAWAII

March 14, 2019

Mr. Leslie Kondo, State Auditor
Office of the Auditor
State of Hawaii

Dear Mr. Kondo:

This is our report on the financial audit of the Department of Health, the State of Hawaii (Department) as of and for the fiscal year ended June 30, 2018. Our audit was performed in accordance with the terms of our contract with the State of Hawaii and 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) and Government Auditing Standards, Audits of States, Local Governments, and Non-Profit Organizations.

OBJECTIVES OF THE AUDIT

The primary purpose of our audit was to form opinions on the fairness of the presentation of the Department's basic financial statements as of and for the fiscal year ended June 30, 2018, and to comply with the requirements of the Uniform Guidance. The objectives of the audit were as follows:

1. To provide a basis for an opinion on the fairness of the presentation of the Department's basic financial statements, including whether the schedule of expenditures of federal awards is fairly stated in relation to the financial statements.
2. To consider the Department's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the basic financial statements.
3. To perform tests on the Department's compliance with laws, regulations, contracts, and grants, including applicable provisions of the Hawaii Public Procurement Code (Chapter 103D and 103F, Hawaii Revised Statutes), that could have a direct and material effect on the determination of financial statement amounts.
4. To consider the Department's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinions on compliance and to test and report on internal control over compliance.
5. To provide a basis for opinions on the Department's compliance with applicable laws, regulations, contracts, and grants that could have a direct and material effect on each major federal program.

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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; *Government Auditing Standards,* issued by the Comptroller General of the United States; and the provisions of the Uniform Guidance. The scope of our audit included an examination of the transactions and accounting records of the Department for the fiscal year ended June 30, 2018.

ORGANIZATION OF THE REPORT

This report is presented in six parts as follows:

- Part I – The basic financial statements and related notes to the financial statements of the Department as of and for the fiscal year ended June 30, 2018, and our opinion on the basic financial statements.
- Part II – Our report on internal control over financial reporting and on compliance and other matters.
- Part III – Our report on compliance for each major program and internal control over compliance.
- Part IV – The schedule of findings and questioned costs.
- Part V – The summary schedule of prior audit findings.
- Part VI – Corrective action plan as provided by the Department.

We wish to express our sincere appreciation for the excellent cooperation and assistance extended by the officers and staff of the Department.

Sincerely,

Wilcox Choy

Wilcox Choy
Partner

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PART I

FINANCIAL SECTION

Independent Auditor's Report

Office of the Auditor
State of Hawaii

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Department of Health, State of Hawaii (Department), as of and for the fiscal year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Department'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.

Auditor's Responsibility

Our responsibility is to express opinions 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 from 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 auditor's 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.

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Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Department as of June 30, 2018, and the respective changes in financial position, and, where applicable, its cash flows, and budgetary comparisons for each major fund for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note 1, the financial statements of the Department are intended to present the financial position, the changes in financial position, and, where applicable, its cash flows and budgetary comparisons, of only that portion of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Hawaii that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State of Hawaii as of June 30, 2018, the changes in financial position, or, where applicable, its cash flows and budgetary comparisons, for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

As discussed in Note 1 to the basic financials statements, in 2018 the Department adopted Government Accounting Standards Board (GASB) Statement No. 75 (GASB 75), *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. As a result of adopting this standard, the Department has restated beginning net position for the fiscal year ended June 30, 2017. Our opinions are not modified with respect to this matter.

As discussed in Note 11 to the basic financial statements, the 2017 financial statements have been restated to correct a misstatement. We also audited the adjustment described in Note 11 that were applied to restate the 2017 financial statements. In our opinion, such adjustment is appropriate and has been properly applied. Our opinions are not modified with respect to this matter.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 11 through 22 be presented to supplement the basic financial statements. Such information, although not a 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 statements 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 Department's basic financial statements. The schedule of expenditures of federal awards, as required by the Office of Management and Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), is 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 relates 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 March 14, 2019 on our consideration of the Department'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 solely 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 the effectiveness of the Department's 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 Department's internal control over financial reporting and compliance.

KMH LLP

KMH LLP

Honolulu, Hawaii
March 14, 2019

Department of Health
State of Hawaii

Management Discussion and Analysis
June 30, 2018

This Management's Discussion and Analysis (MD&A) presents a narrative overview and analysis of the financial activities and performance of the Department of Health, State of Hawaii (the Department) during the fiscal year that ended on June 30, 2018. Please read it in conjunction with the Department's financial statements and the related notes to the basic financial statements (which follow this section). The following is a brief description of the contents of those three sections:

Overview of the Basic Financial Statements

This MD&A serves as an introduction to the Department's basic financial statements. The basic financial statements are comprised of three components: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the basic financial statements.

Government-Wide Financial Statements

The government-wide financial statements provide information about the Department's overall financial position and results of operations. These statements, which are presented on an accrual basis of accounting, consists of the statement of net position and the statement of activities.

The government-wide statements report information about the Department 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 Department's financial position, which assists in assessing the Department's economic condition at the end of the fiscal year. All of the current year revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid. The government-wide financial statements include two statements:

- The *Statement of Net Position* presents all of the Department's assets, deferred outflows, liabilities and deferred inflows, with the difference reported as "net position." Over time, increases and decreases in the Department's net position may serve as a useful indicator of whether the financial position of the Department is improving or deteriorating.
- The *Statement of Activities* presents information showing how the Department's net position changed during the most recent fiscal year.

The government-wide financial statements of the Department are further divided into two categories:

- *Governmental activities* - The activities in this section are primarily supported by State of Hawaii appropriations, funds from the tobacco settlement, beverage container deposit administrative fees, federal grants, taxes, and other fees.
- *Business-type activities* - These functions normally are intended to recover all or a significant portion of their costs through user's fees and charges to external users. These activities include the Department's two revolving loan funds.

Fund Financial Statements

The fund financial statements include the Department's: (1) governmental funds, for which activities are funded primarily from appropriations from the State of Hawaii, beverage container deposit program collections, mental health and substance abuse, and federal grants; (2) proprietary funds, which consist of revolving loan funds and are reported similar to business activities; and (3) fiduciary funds. The governmental funds are presented on the modified accrual basis of accounting. The proprietary and the fiduciary funds are presented on the accrual basis of accounting.

The fund financial statements provide more detailed information about the Department's most significant funds and not the Department as a whole. In these statements, the financial activities of the Department are recorded in individual funds. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Department uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. Funds are reported as a major fund or a non-major (other) fund. The Governmental Accounting Standards Board (GASB) issued Statement 34, *Basic Financial Statements - Management's Discussion and Analysis - for State and Local Governments*, which sets forth the minimum criteria for the determination of major funds. The non-major funds are combined in a column in the fund financial statements.

The fund financial statements also include the budgetary comparison statements, which include reconciliations for the general fund, Hawaii tobacco settlement special fund, deposit beverage container deposit special fund and mental health substance abuse special fund, comparing the excess of revenues over expenditures presented on a budgetary basis to the excess (deficiency) of revenues over expenditures presented in conformity with U.S. generally accepted accounting principles (GAAP) as presented in the governmental fund financial statements.

To reiterate, the Department has three types of funds:

- *Governmental funds* - Governmental funds are used to account for essentially the same functions reported in the governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of expendable resources as well as on the balances of expendable resources available at the end of the fiscal year.

  Because the focus of governmental funds is narrower than that of the government- wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. Both the governmental fund balance sheet and statement of revenues, expenditures, and changes in fund balance provide a reconciliation to facilitate comparison between governmental funds and governmental activities in the government-wide financial statements.

- *Proprietary funds* - Proprietary funds are used to report activities that operate more like those of commercial enterprises. They are known as enterprise funds because they charge fees for services provided to outsiders. They are used to report the same functions presented as business-type activities in the government-wide financial statements. The Department uses enterprise funds to account for the operations of its two revolving loan funds each of which are considered to be major funds of the Department.
- *Fiduciary funds* - The fiduciary funds account for net position held in a trustee or agent capacity for others. These funds are not reflected in the government-wide financial statements since these resources are not available to support the Department's programs.

Notes to the Basic Financial Statements

The Notes to Basic Financial Statements section provides additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the basic financial statements follow the basic financial statements.

Government-wide Financial Highlights

The Department's total net position increased from $1,025.4 million (as restated) as of June 30, 2017 to $1,063.4 million as of June 30, 2018, or by approximately $38.0 million. The total increase in net position was attributed to increases in the Department's governmental activities net position of $29.0 million and business-type activities' net position of $8.9 million during the year.

The Department's governmental activities reported an aggregate increase in net position of approximately $29.0 million during the year totaling $345.1 million at June 30, 2018. Note that this is based on the net position at June 30, 2017 of $316.1 million (as restated).

The Department's proprietary funds, consisting of two revolving loan funds, reported an increase in net position of $8.9 million for FY 2018. Total net position was $709.4 million (as restated) at June 30, 2017 compared to $718.3 million at June 30, 2018.

Government-Wide Financial Analysis

This section includes condensed government-wide financial information and analysis.

Condensed Statement of Net Position ($000)
June 30,

	Governmental Activities		Business-Type Activities		Total	
	2018	2017	2018	2017	2018	2017
Current assets	$ 390,904	$ 366,384	$ 239,687	$ 237,005	$ 630,591	$ 603,389
Capital assets	81,320	84,682	440	633	81,760	85,315
Loans receivable, noncurrent	-	-	489,945	483,277	489,945	483,277
Total assets	472,224	451,066	730,072	720,915	1,202,296	1,171,981
Deferred outflows of resources	-	-	2,196	2,287	2,196	2,287
Current liabilities	108,543	120,991	437	699	108,980	121,690
Long term liabilities	18,576	18,389	13,026	9,302	31,602	27,691
Total liabilities	127,119	139,380	13,463	10,001	140,582	149,381
Deferred inflows of resources	-	-	541	372	541	372
Net position						
Net investment in capital assets	81,320	84,682	440	633	81,760	85,315
Restricted	59,789	59,500	717,824	712,197	777,613	771,697
Unrestricted	203,996	167,504	-	-	203,996	167,504
Total net position	$ 345,105	$ 311,686	$ 718,264	$ 712,830	$ 1,063,369	$ 1,024,516

As noted earlier, changes in net position may serve over time as a useful indicator of the Department's financial position. As of June 30, 2018, the Department's total net position was approximately $1,063.4 million.

At June 30, 2018, in addition to equity in cash and cash equivalents in the state treasury approximating $554.3 million, the Department had total loans receivable from county governments in the amount of $530.3 million arising from its two revolving loan funds. The Department had total liabilities of $140.6 million at June 30, 2018 of which $14.1 million relates to accrued wages and employee benefits payable. Approximately $51.0 million in liabilities relate to vouchers and contracts payable. At June 30, 2018, restricted net position was $777.6 million. The restrictions arise from legal and contractual agreements.

Condensed Statement of Activities ($000)
June 30,

	Governmental Activities		Business-Type Activities		Total	
	2018	2017	2018	2017	2018	2017
Revenue:						
Program revenues:						
Charges for services	$ 22,538	$ 32,224	$ 5,870	$ 5,787	$ 28,408	$ 38,011
Operating grants and contributions	127,948	122,884	6,916	25,296	134,864	148,180
General revenues:						
State appropriated funds	475,880	459,877	-	-	475,880	459,877
Non-imposed fringe benefits	79,817	68,703	-	-	79,817	68,703
Hawaii tobacco settlement special fund	25,689	48,400	-	-	25,689	48,400
Environmental fees and taxes	51,014	50,682	-	-	51,014	50,682
Total revenues	782,886	782,770	12,786	31,083	795,672	813,853
Expenditures:						
General administration	47,766	45,862	-	-	47,766	45,862
Environmental health administration	64,749	79,157	7,612	10,738	72,361	89,895
Behavioral health services administration	338,979	314,113	-	-	338,979	314,113
Health resources administration	278,105	289,076	-	-	278,105	289,076
Total expenditures	729,599	728,208	7,612	10,738	737,211	738,946
Excess before transfers	53,287	54,562	5,174	20,345	58,461	74,907
Transfers	(24,263)	(15,502)	3,733	3,941	(20,530)	(11,561)
Change in net position	29,024	39,060	8,907	24,286	37,931	63,346
Net position:						
Restatement adjustments	4,394	(6,083)	(3,473)	(103)	921	(6,186)
Beginning of year	311,686	278,709	712,830	688,647	1,024,516	967,356
End of year	$ 345,104	$ 311,686	$ 718,264	$ 712,830	$1,063,368	$1,024,516

Governmental activities increased the Department's net position by $29.0 million in FY 2018, which was a 9.2 percent increase from FY 2017 (as restated). The overall increase in governmental activities is the result of higher revenues from several areas. General revenues of state appropriated funds increased by $16.0 million and non-imposed fringe benefits increased by $11.1 million.

Revenues of the Department's business-type activities, which decreased by $18.3 million from 2017, consist of the Department's environmental loan programs, one for water pollution control and the other for drinking water treatment. These revenues were generated from charges for services, program investment income, and federal assistance program funds as well as state matching funds. Charges for services consist primarily of administration loan fees and interest income on loans related to the Department's two revolving loan programs. The majority of the programs' investment income is from the Department's participation in the State Treasury Investment Pool System.

For the fiscal year ended June 30, 2018, business-type activities increased the Department's net position by $8.9 million to $718.3 million as compared to the fiscal year ended June 30, 2017 (as restated).

Total government-wide expenditures for FY 2018 were $737.2 million of which $729.6 million was for governmental activities. As compared to FY 2017, total government-wide expenditures were $738.9 million of which $728.2 million was for governmental activities. Overall, the Department is organized into four major administrations.

The Department’s Behavioral Health Services Administration expended 46.5 percent or $339.0 million of departmental funds with an increase of $24.9 million compared to FY 2017. This administration is responsible for providing available and coordinated mental health and substance abuse treatment and prevention programs. Programs within this administration are:

- Adult Mental Health Division (AMHD) that includes the Hawaii State Hospital and Community Mental Health Center Branches;
- Child and Adolescent Mental Health Division (CAMHD) which includes seven Family Guidance Centers and the Family Court Liaison Branches;
- Alcohol and Drug Abuse Division (ADAD) which plans for and purchases substance abuse prevention and treatment services for adolescents and adults; and
- Developmental Disabilities Division (DDD) that services disabled clients in Hawaii while addressing the conditions of the Makin Settlement.

The Department's Health Resources Administration expended approximately 38.1 percent of Department funds. FY 2018 expenses for this Administration decreased by $11.0 million compared to FY 2017. Major programs in this administration include:

- Chronic Disease Prevention & Health Promotion Division strives to promote wellness and improve the quality and years of life for Hawaii's people through effective prevention, detection and management of chronic diseases;
- Communicable Disease and Public Health Nursing Division (CDPHND) which strives to reduce morbidity and mortality from communicable diseases in Hawaii, to improve the health of individuals and communities, and to support the Medical Marijuana Registry program;
- Disease Outbreak Control Division which provides immunization and disease investigation services as well as provides emergency response to disease outbreaks and potential acts of bioterrorism;
- Emergency Medical Services and Injury Prevention System Branch (EMSIPSB) that includes the State's mandated Emergency Medical Services, which operates the State's emergency ambulance service in the four major counties, and the injury prevention program;
- Family Health Services Division (FHSD) that administers the State's Early Intervention program for children zero to three in compliance with the Federal Individual with Disabilities Education Act, Part C as well as serving children, youth and families through its three branches, namely, Children with Special Health Needs, Maternal and Child Health, and Women, Infants and Children;
- Office of Health Care Assurance (OHCA) which manages the state licensing and Federal certification of medical and health care facilities, agencies, and services provided throughout the State in order to ensure acceptable standards of care provided and to ensure compliance with State and Federal requirements. OHCA is also responsible for the rollout and management of the Medical Marijuana Dispensaries.

The Department's Environmental Health Administration is responsible for the management of the clean air, clean water, solid and hazardous waste, public health sanitation, vector control, and purity of food and drugs. It expended approximately 8.9 percent of the departmental funds with a decrease of $14.4 million expended versus FY 2017 on a government-wide basis. This administration also manages both the Water Pollution Control Revolving and the Drinking Water Treatment Revolving Loan Funds.

Finally, the Department's General Administration provides the overall leadership and oversight for the Department. It includes administrative support staff, three district health offices, and six administratively attached agencies. This administration expended approximately 6.5 percent of the departmental funds.

Governmental Funds Financial Analysis

The following table presents revenues and expenditures of the governmental funds for FY2018 and FY2017 ($000):

	2018	2017
Revenues:		
State general fund allotments	$ 475,880	$ 459,877
Intergovernmental	114,609	122,959
Hawaii tobacco settlement special fund	25,689	48,400
Deposit beverage container deposit special fund	24,174	23,642
Non-imposed fringe benefits	79,818	68,703
Taxes, fees, fines and other	63,716	59,892
Investment income	1,913	1,338
Total revenues	785,799	784,811
Expenditures:		
General administration	46,005	44,336
Environmental health	64,953	77,908
Behavioral health	337,270	313,639
Health resources	278,510	288,011
Total expenditures	726,738	723,894
Excess of revenues over expenditures before transfers	$ 59,061	$ 60,917

The governmental funds revenue consist of the Department's general fund, Hawaii tobacco settlement special fund (HTSSF), deposit beverage container deposit special fund (DBCDSF), intergovernmental (federal) funds, taxes, fees, fines and investment income.

During the fiscal year ended June 30, 2018, general fund revenues were $547.6 million, including $79.7 million for fringe benefits paid directly from the State general fund. General fund expenditures were $522.8 million.

In FY 2018, the DBCDSF earned revenues of $24.6 million from beverage container deposit administrative fees and unredeemed containers income. Of this amount received, $17.5 million in expenditures were paid to redemption centers or utilized to fund the program. The fund collected $47.0 million in deposits from distributors and repaid $32.0 million in deposits to consumers during FY 2018.

The proprietary funds consist of two funds: Water Pollution Control Revolving Fund (WPCRF) and Drinking Water Treatment Revolving Loan Fund (DWTRLF) and are reported in the government-wide statement of net position and statement of activities as business-type activities.

The WPCRF accounts for federal and state funds used to provide loans to county governments for the construction of wastewater treatment facilities and the repayment of principal, interest and fees from such loans and investment of such monies. During FY 2018, WPCRF received $0.2 million and $2.1 million of federal and state funds, respectively. WPCRF also disbursed $19.2 million in loan proceeds and collected $32.9 million in principal repayments in 2018. As compared to 2017, the fund collected $10.2 million and $2.2 million in federal and state contributions, respectively, and disbursed $46.6 million in loan proceeds and collected $30.1 million in principal payments.

The DWTRLF accounts for federal and state funds used to provide loans and other types of financial assistance to public water systems for drinking water infrastructure and the repayment of principal interest and fees from such loans and the investment of such monies. During FY 2018, DWTRLF received $4.7 million and $1.7 million of federal and state funds, respectively. DWTRLF also disbursed $41.4 million in loan proceeds and collected $18.4 million in principal repayments in 2018. As compared to 2017, the DWTRLF collected $13.1 million and $1.8 million in federal and state contributions, respectively, and disbursed $49.1 million in loan proceeds and collected $24.0 million in principal payments.

The Department accounts for funds held as an agent and/or trustee for certain individuals in the fiduciary funds.

Department of Health
State of Hawaii

Management Discussion and Analysis
June 30, 2018

Budgetary Analysis

The following budget information relates to the general fund, deposit beverage container deposit special fund and mental health substance abuse special fund for 2018:

	Budgeted Amounts ($000)		Actual on a Budgetary
	Original	Final	Basis ($000)
General fund			
Revenues	$ 477,410	$ 480,457	$ 474,411
Expenditures			
General administration	31,393	31,968	30,999
Environmental health	24,902	25,015	23,912
Behavioral health	285,813	286,657	284,892
Health resources	135,302	136,816	134,609
Deposit beverage container deposit special fund			
Revenues	71,174	71,225	56,957
Expenditures	71,174	71,225	60,881
Mental health substance abuse fund			
Revenues	11,610	11,610	7,453
Expenditures	11,610	11,610	6,318

The deposit beverage container program recognized revenues on a budgetary basis of $56.9 million, which is based on the actual number of containers sold. In fiscal year 2017, there were 966.5 million containers sold. The amount of containers sold decreased to 939.6 million in fiscal year 2018.

For the mental health substance abuse fund, the actual revenues received of $7.5 million in FY 2018 were $1.1 million more than the actual expenditures.

Capital Assets

As of June 30, 2018, the Department's governmental activities had invested approximately $81.3 million (net of accumulated depreciation) in a broad range of capital assets. See Note 4 to the Department's basic financial statements for a description of capital assets activities for the fiscal year ended June 30, 2018.

Capital Assets Governmental Activities June 30,
($000)

	2018	2017
Land	$ 1,018	$ 1,018
Land improvements	3,305	3,305
Buildings and building improvements	196,863	194,613
Furniture and equipment	26,493	25,868
Total	227,679	224,804
Accumulated depreciation	146,359	140,122
Total capital assets, net	$ 81,320	$ 84,682

Currently Known Facts, Decisions, or Conditions

Although the State's economy improved since last fiscal year, the State continued its cautious approach regarding expenditures. Therefore, the Department has continued to evaluate and monitor the statewide service delivery system of the adult mental health program in order to improve service delivery and to contain operational costs.

In FY 2018, AMHD serviced 8,328 clients as compared to the 9,925 clients serviced in FY 2017. AMHD's Crisis Line of Hawaii (formerly known as Access Line) continues to provide short term confidential counseling, information about available help, and mobile support services in a crisis.

In the developmental disabilities program, the number of clients increased by 110 clients in FY 2018. In FY 2018, the program served 2,956 clients in the home and community-based waiver program as compared to 2,846 clients served in FY 2017.

Further, the Federal Medical Assistance Percentage (FMAP) increased from 53.98 percent to 54.93 percent for the period October 2016 to September 2017. The FMAP decreased from 54.93 percent to 54.78 percent effective October 2017 to September 2018.

And lastly, the WPCRF executed a total of five loan agreements for $49.9 million during FY 2018. DWTRLF executed a total of one loan agreement for $16.0 million during FY 2018. Further, the WPCRF expects to execute a total of seven loan agreements in the amount of $124.7 million while the DWTRLF expects to execute a total of three loan agreements for $30.5 million in FY 2019.

Department of Health
State of Hawaii

Statement of Net Position
June 30, 2018

	Governmental Activities	Business-Type Activities	Total
Assets and Deferred Outflows of Resources			
Current Assets:			
Equity in Cash and Cash Equivalents and Investments in State Treasury	$ 358,017,801	$ 196,235,478	$ 554,253,279
Receivables:			
Due from State Treasury	-	1,306,753	1,306,753
Due from other State agencies	5,261,282	-	5,261,282
Accrued interest and loan fees	1,195,822	1,459,919	2,655,741
Accounts receivable	69,071	1,311	70,382
Due from Federal government	9,441,019	365,510	9,806,529
Tobacco settlement receivable	16,918,750	-	16,918,750
Current maturities of loans receivable	-	40,318,378	40,318,378
Total current assets	390,903,745	239,687,349	630,591,094
Loans Receivable, net of current maturities	-	489,945,299	489,945,299
Capital Assets, net of accumulated depreciation	81,320,162	439,637	81,759,799
Total assets	472,223,907	730,072,285	1,202,296,192
Deferred Outflows of Resources	-	2,195,569	2,195,569
Total assets and deferred outflows of resources	$ 472,223,907	$ 732,267,854	$ 1,204,491,761
Liabilities, Deferred Inflows of Resources, and Net Position			
Current Liabilities:			
Vouchers payable	$ 50,929,541	$ 81,453	$ 51,010,994
Accrued wages and employee benefits payable	13,908,401	226,680	14,135,081
Unearned revenue	4,383,872	-	4,383,872
Accrued vacation, current portion	10,576,016	128,289	10,704,305
Workers' compensation liability	806,891	-	806,891
Due to other State agencies	26,007,317	1,372	26,008,689
Beverage container deposits	1,931,164	-	1,931,164
Total current liabilities	108,543,202	437,794	108,980,996
Accrued Vacation, net of current portion	18,576,228	346,661	18,922,889
Net Pension Liability	-	6,187,787	6,187,787
Net Other Postemployment Benefits Liability	-	6,491,305	6,491,305
Total liabilities	127,119,430	13,463,547	140,582,977
Deferred Inflows of Resources	-	540,734	540,734
Net Position:			
Net investment in capital assets	81,320,162	439,637	81,759,799
Restricted for:			
Loans	-	717,823,936	717,823,936
Trust fund programs	6,542,034	-	6,542,034
Medicaid programs	53,246,681	-	53,246,681
Unrestricted	203,995,600	-	203,995,600
Total net position	345,104,477	718,263,573	1,063,368,050
Total liabilities, deferred inflows of resources, and net position	$ 472,223,907	$ 732,267,854	$ 1,204,491,761

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Statement of Activities
For the Fiscal Year Ended June 30, 2018

		Program Revenues		Net (Expenses) Revenue and Changes in Net Position		
Functions/Programs	**Expenses**	**Charges for Services**	**Operating Grants and Contributions**	**Governmental Activities**	**Business-Type Activities**	**Total**
Governmental Activities:						
General administration	$ 47,765,617	$ 1,652,809	$ 9,413,530	$ (36,699,278)	$ -	$ (36,699,278)
Environmental health administration	64,748,746	9,011,972	8,329,504	(47,407,270)	-	(47,407,270)
Behavioral health services administration	338,979,370	1,410,057	19,778,714	(317,790,599)	-	(317,790,599)
Health resources administration	278,105,617	10,463,587	90,426,583	(177,215,447)	-	(177,215,447)
Total governmental activities	729,599,350	22,538,425	127,948,331	(579,112,594)	-	(579,112,594)
Business-type Activities --						
Environmental Health Loan Programs	7,611,655	5,869,333	6,916,071	-	5,173,749	5,173,749
Total Department	$ 737,211,005	$ 28,407,758	$ 134,864,402	(579,112,594)	5,173,749	(573,938,845)
	General Revenues:					
	State general fund allotments, net			475,880,429	-	475,880,429
	Nonimposed employee fringe benefits			79,817,733	-	79,817,733
	Hawaii tobacco settlement special fund			25,688,624	-	25,688,624
	Tobacco tax			24,799,614	-	24,799,614
	Deposit beverage container fee			24,174,090	-	24,174,090
	Environmental response tax			1,290,770	-	1,290,770
	Advance glass disposal fee			748,684	-	748,684
	Total general revenues			632,399,944	-	632,399,944
	Transfers			(24,263,000)	3,733,000	(20,530,000)
	Change in net position			29,024,350	8,906,749	37,931,099
	Net Position at July 1, 2017, as previously reported			311,686,078	712,829,613	1,024,515,691
	Restatement Adjustments			4,394,049	(3,472,789)	921,260
	Net Position at July 1, 2017, as restated			316,080,127	709,356,824	1,025,436,951
	Net Position at June 30, 2018			$ 345,104,477	$ 718,263,573	$ 1,063,368,050

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Balance Sheet – Governmental Funds
June 30, 2018

	General	Deposit Beverage Container Deposit	Mental Health Substance Abuse	Other Governmental Funds	Total Governmental Funds
Assets:					
Equity in cash and cash equivalents and investments in State Treasury	$ 110,222,089	$ 41,941,940	$ 47,501,865	$ 158,351,907	$ 358,017,801
Due from other State agencies	-	-	1,213,470	4,047,812	5,261,282
Accrued interest receivable	-	323,066	274,532	598,224	1,195,822
Accounts receivable	-	69,071	-	-	69,071
Due from Federal government	-	-	-	9,441,019	9,441,019
Total assets	$ 110,222,089	$ 42,334,077	$ 48,989,867	$ 172,438,962	$ 373,984,995
Liabilities and Fund Balances					
Liabilities:					
Vouchers and contracts payable	$ 26,658,894	$ 2,670,665	$ 4,673	$ 21,595,309	$ 50,929,541
Accrued wages and employee benefits payable	11,032,771	32,987	-	2,842,643	13,908,401
Unearned revenue	-	-	1,213,470	8,431,146	9,644,616
Due to other State agencies	-	-	-	9,088,567	9,088,567
Beverage container deposits	-	1,931,164	-	-	1,931,164
Total liabilities	37,691,665	4,634,816	1,218,143	41,957,665	85,502,289
Fund Balances:					
Restricted:					
Medicaid programs	-	-	47,771,724	5,474,957	53,246,681
Trust fund programs	-	-	-	6,542,034	6,542,034
Committed:					
Behavioral health services	-	-	-	2,664,726	2,664,726
Environmental health	-	-	-	20,591,291	20,591,291
General administration	-	-	-	4,548,474	4,548,474
Health resources	-	-	-	71,624,327	71,624,327
Capital projects activities	-	-	-	11,164,754	11,164,754
Deposit beverage container program	-	37,699,261	-	-	37,699,261
Tobacco settlement program	-	-	-	8,191,728	8,191,728
Assigned:					
Behavioral health services	33,114,464	-	-	-	33,114,464
Environmental health	3,181,615	-	-	-	3,181,615
General administration	14,714,272	-	-	-	14,714,272
Health resources	21,520,073	-	-	-	21,520,073
Unassigned	-	-	-	(320,994)	(320,994)
Total fund balances	72,530,424	37,699,261	47,771,724	130,481,297	288,482,706
Total liabilities and fund balances	$ 110,222,089	$ 42,334,077	$ 48,989,867	$ 172,438,962	$ 373,984,995

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position
June 30, 2018

Total Fund Balances - Governmental Funds	$ 288,482,706
Amounts Reported for Governmental Activities in the Statement of Net Position are Different Because:	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds	81,320,162
Compensated absences reported in the statement of net position do not require the use of current financial resources and therefore are not reported as liabilities in the governmental funds	(29,152,244)
Workers' compensation liability reported in the statement of net position does not require the use of current financial resources and therefore is not reported as a liability in the governmental funds	(806,891)
Other financing sources not collected within 60 days and therefore not available for current financial resources are reported as unavailable revenues in the governmental funds.	5,260,744
Net Position of Governmental Activities	$ 345,104,477

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds
For the Fiscal Year Ended June 30, 2018

	General	Deposit Beverage Container Deposit	Mental Health Substance Abuse	Other Governmental Funds	Total Governmental Funds
Revenues:					
State-alloted appropriations	$ 467,872,429	$ -	$ -	$ 8,008,000	$ 475,880,429
Intergovernmental	-	-	-	114,609,433	114,609,433
Nonimposed employee fringe benefits	79,731,799	3,963	-	81,971	79,817,733
Taxes, fees, fines and other	-	-	83,950	63,631,380	63,715,330
Investment income	-	426,678	470,186	1,016,412	1,913,276
Hawaii tobacco settlement	-	-	-	25,688,624	25,688,624
Deposit beverage container deposit	-	24,174,090	-	-	24,174,090
Total revenues	547,604,228	24,604,731	554,136	213,035,820	785,798,915
Expenditures:					
General administration	35,200,994	-	-	10,804,169	46,005,163
Environmental health	30,571,844	17,512,858	-	16,867,997	64,952,699
Behavioral health services	313,965,203	-	1,637,038	21,667,851	337,270,092
Health resources	143,107,108	-	-	135,402,670	278,509,778
Total expenditures	522,845,149	17,512,858	1,637,038	184,742,687	726,737,732
Excess (deficiency) of revenues over (under) expenditures	24,759,079	7,091,873	(1,082,902)	28,293,133	59,061,183
Other Financing Sources (Uses):					
Transfers in	-	-	46,578,190	100,343,134	146,921,324
Transfers out	(7,110,396)	-	(43,108,674)	(124,779,682)	(174,998,752)
Total other financing sources (uses)	(7,110,396)	-	3,469,516	(24,436,548)	(28,077,428)
Net change in fund balances	17,648,683	7,091,873	2,386,614	3,856,585	30,983,755
Fund Balances at July 1, 2017, as previous reported	54,881,741	30,607,388	45,385,110	122,230,663	253,104,902
Restatement Adjustment	-	-	-	4,394,049	4,394,049
Fund Balances at July 1, 2017, as restated	54,881,741	30,607,388	45,385,110	126,624,712	257,498,951
Fund Balances at June 30, 2018	$ 72,530,424	$ 37,699,261	$ 47,771,724	$ 130,481,297	$ 288,482,706

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Reconciliation of the Statement of Revenues, Expenditures and
Changes in Fund Balances to the Statement of Activities
For the Fiscal Year Ended June 30, 2018

Net Change in Fund Balances - Total Governmental Funds	$	30,983,755
Amounts Reported for Governmental Activities in the Statement of Activities are Different Because:		
Governmental funds report capital outlays as expenditures, however, in the statement of activities, the cost of those assets are allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation exceeded capital outlays less dispositions for the year.		(3,362,158)
Increase in compensated absences reported in the statement of activities do not require the use of current financial resources and therefore not reported as expenditures in the governmental funds.		(141,419)
Increase in workers' compensation liability reported in the statement of activities do not require the use of current financial resources and therefore is not reported as expenditures in the governmental funds.		(20,510)
Other financing sources reported on the statement of activities that do not provide or use current financial resources and are reported as unavailable revenues in the governmental funds, net of prior year transfers recorded in the current period.		1,564,682
Change in Net Position - Governmental Activities	$	29,024,350

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

General Fund
Statement of Revenues and Expenditures - Budget and Actual
For the Fiscal Year Ended June 30, 2018

	Original	Final	Actual on Budgetary Basis	Variance Favorable (Unfavorable)
Revenues --				
State allotments	$ 477,410,321	$ 480,456,677	$ 474,411,073	$ (6,045,604)
Expenditures:				
General administration	31,393,316	31,967,579	30,998,959	968,620
Environmental health	24,902,133	25,015,937	23,911,714	1,104,223
Behavioral health services	285,812,556	286,656,724	284,891,619	1,765,105
Health resources	135,302,316	136,816,437	134,608,781	2,207,656
	477,410,321	480,456,677	474,411,073	6,045,604
Excess of revenues over expenditures	$ -	$ -	$ -	$ -

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Special Revenue Funds
Statement of Revenues and Expenditures - Budget and Actual
For the Fiscal Year Ended June 30, 2018

	Original	Final	Actual on Budgetary Basis: Deposit Beverage Container Deposit Special Revenue Fund	Actual on Budgetary Basis: Mental Health Substance Abuse	Variance Favorable (Unfavorable)
Revenues --					
Intergovernmental revenues:					
Deposit beverage container deposit	$ 71,174,271	$ 71,225,267	$ 56,956,777	$ -	$ (14,268,490)
Mental health substance abuse	11,610,000	11,610,000	-	7,452,930	(4,157,070)
	82,784,271	82,835,267	56,956,777	7,452,930	(18,425,560)
Expenditures:					
Environmental health					
Deposit beverage container deposit	71,174,271	71,225,267	60,880,981	-	10,344,286
Behaviorial health services					
Mental health substance abuse	11,610,000	11,610,000	-	6,317,646	5,292,354
	82,784,271	82,835,267	60,880,981	6,317,646	15,636,640
Excess (deficiency) of revenues over (under) expenditures	$ -	$ -	$ (3,924,204)	$ 1,135,284	$ (2,788,920)

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Statement of Net Position - Proprietary Funds
June 30, 2018

	Business-type Activities - Enterprise Fund		
	Water Pollution Control Revolving Fund	Drinking Water Treatment Revolving Loan Fund	Total
Assets and Deferred Outflows of Resources:			
Current assets:			
Equity in cash and cash equivalents and investments in State Treasury	$ 170,393,501	$ 25,841,977	$ 196,235,478
Loan fees receivable	353,923	640,866	994,789
Accrued interest receivable	325,841	107,509	433,350
Other accrued interest	31,780	-	31,780
Due from Federal Government	-	365,510	365,510
Due from State Treasury	1,101,722	205,031	1,306,753
Accounts receivable	-	1,311	1,311
Current portion of loans receivable	31,059,585	9,258,793	40,318,378
Total current assets	203,266,352	36,420,997	239,687,349
Loans receivable, net of current portion	321,166,074	168,779,225	489,945,299
Capital assets, net of accumulated depreciation	8,712	430,925	439,637
Total assets	524,441,138	205,631,147	730,072,285
Deferred outflows of resources	1,232,652	962,917	2,195,569
Total assets and deferred outflows of resources	$ 525,673,790	$ 206,594,064	$ 732,267,854
Liabilities, Deferred Inflows of Resources, and Net Position:			
Current liabilities--			
Accounts payable and other accrued liabilities	$ 215,954	$ 221,840	$ 437,794
Accrued vacation, net of current portion	194,330	152,331	346,661
Net pension liability	3,757,650	2,430,137	6,187,787
Net other postemployment benefits liability	3,706,469	2,784,836	6,491,305
Total liabilities	7,874,403	5,589,144	13,463,547
Deferred inflows of resources	51,736	488,998	540,734
Net Position:			
Net investment in capital assets	8,712	430,925	439,637
Restricted - expendable	517,738,939	200,084,997	717,823,936
Total net position	517,747,651	200,515,922	718,263,573
Total liabilities, deferred inflows of resources, and net position	$ 525,673,790	$ 206,594,064	$ 732,267,854

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Statement of Revenues, Expenses and Changes in Net Position - Proprietary Funds
For the Fiscal Year Ended June 30, 2018

	Business-type Activities-Enterprise Fund		
	Water Pollution Control Revolving Fund	Drinking Water Treatment Revolving Loan Fund	Total
Operating Revenues:			
Interest income from loans	$ 1,317,117	$ 471,522	$ 1,788,639
Administrative loan fees	1,721,338	2,359,356	4,080,694
Total revenues	3,038,455	2,830,878	5,869,333
Expenses:			
Administrative	2,433,539	1,629,244	4,062,783
State program management	-	1,060,129	1,060,129
Water protection	-	659,001	659,001
Principal forgiveness for SRF	-	1,808,542	1,808,542
Small system technical assistance	-	21,200	21,200
Total expenses	2,433,539	5,178,116	7,611,655
Operating income (loss)	604,916	(2,347,238)	(1,742,322)
Nonoperating Revenues and Expenses:			
State contributions	2,070,000	1,663,000	3,733,000
Federal contributions	208,306	4,722,027	4,930,333
Other interest income	1,614,257	342,569	1,956,826
Other income	15,321	13,591	28,912
Total nonoperating revenues and expenses	3,907,884	6,741,187	10,649,071
Change in net position	4,512,800	4,393,949	8,906,749
Net Position:			
Beginning of year, as previously reported	515,096,701	197,732,912	712,829,613
Restatement due to change in accounting principle	(1,861,850)	(1,610,939)	(3,472,789)
Beginning of year, as restated	513,234,851	196,121,973	709,356,824
End of year	$ 517,747,651	$ 200,515,922	$ 718,263,573

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Statement of Cash Flows - Proprietary Funds
For the Fiscal Year Ended June 30, 2018

	Business-type Activities - Enterprise Fund		
	Water Pollution Control Revolving Fund	**Drinking Water Treatment Revolving Loan Fund**	**Total**
Cash Flows from Operating Activities:			
Payments to employees	$ (1,788,859)	$ (1,811,066)	$ (3,599,925)
Payments to vendors	(128,055)	(1,314,306)	(1,442,361)
Net cash used in operating activities	(1,916,914)	(3,125,372)	(5,042,286)
Cash Flows from Noncapital Financing Activities:			
State contributions	2,070,000	1,663,000	3,733,000
Federal contributions	-	4,528,884	4,528,884
Net cash provided by noncapital financing activities	2,070,000	6,191,884	8,261,884
Cash Flows from Investing Activities:			
Principal repayments on loans	32,891,401	18,422,794	51,314,195
Disbursement of loan proceeds	(19,170,189)	(41,416,630)	(60,586,819)
Interest income from loans	1,354,879	479,905	1,834,784
Administrative loan fees	1,725,348	2,285,067	4,010,415
Other interest income	981,059	332,546	1,313,605
Net cash provided by (used in) investing activities	17,782,498	(19,896,318)	(2,113,820)
Net increase (decrease) in cash	17,935,584	(16,829,806)	1,105,778
Equity in Cash and Cash Equivalents and Investments in State Treasury:			
Beginning of year	152,457,917	42,671,783	195,129,700
End of year	$ 170,393,501	$ 25,841,977	$ 196,235,478
Reconciliation of Operating Income (Loss) to Net Cash Used in Operating Activities:			
Operating income (loss)	$ 604,916	$ (2,347,238)	$ (1,742,322)
Adjustments to reconcile operating income (loss) to net cash used in operating activities:			
Depreciation expense	1,237	201,161	202,398
Principal forgiveness for SRF	-	1,808,542	1,808,542
Interest income from loans	(1,317,117)	(471,522)	(1,788,639)
Administrative loan fees	(1,721,338)	(2,359,356)	(4,080,694)
In-kind contribution from the Environmental Protection Agency	208,306	80,969	289,275
Non-imposed fringe benefits	15,320	13,588	28,908
Change in assets, deferred outflows, liabilities, and deferred inflows:			
Due from State Treasury	(3,830)	-	(3,830)
Accounts receivable	-	2,156	2,156
Accounts payable and other accrued liabilities	(16,121)	(249,951)	(266,072)
Net deferred outflows/inflows of resources	359,507	244,101	603,608
Net pension liability	(92,775)	(86,542)	(179,317)
Net other postemployment benefits liability	44,981	38,720	83,701
Net cash used in operating activities	$ (1,916,914)	$ (3,125,372)	$ (5,042,286)

See accompanying notes to the basic financial statements.

Department of Health
State of Hawaii

Fiduciary Funds
Statement of Fiduciary Net Position - Agency Funds
June 30, 2018

Assets --		
Cash and cash equivalents	$	410,590
Total assets		410,590
Liabilities --		
Due to others		410,590
Total liabilities		410,590
Net Position	$	-

See accompanying notes to the basic financial statements.

1. Organization and Summary of Significant Accounting Policies

a. Financial Reporting Entity

The State of Hawaii, Department of Health (the Department), administers and oversees statewide personal health services, health promotion and disease prevention, mental health programs, monitoring of the environment, and the enforcement of environmental health laws. Federal grants received to support the State's health services and programs are administered by the Department.

The accompanying financial statements of the Department have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) prescribed by the Governmental Accounting Standards Board (GASB).

The Department is part of the executive branch of the State of Hawaii (State). The financial statements of the Department are intended to present the financial position and the changes in financial position and cash flows, where applicable, of only that portion of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2018, and the changes in its financial position and cash flows, and budgetary comparisons, where applicable, for the year then ended in conformity with GAAP. The State Comptroller maintains the central accounts for all State funds and publishes the State's Comprehensive Annual Financial Report (CAFR), which includes the Department's financial activities.

Act 262, Session Laws of Hawaii of 1996, established the Hawaii Health Systems Corporation (HHSC) as a public body corporate and politic and an instrumentality and agency of the State. HHSC consists of the state hospitals and was created to provide quality health care for all of the people in the State. HHSC commenced operations on July 1, 1996 and is administratively attached to the Department. However, HHSC is a component unit of the State and not the Department. HHSC's stand-alone financial statements are included in the State's CAFR but are not included in the Department's basic financial statements.

1. Organization and Summary of Significant Accounting Policies (continued)

b. Government-wide Financial Statements

The government-wide statements of net position and activities 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 imposed by the provider have been met.

Certain eliminations have been made as prescribed by GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, related to interfund activities, receivables, and payables. All internal balances have been eliminated except those representing balances between governmental and business-type activities, which are presented as internal balances and eliminated in the total department column when applicable. In the statement of activities, those transactions between governmental and business-type activities have not been eliminated. In addition, the fiduciary funds account for net position held in a trustee or agent capacity for others. These funds are not reflected in the government-wide financial statements since these resources are not available to support the Department's programs.

c. Fund Financial Statements

The governmental fund 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 Department considers revenues other than federal grants and assistance awards to be available if they are collected within 60 days of the end of the current fiscal year-end.

Federal grants and assistance awards made on the basis of entitlement periods are recorded as revenue 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 expenditure or expenses are incurred as of fiscal year-end and funds are available.

1. Organization and Summary of Significant Accounting Policies (continued)

c. Fund Financial Statements (continued)

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

The proprietary and 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.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. The principal operating revenues of the proprietary funds are interest income and administrative loan fees on loans made to county governments. Federal grants, state matching funds and interest income from sources other than loans are reported as nonoperating revenues. Principal forgiveness for loans are reported as operating expenses.

A description of the funds administered by the Department is as follows:

General Fund **-** The General Fund is the general operating fund of the Department. It is used to account for all financial resources except those required to be accounted for in another fund. The General Fund presented is a part of the State's General Fund and is limited to only those appropriations and obligations of the Department.

Special Revenue Funds **-** Special revenue funds are used to account for the proceeds of specific revenue sources (other than major capital projects) that are legally restricted to expenditures for specified purposes.

Capital Projects Funds **-** Capital projects funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds) and are included in Other Funds in the fund financial statements.

1. Organization and Summary of Significant Accounting Policies (continued)

c. Fund Financial Statements (continued)

The Department accounts for governmental fund balances in accordance with GASB Statement No. 54 (GASBS 54), *Fund Balance Reporting and Governmental Fund Type Definitions*. GASBS 54's hierarchical fund balance classification structure is based primarily on the extent to which a government is bound to follow constraints on how resources can be spent. Classifications include:

Nonspendable fund balance **-** amounts that are not in spendable form (such as inventory) or are required to be maintained intact;

Restricted **-** amounts constrained to specific purposes by their providers (such as creditors, grantors or other governments) through constitutional provisions, or by enabling legislation;

Committed **-** amounts constrained to specific purposes by a government itself, using its highest level of decision-making authority; to be reported as committed, amounts cannot be used for any other purpose unless the government takes the same highest level of action to remove or change the constraint;

Assigned **-** amounts a government intends to use for a specific purpose; intent can be expressed by the governing body or by an official or body to which the government delegates the authority;

Unassigned **-** amounts that are available for any purpose; positive amounts are reported only in the general fund.

When both restricted and unrestricted balances are available for use, it is the Department's policy to use restricted fund balance first, then unrestricted fund balance. Furthermore, committed fund balances are reduced first, followed by assigned amounts, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of those unrestricted classifications can be used.

1. Organization and Summary of Significant Accounting Policies (continued)

c. Fund Financial Statements (continued)

Proprietary Funds (Business-Type Activities)

Enterprise Funds - Enterprise funds are used to account for the activities for which the intent of management is to recover, primarily through user charges, the cost of providing goods or services to customers or where sound financial management dictates that periodic determination of results of operations are appropriate.

Fiduciary Funds

Agency Funds - Agency funds are used to account for cash collected and disbursed by the Department in a custodial capacity.

d. Equity in Cash and Cash Equivalents and Investments in State Treasury

The State Director of Finance is responsible for the safekeeping of cash in the State Treasury in accordance with State laws. The Director of Finance may invest any monies of the State which, in the Director's judgment, are in excess of the amounts necessary for meeting the immediate requirements of the State. Cash is pooled with funds from other State agencies and departments and deposited into approved financial institutions or in the State Treasury Investment Pool System. Funds in the investment pool accrue interest based on the average weighted cash balances of each account.

The State requires that depository banks pledge as collateral, government securities held in the name of the State for deposits not covered by federal deposit insurance.

GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, requires disclosures over common deposit and investment risks related to credit risk, interest rate risk, and foreign currency risk. Investments can be categorized by type, maturity and custodian to determine the level of interest rate, credit and custodial risk assumed by the Department. However, as all of the Department's monies are held in the State cash pool, the Department does not manage its own investments and the types of investments and related interest rate, credit and custodial risks are not determinable at the department level. The risk disclosures of the State's cash pool are included in the CAFR which may be obtained from the Department of Accounting and General Services' (DAGS) website: http://ags.hawaii.gov/accounting/annual-financial-reports/.

1. Organization and Summary of Significant Accounting Policies (continued)

e. Due from Other State Agencies

Receivables due from other State agencies consist of reimbursements from the Department of Human Services (DHS) for Medicaid payments that the Department makes to providers of health services. The Department is responsible to pay the State portion of the Medicaid claims, and DHS reimburses the Department for the Federal portion of the claims. The receivable of $5.3 million is comprised of various Medicaid rehabilitation option claims.

Payments made to providers and received from DHS for the Federal portion of the Medicaid claims are classified as expenditures and transfers in, respectively, for financial statement purposes.

f. Tobacco Settlement

In November 1998, the State settled its tobacco lawsuit as part of a nationwide settlement involving 46 other states and various tobacco industry defendants. Under the settlement, those tobacco companies that have joined in the Master Settlement Agreement will pay the State approximately $1.4 billion over a 27 year period. The Department is responsible for administering the Hawaii Tobacco Settlement Special Fund (HTSSF). The Department of Budget and Finance receives all tobacco settlement monies. The annual tobacco settlement monies are then transferred to the Department. Subsequently, the Department allocates and appropriates 100 percent of the funds to other State agencies and other entities in accordance with Act 118, SLH 2015. The Department receives annual payments on April 15 of each year for tobacco settlements earned for the preceding calendar year.

Effective during the year ended June 30, 2018, the State entered into an arbitration settlement with the Tobacco industry. As a result, arbitration credits of approximately $15.9 million will be applied against the annual tobacco settlement payments over the next five years.

The Department recognized approximately $25.7 million in tobacco settlement revenues during the year ended June 30, 2018. In accordance with GASB Technical Bulletin No. 2004-1, *Tobacco Settlement Recognition and Financial Reporting Entity Issues*, the Department has recorded a tobacco settlement receivable for $16.9 million in the statement of net position representing tobacco settlements earned for the period January 1, 2018 through June 30, 2018.

1. Organization and Summary of Significant Accounting Policies (continued)

g. Loans Receivable

Loans made to counties are funded by federal capitalization grants, State matching funds, repayments and investment interest income. Loan funds are disbursed to local agencies as they expend for the purposes of the loan and request reimbursement from the proprietary funds. Interest is calculated from the date that funds are advanced. After the final disbursement has been made, the payment schedule identified in the loan agreement is adjusted for the actual amounts disbursed and interest accrued during the project period. Certain capitalization grants allow for portions of loans to be forgiven upon satisfaction of certain requirements.

h. Administrative Loan Fees

The Department has implemented an administrative loan fee program to pay for the proprietary fund's administration, including employee salaries and benefits. The proprietary funds apply an administrative fee to all loans as provided for in Chapter 11-65 of the Hawaii Administrative Rules.

i. Capital Assets

Capital assets, which include buildings, furniture, and equipment, are reported in the applicable governmental or business-type activities in the government-wide financial statements and in the proprietary funds' financial statements. Capital assets are defined by the Department as those assets with estimated useful lives greater than one year and with an acquisition cost greater than:

	Minimum Capitalization Amount
Land	All
Land improvements	$ 100,000
Buildings and improvements	100,000
Furniture and equipment	5,000
Motor Vehicles	5,000

1. Organization and Summary of Significant Accounting Policies (continued)

i. Capital Assets (continued)

Such assets are recorded at historical cost if purchased or constructed. Donated assets are recorded at estimated fair value at the time received. Depreciation expense is recorded in the government-wide and proprietary funds' financial statements using the straight-line method over the estimated useful lives of the assets. Generally, the useful lives (in years) are as follows:

	Governmental-Type Activities	Business-Type Activities
Land improvements	15 years	5-100 years
Buildings and improvements	30 years	5-100 years
Furniture and equipment	7 years	1-25 years
Motor Vehicles	5 years	5-10 years

j. Unearned Revenue

Unearned revenues at the government-wide level and fund level arise when the Department receives resources before it has a legal claim to them. In subsequent periods, when the revenue recognition criteria is met, or when the Department has a legal claim to the resources, the liability for unearned revenue is removed from the statement of net position and balance sheet, and revenue is recognized. Unearned revenues at June 30, 2018 consisted primarily of Federal grant funds for which all requirements had not yet been met.

k. Due to Other State Agencies

Payables to other State agencies consist of funds allocated to other State agencies in accordance with the HTSSF. The amount allocated to other funds in accordance with the HTSSF is $23.4 million.

l. Beverage Container Deposits and Container Fees

Deposits of $0.05 are made by distributors to the deposit beverage container deposit special fund (DBCDSF) for each qualifying container sold. The DBCDSF maintains all deposits until the redemption centers claim reimbursement for the deposits paid to consumers. The DBCDSF maintains the deposits that are expected to be redeemed. In addition, deposits of $0.01 are made by the distributors to the DBCDSF for each qualifying container as a container fee.

1. Organization and Summary of Significant Accounting Policies (continued)

l. Beverage Container Deposits and Container Fees (continued)

Amounts paid to consumers are based on containers redeemed or a predetermined weight per type of container redeemed (i.e., aluminum, mixed plastics, etc.). These weights are determined based on the mix of containers redeemed and are reviewed when necessary. Management adjusts the deposit liability balance and unredeemed deposit revenue recognized based on the amount of deposits refunded in the first three months of the subsequent fiscal year related to deposits collected prior to year end. Deposits not refunded within the first three months of the subsequent fiscal year are recognized as revenue for the previous year.

According to Hawaii Revised Statute (HRS) 342G-104, any funds that accumulate in the DBCDSF shall be retained by the fund unless determined to be in excess by the Legislature.

m. Deferred Outflows and Inflows of Resources

Deferred outflows of resources represent a consumption of net position that applies to a future period and will not be recognized as an outflow of resources (expense) until that time. Deferred inflows of resources represent an acquisition of net position that applies to a future period and will not be recognized as an inflow of resources (revenue) until that time. The following is a breakdown of deferred outflows of resources and deferred inflows of resources as of June 30, 2018:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Related to Pensions	$ 1,765,178	$ (532,117)
Related to Other Postemployment Benefits	430,391	(8,617)
	$ 2,195,569	$ (540,734)

1. Organization and Summary of Significant Accounting Policies (continued)

n. Accrued Vacation

Vacation pay is accrued as earned by employees. Vacation pay can accumulate at the rate of one and three-quarters working days for each month of service up to 720 hours at calendar year-end and is convertible to pay upon termination of employment. Accrued vacation also includes compensatory time, as compensatory time is convertible to pay upon termination of employment. As accrued vacation does not require the use of current financial resources, it is not reported in the governmental funds balance sheet.

o. Accumulated Sick Leave

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 State's Employees' Retirement System (ERS). At June 30, 2018, accumulated sick leave was approximately $76.1 million.

p. Intrafund and Interfund Transactions

Significant transfers of financial resources between activities included 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 basic financial statements.

q. Use of Estimates

In preparing financial statements in conformity with GAAP, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

1. Organization and Summary of Significant Accounting Policies (continued)

r. Encumbrances

Encumbrance accounting, under which purchase orders and contractual commitments for the expenditure of funds are recorded in order to reserve that portion of the applicable appropriation, is employed in the governmental funds. Although appropriations generally lapse at year end, open encumbrances are reported as reservations of fund balances because the commitments will be honored when the goods or services are received. Encumbrances do not constitute expenditures or liabilities. Encumbrances at June 30, 2018 for the Department's governmental funds were approximately:

	Governmental Activities
General fund	$ 72,530,000
Deposit beverage container deposit special fund	13,421,000
Mental health substance abuse special fund	3,674,000
Other funds	4,680,000
	$ 94,305,000

s. Use of Restricted and Unrestricted Net Position

When an expense is incurred for which both restricted and unrestricted net position is available, the Department's policy is to apply restricted net position first.

t. Nonmonetary Transactions

The Department receives noncash awards for one of its federally funded programs. The Department expended approximately $16.1 million in vaccines during the fiscal year ended June 30, 2018.

u. Administrative Costs

DAGS assesses the Department's special funds centralized and administrative service fees, which are recorded as direct expenditures in the Department's funds. The DBCDSF is exempt from paying the central service fee assessed by DAGS under ACT 228, SLH 2013.

1. Organization and Summary of Significant Accounting Policies (continued)

v. 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 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.

w. Other Post-employment Benefits (OPEB)

For purposes of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the fiduciary net position of the Hawaii Employer-Union Health Benefits Trust Fund (EUTF) and additions to/deductions from the EUTF's fiduciary net position have been determined on the same basis as they are reported by the EUTF. For this purpose, benefit payments are recognized when due and payable in accordance with benefit terms. Investments are reported at their fair value.

x. New Accounting Pronouncement

In June 2017, GASB issued Statement No. 87, *Leases*. The objective of this Statement is to establish a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thus enhancing the relevance and consistency of information reported about the government's leasing activities. The provisions of this Statement are effective for the period beginning after December 15, 2019. The Department has not yet determined the effect this statement will have on its financial statements.

1. Organization and Summary of Significant Accounting Policies (continued)

y. Recently Adopted Accounting Pronouncement

During fiscal year 2018, the Department implemented GASB Statement No. 75 (GASB 75), *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. The Statement replaces GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and No. 57, *Other Post-Employment Benefits Measurements by Agent Employers and Agent Multiple-Employer Plans*. The Statement required the liability of employers for defined benefit OPEB to be measured as the portion of the present value of projected benefit payments to be provided to current active and inactive employees that is attributed to those employees' past periods of service, less the amount of the OPEB plan's fiduciary net position.

Adoption of GASB 75 has resulted in the restatement of the Department's fiscal year 2017 financial statements to reflect the reporting of a net OPEB liability and deferred outflows related to OPEB in accordance with the provisions of GASB 75. Additional disclosures are reflected in Note 9.

2. Budgeting and Budgetary Control

The Department follows these procedures in establishing the budgetary data reflected in the basic financial statements:

The Budget **-** Not less than 20 days before the State Legislature convenes in every odd-numbered year, the Governor submits to the State Legislature, and to each member thereof, a budget which contains the program and budget recommendation of the Governor for the succeeding biennium. The budget in general contains: the State program structure; statements of statewide objectives; financial requirements for the next biennium to carry out the recommended programs; a summary of State receipts and revenues in the last completed fiscal year; a revised estimate for the fiscal year in progress; and an estimate for the succeeding biennium.

Legislative Review **-** The State Legislature considers the Governor's proposed program and financial plan and budget, evaluates alternatives to the Governor's recommendations, adopts programs, and determines the State budget. It may, from time to time, request the Department of Budget and Finance and any agency to conduct such analysis of programs and finances as will assist in determining the State's program and financial plan and budget.

2. Budgeting and Budgetary Control

Program Execution - Except as limited by policy decisions of the Governor, appropriations by the State Legislature, and other provisions of law, the agencies responsible for the programs administer the programs and are responsible for their proper management. The appropriations by the State Legislature for a biennium are allocated between the two fiscal years of the biennium in the manner provided in the budget or appropriations act and as further prescribed by the Director of Finance. No appropriation transfers or changes between programs or agencies can be made without legislative authorization. Authorized transfers or changes, when made, should be reported to the State Legislature.

Budgetary control is maintained at the appropriation line item level established in the appropriation acts. Budgets are adopted for the Department's funds and are prepared on the cash basis of accounting, except for the encumbrance of purchase orders and contract obligations (basis difference), which is a basis of accounting other than GAAP.

Since budgetary basis differs from GAAP, budget and actual amounts in the budgetary comparison statements are presented on the budgetary basis. A reconciliation of revenues over expenditures (expenditures over revenues) on a budgetary basis at June 30, 2018, to excess of revenues over expenditures presented in conformity with GAAP follows:

	General	Deposit Beverage Container Deposit	Mental Health Substance Abuse	Total
Excess of revenues over expenditures (expenditures over revenues) - actual on a budgetary basis	$ -	$ (3,924,204)	$ 1,135,284	$ (2,738,920)
Reserve for encumbrances at year end	72,530,427	13,421,049	3,674,364	89,625,840
Expenditures for liquidation of prior year's encumbrances	(55,357,423)	(5,122,538)	(3,102,430)	(63,582,391)
Accruals and other adjustments	7,586,075	2,717,566	(2,790,120)	7,513,521
Total change in fund balances	$ 24,759,079	$ 7,091,873	$ (1,082,902)	$ 30,768,050

3. Loans Receivable

At June 30, 2018, the proprietary funds loans receivable consisted of loans to county governmental units for the water pollution control and drinking water treatment programs. The loans require annual, semi-annual or quarterly payments, including interest at 0.00% to 3.02%, commencing not later than one year after project completion, notice to proceed, final loan disbursement, or three years after loan agreement date. Final payment is due not later than twenty years after project completion. During the year ended June 30, 2018, approximately $1.8 million in loans was forgiven. All loans and advances forgiven were in accordance with required conditions. Accrued interest receivable on the loans amounted to approximately $433,000 at June 30, 2018.

The following is a schedule of principal payments due on loans for projects completed or in progress as of June 30, 2018:

Year ending June 30,	
2019	$ 40,318,378
2020	40,358,300
2021	41,016,597
2022	40,942,761
2023	39,664,699
2024-2028	184,237,187
2029-2033	105,557,892
2034-2039	38,155,251
2040	12,612
	$ 530,263,677

As of June 30, 2018, the Department's proprietary funds were committed under existing loan agreements to the following counties:

	Water Pollution Control Revolving Fund	Drinking Water Treatment Revolving Loan Fund	Total
City & County of Honolulu	$ 32,333,482	$ 5,000,000	$ 37,333,482
County of Maui	17,260,684	5,000,000	22,260,684
County of Hawaii	15,282,850	-	15,282,850
County of Kauai	3,700,000	-	3,700,000
	$ 68,577,016	$ 10,000,000	$ 78,577,016

4. Capital Assets

Capital asset activity for governmental and business-type activities for the year ended June 30, 2018 was as follows:

	Balance July 1, 2017	Additions	Disposals	Balance June 30, 2018
Governmental Type Activities:				
Depreciable Assets:				
Land improvements	$ 3,304,766	$ -	$ -	$ 3,304,766
Building and improvements	194,613,538	2,249,746	-	196,863,284
Furniture and equipment	25,868,179	2,048,236	(1,423,469)	26,492,946
Total depreciable assets	223,786,483	4,297,982	(1,423,469)	226,660,996
Less Accumulated Depreciation:				
Land improvements	(2,404,547)	(96,123)	-	(2,500,670)
Building and improvements	(115,780,797)	(5,725,296)	-	(121,506,093)
Furniture and equipment	(21,936,899)	(1,739,020)	1,323,768	(22,352,151)
Total accumulated depreciation	(140,122,243)	(7,560,439)	1,323,768	(146,358,914)
Non-Depreciable Assets -- Land	1,018,080	-	-	1,018,080
Governmental activities capital assets, net	$ 84,682,320	$ (3,262,457)	$ (99,701)	$ 81,320,162
Business-Type Activities				
Depreciable Assets -- Furniture and Equipment	$ 2,595,384	$ 8,898	$ (34,208)	$ 2,570,074
Less Accumulated Depreciation -- Furniture and Equipment	(1,962,247)	(202,398)	34,208	(2,130,437)
Business-type activities capital assets, net	$ 633,137	$ (193,500)	$ -	$ 439,637
Total Department capital assets, net	$ 85,315,457	$ (3,455,957)	$ (99,701)	$ 81,759,799

4. Capital Assets (continued)

Current period depreciation expense was charged to functions as follows:

	Governmental Activities	Business-Type Activities	Total
General administration	$ 1,914,584	$ -	$ 1,914,584
Environmental health	637,857	202,398	840,255
Behavioral health services	2,476,435	-	2,476,435
Health resources	2,531,563	-	2,531,563
Total	$ 7,560,439	$ 202,398	$ 7,762,837

5. Accrued Vacation

The changes to the accrued vacation liability during the year ended June 30, 2018 were as follows:

	Governmental Activities	Business-Type Activities	Total
Balance at July 1, 2017	$ 29,010,825	$ 474,066	$ 29,484,891
Increase	14,569,908	178,382	14,748,290
Decrease	(14,428,489)	(177,498)	(14,605,987)
Balance at June 30, 2018	29,152,244	474,950	29,627,194
Less: Current portion	10,576,016	128,289	10,704,305
Noncurrent portion	$ 18,576,228	$ 346,661	$ 18,922,889

6. Beverage Container Deposits

The changes to the beverage container deposit liability during the year ended June 30, 2018 were as follows:

Balance at July 1, 2017	$ 1,698,494
Increase: Deposits received from distributors	46,976,905
Decrease: Payments made to redemption centers, net of refunds	(31,997,668)
Decrease: Unredeemed deposits recognized as revenue	(14,746,567)
Balance at June 30, 2018	$ 1,931,164

7. Changes in Assets and Liabilities of the Agency Funds

The agency funds are purely custodial (assets equal liabilities) and thus do not involve the measurement of results of operations. The changes in assets and liabilities of the agency funds for the fiscal year ended June 30, 2018, were as follows:

	Balance July 1, 2017	Additions	Deductions	Balance June 30, 2018
Assets --				
Cash	$ 437,041	$ 126,318	$ 152,769	$ 410,590
Liabilities --				
Due to others	$ 437,041	$ 126,318	$ 152,769	$ 410,590

8. Non-imposed Employee Fringe Benefits

Non-imposed employee fringe benefits related to general and State special fund salaries are funded by the State. These costs, totaling approximately $79.8 million for the fiscal year ended June 30, 2018, have been reported as revenues and expenditures of the Department's general and State special revenue funds.

Payroll fringe benefit costs related to Federally-funded salaries are not funded by the State and are recorded as expenditures in the Federal special revenue funds.

9. Employee Benefit Plans

a. Employees' Retirement System

i. 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 that administers 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 publicly available annual financial reports that can be obtained at ERS' website: http://www.ers.ehawaii.gov.

ii. 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.

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

ii. Benefits Provided (continued)

The following summarizes the provisions relevant to the largest employee groups of the respective membership class. Retirement benefits for certain groups, such as police officers, firefighters, some investigators, sewer workers, judges, and elected officials, vary from general employees.

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 the 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.

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

ii. Benefits Provided (continued)

Contributory Plan for Employees 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. Police officers and firefighters' retirement benefits are determined using the benefit multiplier of 2.5% for qualified service, up to a maximum of 80% of average final compensation. Police officers and firefighters with five years of credited service are eligible to retire at age 55. Police officers and fire fighters with 25 years of credited service are eligible to retire at any age, provided the last five years is service credited in these occupations.

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.

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

ii. Benefits Provided (continued)

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.

Contributory Plan for Employees 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. Police officers and firefighters' retirement benefits are determined using the benefit multiplier of 2.25% for qualified service, up to a maximum of 80% of average final compensation. Police officers and firefighters with ten years of credited service are eligible to retire at age 60. Police officers and firefighters with five years of credited service are eligible to retire at age 55. Police officers and fire fighters with 25 years of credited service are eligible to retire at any age, provided the last five years is service credited in these occupations.

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% 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 service for police officers and firefighters and are payable immediately, without an actuarial reduction, at a minimum of 30% of average final compensation.

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

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

ii. Benefits Provided (continued)

<u>*Hybrid Plan for Employees Hired Prior to July 1, 2012*</u>

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.

Death Benefits - For service-connected deaths, the designated 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 dependent 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 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

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

ii. Benefits Provided (continued)

Hybrid Plan for Employees 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. Sewer workers, water safety officers, and emergency medical technicians may retire with 25 years of credited service at age 55.

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.

iii. 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 2018 were 25.00% for police officers and firefighters and 17.00% for all other employees. Contributions to the pension plan from the Department were $382,696 for the fiscal year ended June 30, 2018.

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

iii. Contributions (continued)

On May 18, 2017, the Governor signed into law Act 17 SLH 2017. Per Act 17, future employer contributions from the State and counties are expected to increase pursuant to a phased-in contribution rate increase over four years beginning July 1, 2017. The rate for all employees, except for police officers and firefighters, increases to 18.00% on July 1, 2017; 19.00% on July 1, 2018; 22.00% on July 1, 2019; and 24.00% on July 1, 2020.

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, except for police officers and firefighters who are required to contribute 12.2% of their salary. Contributory members hired after June 30, 2012 are required to contribute 9.8% of their salary, except for police officers and firefighters who are required to contribute 14.2% of their salary. Hybrid members hired prior to 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.

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

At June 30, 2018, the Department reported a liability of $6,187,787 for its proportionate share of net pension liability of the State. The net pension liability was measured as of June 30, 2017, 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, 2017 and 2016, the Department's proportion of the State share was 0.09%.

There was no change in actuarial assumptions as of June 30, 2016 to June 30, 2017. There were no changes in assumptions between the measurement date, June 30, 2017, and the reporting date, June 30, 2018, that are expected to have a significant effect on the proportionate share of the net pension liability.

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

iv. Net Pension Liabilities, Pension Expense, and Deferred Outflows and Inflows of Resources, Related to Pensions (continued)

For the year ended June 30, 2018, the Department recognized pension expense of $885,912. At June 30, 2018, the Department reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 133,348	$ (70,744)
Changes in assumptions	1,009,334	-
Net difference between projected and actual earnings on pension plan investments	207,683	(445,837)
Changes in proportion and difference between Department contributions and proportionate share of contributions	32,117	(15,536)
Department contributions subsequent to the measurement date	382,696	-
	$ 1,765,178	$ (532,117)

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

iv. Net Pension Liabilities, Pension Expense, and Deferred Outflows and Inflows of Resources, Related to Pensions (continued)

The $382,696 reported as deferred outflows of resources related to pensions resulting from Department contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the fiscal year ended June 30, 2018. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Fiscal Year Ending June 30,	
2019	$ 643,883
2020	94,825
2021	79,753
2022	31,260
2023	644
Total	$ 850,365

v. Actuarial Assumptions

The total pension liability in the June 30, 2017 actuarial valuation was determined using the following actuarial assumptions adopted by the Board of Trustees of the Employees' Retirement System of the State of Hawaii, on December 12, 2016, based on the most recent experience study dated July 5, 2016:

Inflation	2.50%
Payroll growth rate	3.50%
Investment rate of return	7.00% per year, compounded annual including inflation

There were no changes to ad hoc postemployment benefits including COLA.

Post-retirement mortality rates are based on the 2016 Public Retirees of Hawaii mortality table with adjustments based on generational projections of the BB projection table for 2016 and full generational projections in future years. Pre-retirement mortality rates are based on multiples of RP-2014 mortality table based on the occupation of the member.

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

v. Actuarial Assumptions (continued)

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 a 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 geometric real rates of return for each major asset class are summarized in the following table:

Strategic Allocation (risk-based classes)	Target Allocation	Long-term Expected Geometric Rate of Return
Broad growth	63.0%	5.80%
Principal protection	7.0%	0.20%
Real return	10.0%	3.60%
Crisis risk offset	20.0%	3.10%
	100.0%	

Discount Rate **-** The discount rate used to measure the net pension liability was 7.00%, the same 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 periods of projected benefit payments to determine the total pension liability.

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

v. Actuarial Assumptions (continued)

Sensitivity of the Department's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate **-** The following presents the Department's proportionate share of the net pension liability calculated using the discount rate of 7.00%, as well as what the Department's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (6.00%) or 1-percentage point higher (8.00%) than the current rate:

	1% Decrease (6.00%)	Discount Rate (7.00%)	1% Increase (8.00%)
Department's proportionate share of the net pension liability	$ 8,552,685	$ 6,187,787	$ 4,985,777

vi. 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.

9. Employee Benefit Plans (continued)

a. Employees' Retirement System (continued)

vi. Pension Plan Fiduciary Net Position (continued)

The State's comprehensive annual financial report contains further disclosures related to the State's proportionate share of the net pension liability and employer pension contributions.

vii. Payables to the Pension Plan

At June 30, 2018, there was no payable to the ERS.

b. Deferred Compensation Plan

The State offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all State 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 an unforeseeable emergency.

All plan assets are held in a trust fund to protect them from claims of general creditors. The State has no responsibility for loss due to the investment or failure of investment of funds and assets in the plan, but has the duty of due care that would be required of an ordinary prudent investor.

c. Post-Employment Healthcare and Life Insurance Benefits

i. Plan Description

The State provides certain health care and life insurance benefits to all qualified employees. Pursuant to Act 88, Session Laws of Hawaii (SLH) of 2001, the state contributes to the Hawaii Employer Union Health Benefits Trust Fund (EUTF), an agent multiple employer defined benefit plan, 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.

9. Employee Benefit Plans (continued)

c. Post-Employment Healthcare and Life Insurance Benefits (continued)

i. Plan Description (continued)

State Policy - The actuarial valuation of the EUTF does not provide OPEB information by department or agency. Accordingly, the State's policy on the accounting and reporting for OPEB is to allocate a portion of the State's Annual Required Contribution (ARC), interest, and any adjustment to the ARC, to component units and proprietary funds that are reported separately in stand alone departmental financial statements or in the State's CAFR. The basis for the allocation is the proportionate share of contributions made by each component unit or proprietary fund for retiree health benefits.

ii. Contributions

Contributions are governed by HRS Chapter 87A and may be amended through legislation. Contributions to the OPEB plan from the Department was approximately $430,000 for the fiscal year ended June 30, 2018. The employer is required to make all contributions for members.

iii. Net OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

At June 30, 2018, the Department reported a liability of $6,491,305 for its proportionate share of net OPEB liability of the State. The net OPEB liability was measured as of June 30, 2017, and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of that date. The State's proportion of the net OPEB liability was based on a projection of the State's long-term share of contributions to the EUTF relative to projected contributions of all participants, actuarially determined. The Department's proportion of the net OPEB liability was based on an allocation of the State's net OPEB liability based on the proportionate share of qualified payroll. At June 30, 2017 and 2016, the Department's proportion of the State's share was 0.07%.

There were no changes in assumptions between the measurement date, June 30, 2017, and the reporting date, June 30, 2018, that are expected to have a significant effect on the proportionate share of the net OPEB liability.

See Note 11 for discussion on the impact of implementing GASB 75.

9. Employee Benefit Plans (continued)

c. Post-Employment Healthcare and Life Insurance Benefits (continued)

iii. Net OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB (continued)

For the year ended June 30, 2018, the Department recognized OPEB expense of $435,166. At June 30, 2018, the Department reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ -
Changes in assumptions	-	-
Net difference between projected and actual earnings on investments	-	(8,617)
Department contributions subsequent to the measurement date	430,391	-
	$ 430,391	$ (8,617)

The $430,391 reported as deferred outflows of resources related to OPEB resulting from Department contributions subsequent to the measurement date will be recognized as a reduction of the net OPEB liability in the fiscal year ended June 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows:

Fiscal Years Ending June 30,	Amount
2019	$ (1,723)
2020	(1,723)
2021	(1,723)
2022	(1,723)
2023	(1,725)
Total	$ (8,617)

9. Employee Benefit Plans (continued)

c. Post-Employment Healthcare and Life Insurance Benefits (continued)

iv. Actuarial Assumptions

The total OPEB liability in the June 30, 2017 actuarial valuation was determined using the following actuarial methods and assumptions, applied to all periods included in the measurement, unless otherwise specified:

Actuarial cost method	Entry age normal
Discount rate	7.00%
Inflation	2.50%
Salary increases	3.50% to 7.00%, including inflation
Investment rate of return	7.00%, net of investment expenses, including inflation
Demographic assumptions	Based on the experience study covering the five year period ended June 30, 2015, as conducted for the ERS
Mortality	System-specific mortality tables utilizing scale BB to project generational mortality improvement
Healthcare trend rates:	
PPO*	Initial rates of 6.60%, 6.60%, and 9.00%; declining to a rate of 4.86% after 14 years
HMO*	Initial rate of 9.00%; declining to a rate of 4.86% after 14 years
Part B & BMC	Initial rates of 2.00% and 5.00%; declining to a rate of 4.70% after 14 years
Dental	3.50%
Vision	2.50%
Life insurance	0.00%

* Blended rates for medical and prescription drug.

9. Employee Benefit Plans (continued)

c. Post-Employment Healthcare and Life Insurance Benefits (continued)

iv. Actuarial Assumptions (continued)

The long-term expected rate of return on EUTF's investments was determined using a building-block method 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:

Asset Class	Target Allocation	Long-term Expected Rate of Return
U.S. equity	19.00%	5.50%
International equity	19.00%	7.00%
U.S. microcap	7.00%	7.00%
Private equity	10.00%	9.25%
REITs	6.00%	5.85%
Core real estate	10.00%	3.80%
Global options	7.00%	5.50%
Core bonds	3.00%	0.55%
Long treasuries	7.00%	1.90%
Trend following	7.00%	1.75%
TIPS	5.00%	0.50%
	100.0%	

v. Discount Rate

Projected benefits payments are required to be discounted to their actual present values using a single discount rate that reflects (1) a long-term expected rate of return on the EUTF's investments (to the extent that the plan's fiduciary net position is projected to be sufficient to pay benefits), and (2) tax-exempt municipal bond rate based on an index of 20-year general obligation bonds with an average AA credit rating as of the measurement date (to the extent that the contributions for use with the long-term expected rate of return are not met).

9. Employee Benefit Plans (continued)

c. Post-Employment Healthcare and Life Insurance Benefits (continued)

v. Discount Rate (continued)

A single discount rate of 7.00% was used to measure the total OPEB liability. This discount rate was based on the expected rate of return on the EUTF's investments of 7.00%. Beginning with the fiscal year 2019 contributions, the State's funding policy is to pay the recommended actuarially determined contributions, which is based on layered, closed amortization periods. As a result, the EUTF's fiduciary net position is expected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on EUTF's investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

vi. Changes in Net OPEB Liability

The following table represents a schedule of changes in the net OPEB liability. The ending balances are as of the measurement date, July 1, 2017.

	Total OPEB Liability	Plan Fiduciary Net Position	Net OPEB Liability
Beginning Balance	$ 6,744,044	$ 336,440	$ 6,407,604
Service cost	114,840	-	114,840
Interest on the total OPEB liability	348,704	-	348,704
Changes of benefit terms	-	-	-
Difference between expected and actual experience	-	-	-
Changes of assumptions	-	-	-
Employer contributions	-	342,848	(342,848)
Net investment income	-	34,327	(34,327)
Benefit payments	(172,405)	(172,405)	-
Administrative expense	-	(88)	88
Other	-	2,756	(2,756)
Net changes	291,139	207,438	83,701
Ending balance	$ 7,035,183	$ 543,878	$ 6,491,305

9. Employee Benefit Plans (continued)

c. Post-Employment Healthcare and Life Insurance Benefits (continued)

vii. Sensitivity of the Department's Proportionate Share of the Net OPEB Liability to Changes in the Discount Rate

The following presents the Department's proportionate share of the net OPEB liability calculated using the discount rate of 7.00%, as well as what the Department's proportionate share of the net OPEB liability would be if it were calculated using a discount rate that is one percentage point lower (6.00%) or one percentage point higher (8.00%) than the current rate:

	1% Decrease (6.00%)	Discount Rate (7.00%)	1% Increase (8.00%)
Department's proportionate share of the net OPEB liability	$ 7,618,732	$ 6,491,305	$ 5,578,983

viii. Sensitivity of the Department's Proportionate Share of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rate

The following presents the Department's proportionate share of the net OPEB liability calculated using current healthcare cost trend rates, as well as what the Department's proportionate share of the net OPEB liability would be if it were calculated using a healthcare cost trend rate that is one percentage point lower or one percentage point higher than the current rate:

	1% Decrease	Current Healthcare Cost Trend Rate	1% Increase
Department's proportionate share of the net OPEB liability	$ 5,526,452	$ 6,491,305	$ 7,709,058

9. Employee Benefit Plans (continued)

c. Post-Employment Healthcare and Life Insurance Benefits (continued)

ix. OPEB Plan Fiduciary Net Position

The OPEB plan's fiduciary net position is determined on the same basis used by the OPEB plan. The EUTF's financial statements are prepared using the accrual basis of accounting under which revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. Employer 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 EUTF financial report. EUTF's complete financial statements are available at http://eutf.hawaii.gov.

x. Required Supplementary Information and Disclosures

The State's CAFR includes the required footnote disclosures and supplementary information on the State's OPEB plan.

10. Commitments and Contingencies

a. Operating Leases

The Department leases various office facilities and equipment through fiscal year 2023 on a long-term basis as provided for in the lease agreements. The following is a schedule of minimum future rent payments on noncancelable operating leases at June 30, 2018:

Year ending June 30,	Amount
2019	$ 244,389
2020	245,867
2021	181,841
2022	134,697
2023	31,939
Total	$ 838,733

Rental expenditures for the fiscal year ended June 30, 2018 approximated $2,370,000.

10. Commitments and Contingencies (continued)

b. Insurance Coverage

The State maintains certain insurance coverage to satisfy bond indenture agreements as well as for other purposes, but is substantially self-insured for all other perils including workers' compensation. The State records a liability for risk financing and insurance related losses, including incurred but not reported, if it is determined that a loss has been incurred and the amount can be reasonably estimated. The State retains various risks and insures certain excess layers with commercial insurance companies. At June 30, 2018, the State recorded estimated losses for workers' compensation, automobile, and general liability claims as long- term liabilities as the losses will not be liquidated with currently expendable available financial resources. The estimated losses will be paid from legislative appropriations of the State's General Fund.

The Department's portion of the State's workers' compensation expenditures for the year ended June 30, 2018 were approximately $496,000 and $62,000 for the general fund and other funds, respectively.

c. Litigation

The Department is a party to various legal proceedings, the outcome of which, in the opinion of management, will not have a material adverse effect on the Department's financial position. Losses, if any, are either covered by insurance or will be paid from legislative appropriations of the State's General Fund.

11. Restatements

During the current year, the following restatement adjustments were identified:

- Revenues related to fees for covered and non-covered sources were understated at June 30, 2017. As a result, taxes, fines, fees, and other revenues were restated resulting in an adjustment of approximately $4.4 million to the July 1, 2017 net position and fund balance.
- Net position at June 30, 2017 was restated due to the implementation of GASB 75. The resulting adjustments were approximately $1.9 million and $1.6 million to the July 1, 2017 net position for the Water Pollution Control Revolving Fund (WPCRF) and Drinking Water Treatment Revolving Loan Fund (DWTRLF), respectively.

The results of these adjustments have the following impact on the June 30, 2017 financial statements:

	Other Governmental Funds	Total Governmental Funds
Fund balance, as previously reported	$ 122,230,663	$ 253,104,902
Restatement adjustment	4,394,049	4,394,049
Fund balance, as restated	$ 126,624,712	$ 257,498,951

	WPCRF	DWTRLF	Business-Type Activities
Net position, as previously reported	$ 515,096,701	$ 197,732,912	$ 712,829,613
Restatement adjustment	(1,861,850)	(1,610,939)	(3,472,789)
Net position, as restated	$ 513,234,851	$ 196,121,973	$ 709,356,824

SUPPLEMENTARY INFORMATION

Department of Health
State of Hawaii
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Fiscal Year Ended June 30, 2018

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Project Number	Federal CFDA Number		Passed through to Subrecipients	Total Federal Expenditures
Department of Health and Human Services					
Direct Programs:					
TB Epidemiological Studies Consortium	626	200-2011-41277		$ -	$ 290,841
Special Programs for the Aging - Title VII Chapter 3	468	93.041		-	10,832
Special Programs for the Aging - Title VII Chapter 2	468	93.042		-	111,826
Special Programs for the Aging - Title III Part D	401	93.043		66,896	66,896
Aging Cluster:					
Special Programs for the Aging - Title III Part B - Grants for Supportive Services and Senior Centers	401	93.044		1,820,001	1,860,492
Special Programs for the Aging - Title III Part C - Nutrition Services	401	93.045		3,068,450	3,632,304
Nutrition Services Incentive Program	406	93.053		586,771	586,771
Subtotal Aging Cluster			*	5,475,222	6,079,567
Special Programs for the Aging - Title IV and Title II - Discretionary Projects	405, 757	93.048		-	1,114,454
Alzheimer's Disease Demonstration Grants to States	769	93.051		-	44,707
National Family Caregiver Support, Title III, Part E	401	93.052		693,743	693,743
Public Health Emergency Preparedness	577, 760, 1297	93.069	*	-	4,864,755
Environmental Public Health and Emergency Response	444	93.070		129,077	230,727
Medicare Enrollment Assistance Program	765, 766, 767	93.071		-	42,186
Hawaii Birth Defects Surveillance and Intervention for Zika Virus	761	93.073		48,317	71,787
HPP and PHEP Cooperative Agreements	752	93.074		-	139,881
Affordable Care Act Personal Responsibility Education Program	613	93.092		88,520	189,887
Comprehensive Community Mental Health Services for Children with Serious Emotional Disturbances (SED)	764	93.104		-	868,966
Maternal and Child Health Federal Consolidated Programs	257, 307, 466	93.110		587,731	852,171
Project Grants and Cooperative Agreements for Tuberculosis Control Programs	247	93.116		-	1,002,917
Cooperative Agreements to States/Territories for the Coordination and Development of Primary Care Offices	298	93.130		17,201	195,614
Injury Prevention and Control Research and State and Community Based Programs	various	93.136		133,387	860,669
Projects for Assistance in Transition from Homelessness	26208, 30208	93.150		226,568	227,702
Childhood Lead Poisoning Prevention Projects - State and Local Childhood Lead Poisoning Prevention and Surveillance of Blood Lead Levels in Children	780	93.197		-	13,261

* Denotes Major Federal Program

Department of Health
State of Hawaii
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Fiscal Year Ended June 30, 2018

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Project Number	Federal CFDA Number		Passed through to Subrecipients	Total Federal Expenditures
Department of Health and Human Services (Continued)					
Hansen's Disease National Ambulatory Care Program	264	93.215		$ -	$ 931,325
Family Planning - Services	239	93.217		1,321,381	1,685,518
Affordable Care Act Abstinence Education Program	273	93.235		13,654	13,654
State Rural Hospital Flexibility Program	415	93.241		231,812	424,225
Substance Abuse and Mental Health Services - Projects of Regional and National Significance	various	93.243		2,123,686	2,724,719
Universal Newborn Hearing Screening	416	93.251		18,814	241,736
Immunization Cooperative Agreements	457	93.268	*	-	17,531,663
Adult Viral Hepatitis Prevention and Control	397	93.270		-	90,078
Centers for Disease Control and Prevention - Investigations and Technical Assistance	649, 448	93.283		768,528	1,111,280
Small Rural Hospital Improvement Grant Program	454	93.301		163,382	163,382
National State Based Tobacco Control Programs	744	93.305		239,500	884,943
Epidemiology and Laboratory Capacity for Infectious Diseases	700	93.323		-	2,229,539
State Health Insurance Assistance Program	403	93.324		-	190,715
Behavioral Risk Factor Surveillance System - Zika	747	93.336		75,000	129,266
Food Safety and Security Monitoring Project	580	93.448		-	237,994
Affordable Care Act - Maternal, Infant, and Early Childhood Home Visiting Program	602, 753	93.505	*	2,625,252	2,831,114
ACA Nationwide Program for National and State Background Checks for Direct Patient Access Employees of Long Term Care Facilities and Providers	644	93.506		-	136,552
ACA Building Epidemiology, Laboratory, and Health Information Systems Capacity in the Epidemiology and Laboratory Capacity for Infectious Disease and Emerging Infections Program Cooperative Agreements	607	93.521		-	626,055
PPHF Capacity Building Assistance to Strengthen Public Health Immunization Infrastructure and Performance - financed in part by Prevention and Public Health Funds	758	93.539		-	1,276,288
Community-Based Child Abuse Prevention Grants	270	93.590		59,449	190,722
Developmental Disabilities Basic Support and Advocacy Grants	240	93.630		-	472,809
State Public Health Approaches for Ensuring Quitline Capacity - funded in part by Prevention and Public Health Funds	701	93.735		-	41,491
Behavioral Risk Factor Surveillance System	768	93.745		47,680	53,317
State and Local Public Health Actions to Prevent Obesity, Diabetes, Heart Disease and Stroke	various	93.757	*	3,748,681	4,552,935

* Denotes Major Federal Program

Department of Health
State of Hawaii

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Fiscal Year Ended June 30, 2018

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Project Number	Federal CFDA Number		Passed through to Subrecipients	Total Federal Expenditures
Department of Health and Human Services (Continued)					
Preventive Health and Health Services Block Grant funded solely with Prevention and Public Health Funds	35203, 36203	93.758		$ 40,000	$ 807,979
State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare	221, 380, 387	93.777		-	2,258,360
Medical Assistance Program	662	93.778		-	342,869
State Targeted Response to the Opioid Crisis	654	93.788		991,142	1,020,758
Domestic Ebola Supplement to the Epidemiology and Laboratory Capacity for Infectious Diseases	751	93.815		-	193,453
Hospital Preparedness Program (HPP) Ebola Preparedness and Response Activities	754	93.817		-	55,603
Maternal, Infant and Early Childhood Home Visiting Grant Program	602	93.870	*	2,010,948	2,313,202
National Bioterrorism Hospital Preparedness Program	435	93.889		1,034,122	1,325,191
Cancer Prevention and Control Programs for State, Territorial and Tribal Organizations	448	93.898		82,524	445,368
Grants to States for Operation of Offices of Rural Health	299	93.913		15,090	168,984
HIV Care Formula Grants	293	93.917		712,228	1,741,538
HIV Prevention Activities - Health Department Based	266	93.940		52,327	867,838
HIV / AIDS Surveillance	272	93.944		9,948	157,731
Assistance Programs for Chronic Disease Prevention and Control	647, 661, 664	93.945		207,253	589,744
Cooperative Agreements to Support State-Based Safe Motherhood and Infant Health Initiative Programs	319	93.946		-	158,656
Block Grants for Community Mental Health Services	various	93.958		1,013,108	2,553,219
Block Grants for Prevention and Treatment of Substance Abuse	34204, 35204	93.959	*	8,825,408	8,958,083
Preventive Health Services - Sexually Transmitted Diseases Control Grants	268	93.977		-	427,339
Maternal and Child Health Services Block Grant to the States	various	93.994		25,107	1,735,017
Drug and Alcohol Services Information System (DASIS)	371	93.UNKNOWN		21,040	181,188
Hawaii State Mental Health Data Infrastructure Grants for Quality Improvement	318	93.UNKNOWN		28,603	99,887
Hawaii Tobacco State Enforcement Contract	633	93.FAR 52.217-9		152,290	228,736
Electronic Death Registration	208	93.UNKNOWN		-	58,708
Vital Statistics Cooperative Program (VSCP) Special Project	285	93.UNKNOWN		-	279,259
Total Department of Health and Human Services Programs				34,124,619	83,713,419

* Denotes Major Federal Program

Department of Health
State of Hawaii
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Fiscal Year Ended June 30, 2018

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Project Number	Federal CFDA Number		Passed through to Subrecipients	Total Federal Expenditures
Department of Agriculture					
Direct Programs:					
Plant and Animal Disease, Pest Control, and Animal Care	720	10.025		$ -	$ 21,394
Special Supplemental Nutrition Program for Women, Infants and Children	275, 295	10.557		2,008,515	27,369,135
WIC Grants To States (WGS)	740, 741, 790	10.578		427,060	450,218
Total Department of Agriculture Programs				2,435,575	27,840,747
Environmental Protection Agency					
Direct Programs:					
Air Pollution Control Program Support	233	66.001		-	712,319
State Indoor Radon Grants	321	66.032		-	35,039
Surveys, Studies, Research, Investigations, Demonstrations and Special Purpose Activities Relating to the Clean Air Act	294	66.034		-	168,163
Multipurpose Grants to States and Tribes	235, 236	66.204		-	105,253
Water Pollution Control State, Interstate, and Tribal Program Support	231, 237, 601	66.419		37,995	1,783,531
State Public Water System Supervision	232	66.432		-	314,800
Water Quality Management Planning	various	66.454		49,795	110,566
Capitalization Grants for Clean Water State Revolving Funds	various	66.458	*	7,759,837	7,759,837
Nonpoint Source Implementation Grants	various	66.460		1,279,074	1,693,060
Capitalization Grants for Drinking Water State Revolving Funds	various	66.468	*	7,451,878	7,675,478
Beach Monitoring and Notification Program Implementation Grants	8291	66.472		-	465,364
Environmental Information Exchange Network Grant Program and Related Assistance	570	66.608		-	72,267
Toxic Substances Compliance Monitoring Cooperative Agreements	243	66.701		-	37,180
TSCA Title IV State Lead Grants Certification of Lead-Based Paint Professionals	330	66.707		-	191,108
Hazardous Waste Management State Program Support	230	66.801		-	521,183
Superfund State, Political Subdivision, and Indian Tribe Site-Specific Cooperative Agreements	394	66.802		-	316,307

Department of Health
State of Hawaii
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Fiscal Year Ended June 30, 2018

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Project Number	Federal CFDA Number		Passed through to Subrecipients	Total Federal Expenditures
Environmental Protection Agency (Continued)					
Underground Storage Tanks Prevention, Detection and Compliance Program	339	66.804		$ -	$ 364,599
Leaking Underground Storage Tank Trust Fund Corrective Action Program	258	66.805		-	400,438
State and Tribal Response Program Grants	360	66.817		-	891,202
Total Environmental Protection Agency Programs				16,578,579	23,617,694
Department of Education					
Direct Program--					
Special Education - Grants for Infants and Families	213	84.181	*	-	1,994,030
Total Department of Education Programs				-	1,994,030
Department of Defense					
Direct Program--					
State Memorandum of Agreement Program for the Reimbursement of Technical Services	245	12.113		-	358,192
Total Department of Defense Programs				-	358,192
Department of Transportation					
Direct Program--					
Interagency Hazardous Materials Public Sector Training and Planning Grants	641	20.703		-	35,921
Total Department of Transportation Programs				-	35,921
Department of Homeland Security					
Direct Program--					
Homeland Security Grant Program	470	97.067		-	1,437
Total Department of Homeland Security Programs				-	1,437
Total Expenditures of Federal Awards				$ 53,138,773	$ 137,561,440

* Denotes Major Federal Program

Notes to Schedule of Expenditures of Federal Awards
Fiscal Year Ended June 30, 2018

1. Basis of Presentation

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of the State of Hawaii, Department of Health (the Department) under programs of the federal government for the fiscal year ended June 30, 2018. The information in this Schedule is presented in accordance 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). Because the Schedule presents only a selected portion of the operations of the Department, it is not intended to and does not present the financial position, change in net position, or cash flows of the Department.

2. Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the cash basis of accounting which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

3. Loans Outstanding

The Department had the following loan balances outstanding at June 30, 2018. Loans made during the year are included in the federal expenditures presented in the schedule of expenditures of federal awards.

Program Title	CFDA Number	Amount Outstanding
Capitalization Grants for Clean Water State Revolving Funds	66.458	$ 25,931,599
Capitalization Grants for Drinking Water State Revolving Funds	66.468	$ 35,756,395

4. Noncash Awards

The Department also receives noncash awards for the Immunization Cooperative Agreements Program. The Department expended approximately $16,100,000 in vaccines for the Immunization Cooperative Agreements Program for the fiscal year ended June 30, 2018.

5. Indirect Cost Rate

The Department has elected not to use the 10-percent de minimus indirect cost rate allowed under the Uniform Guidance.

PART II

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*

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*

Independent Auditor's Report

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 the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Hawaii, Department of Health (Department), as of and for the fiscal year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Department's basic financial statements, and have issued our report thereon dated March 14, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Department'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 Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

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. We consider the deficiency described in the accompanying schedule of findings and questioned costs as Finding No. 2018-001 to be a material weakness.

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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. We consider the deficiency described in the accompanying schedule of findings and questions costs as Finding No. 2018-002 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, 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*.

Department's Response to Findings

The Department's response to the findings identified in our audit is described in the accompanying corrective action plan. The Department's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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. Accordingly, this communication is not suitable for any other purpose.

KMH LLP

KMH LLP

Honolulu, Hawaii
March 14, 2019

PART III

REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

Report on Compliance for Each Major Federal Program and on Internal Control over Compliance Required by Uniform Guidance

Independent Auditor's Report

Office of the Auditor
State of Hawaii

Report on Compliance for Each Major Federal Program

We have audited the State of Hawaii, Department of Health's (Department's) 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 Department's major federal programs for the fiscal year ended June 30, 2018. The Department'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 Department'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 Department's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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We believe that our audit provides a reasonable basis for our qualified and unmodified opinions on compliance for major federal programs. However, our audit does not provide a legal determination of the Department's compliance.

Basis for Qualified Opinion on Major Federal Programs in the Table Below

As described in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding:

CFDA Number	Name of Federal Program	Compliance Requirement	Ref. No.
93.959	Block Grants for Prevention and Treatment of Substance Abuse	Reporting	2018-003
93.959	Block Grants for Prevention and Treatment of Substance Abuse	Subrecipient Monitoring	2018-004
93.044 93.045 93.053	Aging Cluster	Cash Management	2018-005
93.069	Public Health Emergency Preparedness		
93.268	Immunization Cooperative Agreements		
93.505 93.870	Maternal, Infant, and Early Childhood Home Visiting Cluster		
93.757	State and Local Public Health Actions to Prevent Obesity, Diabetes, Heart Disease and Stroke		
93.959	Block Grants for Prevention and Treatment of Substance Abuse		
84.181	Special Education – Grants for Infants and Families		

Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to that program.

Qualified Opinion on the Major Federal Programs in the Table Above

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, the Department complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the major federal programs identified in the Basis for Qualified Opinion paragraph for the fiscal year ended June 30, 2018.

Unmodified Opinion on Each of the Other Major Federal Programs

In our opinion, the Department 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 other major federal programs identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs for the fiscal year ended June 30, 2018.

Other Matters

The Department's response to the noncompliance findings identified in our audit are described in the accompanying corrective action plan. The Department's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Management of the Department 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 Department'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 Department'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 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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify certain deficiencies in internal control over compliance, described in the accompanying schedule of findings and questioned costs as Finding No. 2018-003 through 2018-006, that we consider to be material weaknesses.

The Department's response to the internal control over compliance findings identified in our audit is described in the accompanying corrective action plan. The Department's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

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.

KMH LLP

KMH LLP

Honolulu, Hawaii
March 14, 2019

PART IV

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Department of Health
State of Hawaii

Schedule of Findings and Questioned Costs
June 30, 2018

Section I – Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: Unmodified

Internal control over financial reporting:

- Material weakness(es) identified? _√_ Yes ____No
- Significant deficiency(ies) identified that are not considered to be material weaknesses? _√_ Yes ____None reported

Noncompliance material to financial statements noted? ___Yes _√_ No

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? _√_ Yes ____No
- Significant deficiency(ies) identified? ____Yes _√_ None reported

Type of auditor's report issued on compliance for major federal programs: Qualified

Any audit findings disclosed that are required to be reported in accordance with section 2 CFR 200.516(a)? _√_ Yes ____No

Department of Health
State of Hawaii

Schedule of Findings and Questioned Costs
June 30, 2018

Section I – Summary of Auditor's Results (continued)

Identification of major federal programs:

CDFA Number	Name of Federal Program
	Department of Health & Human Services
	Aging Cluster:
93.044	Special Programs for Aging – Title III Part B – Grants for Supportive Services and Senior Centers
93.045	Special Programs for Aging – Title III Part C – Nutrition Services
93.053	Nutrition Services Incentive Program
93.069	Public Health Emergency Preparedness
93.268	Immunization Cooperative Agreements
93.505	Affordable Care Act - Maternal, Infant, and Early Childhood Home Visiting Program
93.757	State and Local Public Health Actions to Prevent Obesity, Diabetes, Heart Disease and Stroke
93.870	Maternal, Infant and Early Childhood Home Visiting Grant Program
93.959	Block Grants for Prevention and Treatment of Substance Abuse
	Department of Education
84.181	Special Education – Grants for Infants and Families
	Environmental Protection Agency
66.458	Capitalization Grants for Clean Water State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds

Dollar threshold used to distinguish between type A and type B programs: $3,000,000

Auditee qualified as low-risk auditee? Yes ___ No _√_

Section II – Financial Statement Findings

Finding No.: 2018-001 Financial Statement Reporting

Type of Finding: Material Weakness

Criteria: In accordance with Governmental Accounting Standards Board (GASB) Statement No. 34, fund financial statements should be prepared using the current financial resources measurement focus and the modified accrual basis of accounting. Under this focus/basis, revenues are recognized only to the extent that they are susceptible to accrual. Revenues are recorded when earned, regardless of the timing of related cash flows.

Condition: During our audit, we proposed and management accepted a restatement adjustment related to clean air permit revenues for approximately $4.4 million. The adjustment was recorded in beginning net position as of July 1, 2017 in the Department's financial statements as of June 30, 2018.

Context: Due to staffing constraints, the Department annually contracts with its auditors to assist in compiling the Department's financial statements. The error noted above was detected during the audit because of unusual variances or patterns noted in the related financial statement balances.

The Department does not reconcile the clean air permit revenues from the program schedule to FAMIS. As a result, there were revenues related to the year ending June 30, 2017 that were recorded in the year ending June 30, 2018. This resulted in an overstatement of revenues related to taxes, fines, fees, and other revenue balance related to the other funds.

Cause: The Department does not perform a reconciliation of the clean air permit revenues from the program schedule to FAMIS.

Effect: The absence of a reconciliation process increases the risk of material misstatements as illustrated by the results of the fiscal year 2018 audit.

Section II – Financial Statement Findings (continued)

Identification as a Repeat Finding, if applicable: Not applicable

Recommendations: Management should implement a process to reconcile the clean air permit fees from the program schedule to FAMIS.

Views of Responsible Officials and Planned Corrective Action: See Part VI Correction Action Plan.

Section II – Financial Statement Findings (continued)

Finding No.: 2018-002 Reliance on Third Party Certifications

Type of Finding: Significant Deficiency

Criteria: Section 342G-105, Hawaii Revised Statutes (HRS), states that payment of the deposit beverage container fee and deposits shall be made monthly, based on inventory reports of the deposit beverage distributors. All deposit beverage distributors shall submit to the Department documentation in sufficient detail that identifies the net number of deposit beverage containers sold, donated, or transferred, by container size and type.

In addition, Section 342G-110, HRS, specifies that the deposit on each filled deposit beverage container shall be paid by the beverage distributor, who manufactures or imports beverages in deposit beverage containers. Beverage distributors shall also pay a deposit beverage container fee and register with the State.

Section 342G-119, HRS, specifies that the Department shall pay certified redemption centers handling fees and deposit refunds based on collection reports submitted by the redemption centers. The redemption reports include the number or weight of deposit beverage containers of each material type accepted at the redemption center for the reporting period; the amount of refunds paid out by material type; the number or weight of deposit beverage containers of each material type transported out of state or to a permitted recycling facility; and copies of out-of-state transport and weight receipts or acceptance receipts from permitted recycling facilities. Additionally, Section 11-282-47, Hawaii Administrative Rules (HAR), states that the Department shall pay certified redemption centers handling fees and refund values based on reports submitted by the redemption centers to the Department.

Section 342G-103, HRS, requires all beverage distributors operating within the State to register with the Department and maintain records reflecting the manufacture of their beverages in deposit beverage containers as well as the importation and exportation of deposit beverage containers. The records shall be made available, upon request, for inspection by the Department.

Similarly Section 342G-121, HRS, requires distributors and redemption centers to make their records available upon request by the Department, a duly authorized agent of the Department, or the Office of the Auditor.

Section II – Financial Statement Findings (continued)

Condition: The Deposit Beverage Container Program (Program) receives beverage container deposits and container fees from distributors and refunds deposits and pays handling fees to redemption centers based on certified information. The Program relies on certifications from distributors to support deposits and container fees received. The Program also relies on certifications from redemption centers to support deposit refunds and handling fees paid.

In 2018 and during our testing of the redemption centers, we noted that in 2 out of 15 redemption center visits, the amounts provided in the redemption transaction logs, noted as the manually prepared Cash Receipts Log, did not match to our receipts and the amount paid. In both instances, the Cash Receipts Log appears to have been altered after we had visited the location to reflect additional material type containers, resulting in an increase in the amounts reimbursed to the redemption center. We reported our findings to the Office of the Auditor and the Director of the Department of Health on November 20, 2018.

Context and Cause: As noted below, this is a recurring finding. The Department still has not been able to recruit or retain the personnel needed to monitor the distributors and the certified redemption centers.

Effect: Overreliance on the self-reporting by distributors and redemption centers may result in underpayments on deposits and the related container fees received by the Department to administer the program, overpayments of deposit refunds and handling fees to redemption centers, and an overstated redemption rate. An overstated redemption rate could result in a misstatement in the Department's financial statements, as well as higher container fees for consumers to support the program.

The Program could mitigate the risk of fraud (underpayments by distributors and overpayments to redemption centers) by implementing a systematic process for monitoring the activities of and reports submitted by distributors and redemption centers. However, due to insufficient staff positions and turnover, management has been unable to establish a systematic monitoring process.

Identification as a Repeat Finding, if applicable: See finding 2017-003 included in the Summary Schedule of Prior Audit Findings.

Section II – Financial Statement Findings (continued)

Recommendation: We recommend that the Program perform the following: (1) develop a risk-based process to select distributor and redemption center reports submitted to the Program to audit on a periodic basis; (2) summarize the results of distributor and redemption center audits and assess whether enforcement actions should be considered to ensure amounts that are being reported are appropriate; (3) modify the Program requirements in order to increase distributors' accountability for information provided to the Program; and (4) for redemption centers, the Program should consider having all redemption centers install reverse vending machines or some type of "mechanical devices" at all locations.

Views of Responsible Officials and Planned Corrective Action: See Part VI Correction Action Plan

Section III – Federal Award Findings and Questioned Costs

Finding No.: 2018-003	**Timely Submission of Federal Financial Report**
Federal Agency:	Department of Health and Human Services (DHHS)
CFDA No.:	93.959
Requirement:	Reporting
Type of Finding:	Material Noncompliance and Material Weakness
Program:	Block Grants for Prevention and Treatment of Substance Abuse
Federal award no. and year:	3B08TI010015-16 10/01/2015 – 09/30/2017

Criteria: 2 CFR section 200.327 states that "(financial) information must be collected with the frequency required by the terms and conditions of the Federal award, but no less frequently than annually nor more frequently than quarterly except in unusual circumstances." Under the reporting requirements of the Substance Abuse Prevention and Treatment Block Grant (SABG), the program must submit a closing Federal Financial Report (FFR) within 90 days after the end of the obligation and expenditure period of the grant.

Condition: Reporting requirements for one FFR was not met.

Context: SABG was required to submit one closing FFR during FY 2018. During the audit, we noted that the FFR was submitted 395 days after the end of the obligation and expenditure period of the grant.

Cause: Based on further inquiry with Department personnel, we noted the delay in submission was caused by the re-opening of the grant after the award period. However, approval to re-open the grant was not obtained until 356 days after the end of the obligation and expenditure period of the grant.

Effect: Failure to submit reports results in noncompliance with the reporting requirement.

Questioned Costs: None

Identification as a Repeat Finding, if applicable: See finding 2017-004 included in the Summary Schedule of Prior Audit Findings.

Recommendation: We recommend program management be more diligent in following its procedures and internal controls related to contract close-outs and the de-obligation of funds in order to ensure compliance with Federal requirements.

Views of Responsible Officials and Planned Corrective Action: See Part VI Correction Action Plan.

Section III – Federal Award Findings and Questioned Costs

Finding No.: 2018-004	**Monitoring Procedures and Risk Assessment Process**
Federal Agency:	Department of Health and Human Services (DHHS)
CFDA No.:	93.959
Requirement:	Subrecipient Monitoring
Type of Finding:	Material Noncompliance and Material Weakness
Program:	Block Grants for Prevention and Treatment of Substance Abuse
Federal award no. and year:	3B08TI010015-16 10/01/2015 – 09/30/2017

Criteria: In accordance with 2 CFR section 200.331, all pass-through entities must monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. In addition, all pass-through entities must evaluate each subrecipient's risk of noncompliance with Federal statutes, regulations, and the terms and conditions of the subaward for purposes of determining the appropriate subrecipient monitoring.

Condition: The program did not comply with its documented monitoring procedures consistently. Also, from a control standpoint, the program does not have a formal, documented risk assessment policy. In addition, through discussions with program personnel, we noted that contracts are chosen for on-site visits on an ad hoc basis, rather than based on a formal risk assessment policy.

Context: Of a total of 70 contracts, we selected seven contracts based on a non-statistical sample. We noted that two of the seven contracts were not monitored based on the program's documented procedures.

Cause: There was a lack of diligence in following documented monitoring procedures.

Effect: Failure to have and follow a subrecipient monitoring policy that meets the requirements in 2 CFR section 200.331 results in noncompliance with the subrecipient monitoring requirement.

Questioned Costs: None

Identification as a Repeat Finding, if applicable: See finding 2017-005 included in the Summary Schedule of Prior Audit Findings.

Recommendation: We recommend that management establish a formal, documented risk assessment policy in order to support which subrecipients are chosen and how they are monitored. We also recommend that management follow its documented monitoring procedures.

Views of Responsible Officials and Planned Corrective Action: See Part VI Correction Action Plan.

Section III – Federal Award Findings and Questions Costs (continued)

Finding No.: 2018-005	**Cash Management**
Federal Agency:	Department of Health and Human Services (DHHS) Department of Education
CFDA No.:	93.044, 93.045, 93.053, 93.069, 93.268, 93.505, 93.757, 93.870, 93.959, and 84.181
Requirement:	Cash Management
Type of Finding:	Material Noncompliance and Material Weakness
Program:	Aging Cluster: Special Programs for Aging – Title III Part B – Grants for Supportive Services and Senior Centers Special Programs for Aging – Title III Part C – Nutrition Services Nutrition Services Incentive Program Public Health Emergency Preparedness Immunization Cooperative Agreements Affordable Care Act - Maternal, Infant, and Early Childhood Home Visiting Program State and Local Public Health Actions to Prevent Obesity, Diabetes, Heart Disease and Stroke Maternal, Infant and Early Childhood Home Visiting Grant Program Block Grants for Prevention and Treatment of Substance Abuse Special Education – Grants for Infants and Families

Section III – Federal Award Findings and Questions Costs (continued)

Federal award no. and year:	15AAHIT3SS	10/01/2014 -	18AAHINSIP	10/01/2017 -
	16AAHIT3SS	10/01/2015 -	NU90TP000513-	07/01/2016 -
	17AAHIT3SS	10/01/2016 -	NU90TP921898-	07/01/2017 -
	18AAHIT3SS	10/01/2017 -	5NH23IP000721-	04/01/2017 -
	15AAHIT3CM	10/01/2014 -	6NH23IP000721-	04/01/2017 -
	16AAHIT3CM	10/01/2015 -	X02MC28216-01	03/01/2015 -
	17AAHIT3CM	10/01/2016 -	D89MC2820-01	03/01/2015 -
	18AAHIT3CM	10/01/2017 -	X10MC29466-01	04/01/2016 –
	15AAHIT3HD	10/01/2014 -	X10MC31137-01	09/30/2017 –
	16AAHIT3HD	10/01/2015 -	NU58DP005502-	09/30/2016 –
	17AAHIT3HD	10/01/2016 -	NU58DP005502-	09/30/2017 –
	18AAHIT3HD	10/01/2017 -	NU58DP005502-	06/30/2017 –
	15AAHINSIP	10/01/2014 -	2B08TI010015-16	10/01/2015 –
	16AAHINSIP	10/01/2015 -	3B08TI010015-17	10/01/2016 –
	17AAHINSIP	10/01/2016 -	H181A170091	07/01/2017 –

Criteria: The federal award programs noted above are not subject to the Treasury-State Agreement and, as such, are subject to 2 CFR 200.305(b), which states:

"The timing and amount of advance payments must be as close as is administratively feasible to the actual disbursements by the non-Federal entity for direct program or project costs and the proportionate share of any allowable indirect costs. The non-Federal entity must make timely payment to contractors in accordance with the contract provisions..."

Condition: Systemic problem. During our testing of the Department's cash management procedures, we could not verify whether the State of Hawaii, Department of Accounting and General Services (DAGS) disbursed funds from federal sources as close as administratively feasible to the Department's disbursements for the federal award programs identified above after the Department drew down the funds, in accordance with 2 CFR 200.305(b).

Section III – Federal Award Findings and Questions Costs (continued)

Context: During the fiscal year ended June 30, 2018, the Department expended the following amounts under the following major programs as reported in the schedule of expenditures on pages 75 - 80:

CFDA 93.044, 93.045, and 93.053	$ 6,079,567
CFDA 93.069	4,864,755
CFDA 93.268 (excluding non-cash expenditures)	1,436,879
CFDA 93.505	2,831,114
CFDA 93.757	4,552,935
CFDA 93.870	2,313,202
CFDA 93.959	8,958,083
CFDA 84.181	1,994,030
	$ 33,030,565

Cause: The Department draws down federal funds that it estimates will be needed based on the vouchers processed daily. However, since deposits must be posted prior to the processing of payments or disbursing of the funds, it is difficult for the Department to disburse federal funds in accordance with 2 CFR 200.305(b), and we could not verify compliance with 2 CFR 200.305(b).

Effect: Noncompliance with federal regulations could result in a loss of funding that may jeopardize the operations of the Department's federally funded programs.
Questioned Costs: None

Identification as a Repeat Finding, if applicable: See finding 2017-007 included in the Summary Schedule of Prior Audit Findings.

Recommendation: We recommend that the Department work with DAGS and the Department of Budget and Finance to ensure timely disbursement of federal funds in accordance with 2 CFR 200.305(b).

Views of Responsible Officials and Planned Corrective Action: See Part VI Correction Action Plan.

Section III – Federal Award Findings and Questioned Costs (continued)

Finding No.: 2018-006	**Monitoring Procedures and Risk Assessment Process**
Federal Agency:	Department of Health and Human Services (DHHS)
CFDA No.:	93.757
Requirement:	Subrecipient Monitoring
Type of Finding:	Material Weakness
Program:	State and Local Public Health Actions to Prevent Obesity, Diabetes, Heart Disease and Stroke
Federal award no. and year:	U58DP005502 09/30/2014 – 09/30/2018

Criteria: In accordance with 2 CFR section 200.331, all pass-through entities must monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. In addition, all pass-through entities must evaluate each subrecipient's risk of noncompliance with Federal statutes, regulations, and the terms and conditions of the subaward for purposes of determining the appropriate subrecipient monitoring.

Condition: The program does not have documented monitoring procedures or a formal, documented risk assessment policy.

Context: Through discussions with program management, we noted that the program does not have documented monitoring procedures or a formal, documented risk assessment policy. In addition, we noted that the program has had significant turnover in personnel, which has prolonged the completion of documented policies and procedures.

Cause: Lack of documented policies and procedures and a formal, documented risk assessment policy.

Effect: Lack of documented policies and procedures and a formal, documented risk assessment policy could lead to non-compliance with the subrecipient monitoring requirement.

Questioned Costs: None

Identification as a Repeat Finding, if applicable: Partially applicable. See finding 2017-009 included in the Summary Schedule of Prior Audit Findings.

Recommendation: We recommend program management develop formal policies and procedures to ensure compliance with Federal requirements.

Views of Responsible Officials and Planned Corrective Action: See Part VI Correction Action Plan.

PRIOR YEAR FINDINGS AND QUESTIONED COSTS

Department of Health
State of Hawaii

Summary Schedule of Prior Audit
June 30, 2018

STATUS REPORT

This section contains the current status of prior audit recommendations. The recommendations are referenced to the pages of the previous audit report for the fiscal year ended June 30, 2017, dated March 28, 2018.

Part II – Financial Statement Findings

2017-001 Financial Statement Reporting

Recommendations	Status
Management should revisit its process in reviewing its financial statements. For example, management should ensure that the review process includes the consideration and investigation of material variances from prior years or material changes in the Department's business environment (e.g., new laws, agreements, etc.) that may impact the financial statements.	Develop procedures to review prior year financial statements and determine whether variances and other material changes to the financial statement of the year being audited need further review based on rule changes, new laws or the State's overall business climate that may contribute to the variances and material changes. Accomplished. This finding is no longer applicable.

2017-002 Vouchers Payable

Recommendations	Status
We recommend the Department of Health revisit their process to identify vouchers payable that should be accrued. Due to the diverse nature of the Department's activities, it is important to work with the respective divisions and programs to obtain timely and accurate information	Develop procedures to obtain information from the program on vouchers payable that require Department programs to submit information for all payables that cannot be paid in the fiscal year that it was received/incurred. Accomplished. This finding is no longer applicable.

Department of Health
State of Hawaii

Summary Schedule of Prior Audit
June 30, 2018

Recommendations	Status

Part II – Financial Statement Findings (continued)

2017-003 Reliance on Third Party Certifications

Recommendations	Status
We recommend that the Program implement a systemic process and direct Department personnel to oversee distributors and redemption centers, including conducting regular audits of reports submitted and payments made by distributors and reports submitted for deposit refund and handling fee requests from redemption centers.	Implement a comprehensive auditing function through filling positions within the Program and by outsourcing the auditing duties to an independent public accounting firm on an "as needed" basis. Not accomplished. Refer to finding 2018-002.

Part III – Federal Award Findings and Questioned Costs

2017-004 Timely Submission of Federal Financial Report

Recommendations	Status
We recommend program management be more diligent in following its procedures and internal controls related to contract close-outs and the de-obligation of funds in order to ensure compliance with Federal requirements.	Three months prior to the end of each contract year, letters notifying providers and contractors of invoice deadlines and time submittal of invoices will be issued. Alcohol and Drug Abuse Division intends to submit the Federal Financial Report directly to Substance Abuse and Mental Health Services Administration. Not accomplished. Refer to finding 2018-003.

Recommendations	Status

Part III – Federal Award Findings and Questioned Costs (continued)

2017-005 Monitoring Procedures and Risk Assessment Process

Recommendations	Status
We recommend that management establish a formal, documented risk assessment policy in order to support which subrecipients are chosen and how they are monitored. We also recommend that management follow its documented monitoring procedures.	Implement a risk assessment policy and revise the control narrative to allow for desk-top audits rather than only face-to-face audits. Not accomplished. Refer to finding 2018-004.

2017-006 Timely Submission of Federal Financial Report

Recommendations	Status
We recommend program management be more diligent in following Federal deadlines in order to ensure compliance with Federal requirements.	Program and respective Department Administrative Services Accountant will work together to ensure that Federal deadlines are met. Accomplished. This finding is no longer applicable.

Recommendations	Status
Part III – Federal Award Findings and Questioned Costs (continued)	
2017-007 Cash Management	
We recommend that the Department work with DAGS and B&F to ensure timely disbursement of federal funds in accordance with 31 CFR 205.	The State has been looking at its processes for managing federal awards and is taking steps towards addressing the issues relating to cash management. This affects all State agencies in the Executive Branch that receive Federal awards and DOH is waiting for the State to provide guidance and changes to process. Once guidance and processes are received from the State Office of Budget and Finance (B&F), DOH will work to comply with the requirements. Not accomplished. Refer to finding 2018-005.
2017-008 Timely Submission of Federal Financial Report	
We recommend program management review its notice of award documentation and relevant Federal regulations and develop formal policies and procedures to ensure compliance with Federal requirements.	Implement procedures to ensure timely submission of Federal Financial Reports. Maintain a timeline of all Federal requirements deadlines that will be recorded on SharePoint. Additionally, the division accountant will keep a record of all Federal Financial Report deadlines. Accomplished. This finding is no longer applicable.

Recommendations	Status

Part III – Federal Award Findings and Questioned Costs (continued)

2017-009 Obtaining Single Audit Reports

Recommendations	Status
We recommend program management develop formal policies and procedures to ensure compliance with Federal requirements.	Implement procedures and add contract language to obtain a Single Audit Report from applicable contractors. Partially accomplished. Refer to finding 2018-006.

2017-010 Maintenance of State Funding Levels

Recommendations	Status
We recommend program management establish monitoring procedures to ensure that final non-Federal funding meets the level of effort requirement.	Program accountant will track and verify that maintenance of effort requirements are met on an annual basis. Accomplished. This finding is no longer applicable.

Recommendations	Status

Part III – Federal Award Findings and Questioned Costs (continued)

2017-011 Accrued Vacation

Recommendations	Status
The Department should review and correct its payout process for accrued leave to prevent future errors.	The Department has outlined a process where once an individual paid on federal funds separates from service, the program reviews the expenditures made to the account and identifies the vacation payout amount charged to the federal fund. The vacation payout is then transferred to a non-federal fund account within 90 days or prior to the submission of the final Federal Financial Report, whichever is sooner. Accomplished. This finding is no longer applicable.

2017-012 Excluded Parties Listing Search (EPLS)

Recommendations	Status
We recommend program management establish procedures to perform and retain EPLS check documentation	Establish policies and procedures requiring the Contract Specialist to review the contract checklist, perform and retain EPLS check documentation to ensure that no awards, sub-awards, and contracts are issued to any parties that are debarred, suspended or otherwise excluded from or ineligible for participation in Federal assistance programs or activities and save documentation in the contract file. Accomplished. This finding is no longer applicable.

Recommendations	Status

Part III – Federal Award Findings and Questioned Costs (continued)

2017-013 Schedule of Expenditures of Federal Awards (SEFA) Preparation

We recommend the Department of Health revisit their process of compiling the Schedule of Expenditures and Federal Awards.	The DOH-ASO is developing a procedure to assist DOH programs in compiling their expenditure data and is currently working on training materials and a training session on how to gather the data. Accomplished. This finding is no longer applicable.

PART VI

CORRECTIVE ACTION PLAN

DAVID Y. IGE
GOVERNOR OF HAWAII

BRUCE S. ANDERSON, Ph.D.
DIRECTOR OF HEALTH

In reply, please refer to:
File:ASO-F/19-215

STATE OF HAWAII
DEPARTMENT OF HEALTH
P. O. BOX 3378
HONOLULU, HI 96801-3378

March 22, 2019

Mr. Leslie H. Kondo, State Auditor
Office of the Auditor, State of Hawaii
465 S. King Street, Room 500
Honolulu, Hawaii 96813

Subject: Response to Draft Report "Financial Audit of the Department of Health, State of Hawaii, for the Fiscal Year Ended June 30, 2018".

Dear Mr. Kondo:

Attached are the Department of Health's comments of the audit findings for the above mentioned audit of the Department of Health.

We appreciate the opportunity to comment on the report.

Sincerely,

Bruce S. Anderson, Ph.D.
Director of Health

Attachment

SUBJECT: FINANCIAL AUDIT OF THE DEPARTMENT OF HEALTH, STATE OF HAWAII, FOR THE FISCAL YEAR ENDED JUNE 30, 2018

The Department of Health (DOH) appreciates the opportunity to comment on the subject report. We realize that audit findings and recommendations from the auditor is a management tool to assist DOH in making ongoing improvements to our existing processes in order to better manage and monitor these sources of funding.

We would like to comment on "Part IV – Schedule of Findings and Questioned Costs" portion of the report. Please note that we are responding to the Draft Report "Financial Audit of the Department of Health, State of Hawaii, for the Fiscal Year Ended June 30, 2018.

Reference No.: 2018-001 Financial Statement Reporting (Material Weakness)

The Clean Air Branch (CAB) is responsible for collecting the clean air permit revenues. Permit holders are required to submit their annual fees for noncovered and covered source permits source fees 60 and 120 days, respectively, after the start of the calendar year.

To address the Finding of this audit, the CAB proposes to:

- Reconcile annual fee logs across multiple years to reconcile deposits to FAMIS;
- Make deposits in a timely manner; and
- Add a deposit date field to the CAB annual fees log to enable tracking by this date.

Currently, the CAB tracks fee payments using Excel spreadsheets for the purpose of checking compliance: did a permittee pay, pay the correct amount, and pay on time. No attempt is made to reconcile the totals to FAMIS. The main example of when this may be a problem is when a permittee pays the fee for both a previous year (a late payment) and the current year using the same check. The late payment is entered into the previous year's log but the revenue occurs in the current year.

In the future, we will associate payments with the proper accrual period. We will monitor the total revenue for the current period across multiple fee years (e.g., late payment for 2018 fee that is received in 2019). We will be able to reconcile all payments to FAMIS across fee years while continuing to monitor for compliance. To improve tracking, CAB further proposes to track the deposit date in the CAB annual fees log, which is currently not being done. Variation in revenues collected from year to year may occur due to permit fee extensions allowed by Hawaii Administrative Rules. CAB's reconciliation of the annual fee logs across multiple years to FAMIS, depositing of fees in a timely manner, and the incorporation of tracking by deposit date will help to decrease the variation and ensure that all fees collected are appropriately tracked.

Person Responsible: Barry Ching, Supervisor, Planning & Administrative Support Staff
Environmental Management Division, Clean Air Branch

Anticipated Date of Completion: December 31, 2019

Reference No.: 2018-002 Reliance on Third Party Certifications (Significant Deficiency)

The Deposit Beverage Container Program (DBCP) recognizes that overreliance on the self-reporting by distributors may result in the inaccurate payments on deposits and container fees to the Department of Health (DOH) in addition to the inaccurate payments of deposit refunds and handling fees to redemption center operators.

The DBCP is developing a risk-based process to select distributors and redemption center operators to audit. The risk-based selection process is dependent on the financial liability the distributor or redemption center operator poses to the DBCP and the history of non-compliance. Auditing of the selected distributors and redemption center operators will be accomplished through the procurement of services from a Certified Public Accounting (CPA) Firm. The solicitation and the selection of a CPA firm is anticipated to be completed by June 30, 2019. Awarding the contract to the selected vendor should be completed by October 31, 2019. The audits of the distributors and redemption center operators are anticipated to be completed by June 30, 2020. If the CPA firm reveals potential administrative or criminal non-compliance in the audits of distributors and redemption center operators, the DOH or the State of Hawaii Department of the Attorney General (DAG) will take appropriate enforcement actions respectively. In addition, the DBCP will modify the current Memorandum of Agreement with the DAG to include criminal investigation of non-compliance arising from the audits.

The DBCP will increase the information distributors are required to submit to DOH to include but not limited to sales records used to generate the distributors' report and payment. The DBCP supported the implementation of reverse vending machines (RVMs) at the start of the program in 2005 however over time these RVMs were phased out due to the high maintenance costs, low capacity, utility requirements and frequent jams. The DBCP is currently considering and evaluating point of sale or inventory systems that are primarily implemented at scrap material or solid waste facilities for tracking redemption transactions at all certified redemption centers. These types of systems will increase the accountability of certified redemption center operators and provide tamper proof documents for auditing purposes.

Person Responsible: Darren Park, Solid Waste Management Coordinator
Solid, Solid and Hazardous Waste Branch

Anticipated Date of Completion: June 30, 2020

Reference No.: 2018-003 Timely Submission of Federal Financial Report (Material Noncompliance and Material Weakness)

The program recognizes that the Federal Financial Report (FFR) was not submitted within 90 days after the end of the obligation and expenditure period of the grant.

The program continues to take corrective action towards completing the FFR on time. Three corrective actions are being implemented. First, three months prior to the end of the contract year, a letter notifying providers and contractors of invoice deadlines and timely submittal of invoices are issued. Second, with the assistance of the DOH-ASO, the program submits the FFR directly to SAMHSA. Third, when it is anticipated that the FFR cannot be completed within the 90 day period after the ending of the obligation and expenditure period, the program seeks SAMHSA's approval in writing (versus sending an email) for an extension of time to complete the report.

Person(s) Responsible: John Valera, Acting Division Chief, Alcohol and Drug Abuse Division
Melanie Muraoka, Administrative Officer V, Alcohol and Drug Abuse Division

Anticipated Date of Completion: Next Financial Audit for the Period Ending June 30, 2019 for the Department of Health.

Reference No.: 2018-004 Monitoring Procedures and Risk Assessment Process (Material Noncompliance and Material Weakness)

The program recognizes that the subrecipient monitoring protocols were not consistently followed.

The program will take corrective action towards ensuring that subrecipient monitoring protocols for every audited contract are followed. The program will also consider the development of a risk assessment policy as part of its subrecipient monitoring protocol.

Person(s) Responsible: John Valera, Acting Division Chief, Alcohol and Drug Abuse Division
Melanie Muraoka, Administrative Officer V, Alcohol and Drug Abuse Division

Anticipated Date of Completion: Following Financial Audit for the Period Ending June 30, 2020 for the Department of Health.

Reference No.: 2018-005 Cash Management (Material Noncompliance and Material Weakness)

The audit finds that the drawdown of funds for federal awards are not in compliance with 2 CFR 200.305 (b) that requires disbursement of federal funds as close as administratively possible to DOH's disbursement for the federal awards programs. As mentioned in the previous financial audits of the Department of Health, State of Hawaii, For the Fiscal Years Ending June 30, 2016 and June 30, 2017 disbursing the drawdowns of the funds is a very cumbersome process. The State Department of Budget and Finance (B&F) validates the deposits recorded in the State's Financial Accounting Management and Information system (FAMIS) done by the State Department of Accounting and General Services (DAGS). The process for obtaining validation and posting to the FAMIS take approximately 5 to 10 days and it is only when these processes are secured, can DOH disburse the funds to vendors. This process affects all State agencies that receive federal funding. DAGS and B&F are reviewing the State's FAMIS and is looking at the policies and processes currently in place to determine what types of modifications are needed for improvements.

Person(s) Responsible: State of Hawaii Budget & Finance (B&F) and State of Hawaii
Department of Accounting and General Services (DAGS)

Anticipated Date of Completion: Unknown

Reference No.: 2018-006 Monitoring Procedures and Risk Assessment Process (Material Weakness)

The program recognizes the lack of documented policies and procedures and a formal, documented risk assessment policy. We understand that the lack of documented policies and procedures and a formal, documented risk assessment policy could lead to non-compliance with the subrecipient monitoring requirement.

The program has had significant turnover in personnel which has prolonged the completion of the documented policies and procedures. The program acknowledges that it is a repeat finding and considers it as a top priority to ensure compliance with Federal requirements. As the programs hire and train more personnel, we will have a first meeting with management, branch chiefs, and project managers in June 2019 to kickstart the development, implementation, and monitoring of the written formal documented policies and procedures and a formal, documented risk assessment policies.

Person Responsible: Sayuri Sugimoto, Administrative Officer
Chronic Disease Prevention and Health Promotion Division

Anticipated Date of Completion: December 31, 2019