KDLY LLC
CERTIFIED PUBLIC ACCOUNTANTS

Harbors Division
Department of Transportation
State of Hawaii

(An Enterprise Fund of the State of Hawaii)

Financial Statements and Supplementary Information
(With Independent Auditors' Report Thereon)

June 30, 2018 and 2017

Submitted by

THE AUDITOR
STATE OF HAWAII

Harbors Division
Department of Transportation
State of Hawaii
(An Enterprise Fund of the State of Hawaii)

Financial Statements and Supplementary Information

June 30, 2018 and 2017

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PART I

INTRODUCTION SECTION

December 6, 2018

The Auditor
State of Hawaii:

We have completed our audits of the financial statements of the Harbors Division, Department of Transportation, State of Hawaii (the Harbors Division), an enterprise fund of the State of Hawaii, as of and for the years ended June 30, 2018 and 2017. We transmit herewith our independent auditors' report containing our opinion on those financial statements and our 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.*

Audit Objectives

The objectives of the audits were as follows:

1. To provide an opinion on the fair presentation of the Harbors Division's financial statements in accordance with accounting principles generally accepted in the United States of America.

2. To consider the Harbors Division's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements.

3. To perform tests of the Harbors Division's 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.

Scope of Audit

We performed our audits of the Harbors Division's financial statements as of and for the years ended June 30, 2018 and 2017, 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.

As part of the audit of the Harbors Division's financial statements, we considered the Harbors Division's internal control over financial reporting to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We also performed tests of the Harbors Division's 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.

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Organization of Report

This report has been organized into three parts as follows:

1. The Introduction Section describes briefly the objectives and scope of our audit and the organization and contents of this report.

2. The Financial Section includes management's discussion and analysis, the Harbors Division's financial statements and the related notes, and other supplementary information as of and for the years ended June 30, 2018 and 2017, and our independent auditors' report thereon.

3. The Internal Control and Compliance Section contains our independent auditors' report on the Harbors Division's internal control over financial reporting and on compliance and other matters based on an audit of the financial statements performed in accordance with *Government Auditing Standards*.

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We would like to take this opportunity to express our appreciation for the courtesy and assistance extended to us by the personnel of the Harbors Division during the course of our engagement. Should you wish to discuss any of the matters contained herein, we will be pleased to meet with you at your convenience.

Very truly yours,

KKDLY LLC

PART II

FINANCIAL SECTION

KKDLY LLC
CERTIFIED PUBLIC ACCOUNTANTS

Independent Auditors' Report

The Auditor
State of Hawaii:

Report on the Financial Statements

We have audited the accompanying financial statements of the Harbors Division, Department of Transportation, State of Hawaii (the Harbors Division), an enterprise fund of the State of Hawaii, which comprise the statements of net position as of June 30, 2018 and 2017, and the related statements of revenues, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Harbors Division as of June 30, 2018 and 2017, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

Change in Accounting Principles

As discussed in Note 2 to the financial statements, the Harbors Division adopted the provisions of Governmental Accounting Standards Board Statement (GASB) No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, and GASB Statement No. 85, *Omnibus 2017*, effective July 1, 2017. Our opinion is not modified with respect to these matters.

Relationship to the State of Hawaii

As discussed in Note 1 to the financial statements, the financial statements of the Harbors Division are intended to present the financial position, the changes in financial position and, where applicable, cash flows of only that portion of the business-type activities and proprietary fund type of the State of Hawaii that is attributable to the transactions of the Harbors Division. They do not purport to, and do not, present fairly the financial position of the State of Hawaii as of June 30, 2018 and 2017, and the changes in its financial position, or, where applicable, its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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 audits 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 audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Harbors Division's basic financial statements. The supplementary information included in Schedules 1 through 4 is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The supplementary information 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 audits 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 supplementary information 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 December 6, 2018, on our consideration of the Harbors Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is 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 Harbors Division'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 Harbors Division's internal control over financial reporting and compliance.

KKDLY LLC

Honolulu, Hawaii
December 6, 2018

Harbors Division
Department of Transportation
State of Hawaii
(An Enterprise Fund of the State of Hawaii)

Management's Discussion and Analysis

June 30, 2018 and 2017

The following Management's Discussion and Analysis of the Harbors Division, Department of Transportation, State of Hawaii (the Harbors Division), an enterprise fund of the State of Hawaii, presents the reader with an introduction and overview of the Harbors Division's financial performance for the fiscal years ended June 30, 2018 and 2017. This discussion has been prepared by management and should be read in conjunction with the financial statements, and the notes thereto, which follow this section.

The statewide system of commercial harbors consists of ten harbors on six islands. The system plays a vital role in Hawaii's economy as the ports serve as the primary means for goods to enter and exit the state. Hawaii imports approximately 80% of what it consumes, the majority of which enters the state through the commercial harbors system.

The Harbors Division is self-sustaining. The Department of Transportation, State of Hawaii (DOT), is authorized to impose and collect rates and charges for the use of the harbors system and its properties to generate revenues to fund operating expenses. The Capital Improvements Program (CIP) is also funded by the Harbors Division's revenues and proceeds from the issuance of harbors system revenue bonds.

Using the Financial Statements

The Harbors Division is accounted for as a proprietary fund and utilizes the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The proprietary fund includes the enterprise fund type, which is used to account for the acquisition, operation, and maintenance of government facilities and services that are entirely or predominantly supported by user charges.

The Harbors Division's financial report includes three financial statements; the statements of net position, the statements of revenues, expenses, and changes in net position, and the statements of cash flows. The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) as promulgated by the Governmental Accounting Standards Board (GASB).

Change in Accounting Principles

Effective July 1, 2017, the Harbors Division adopted the provisions of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (Statement No. 75). This statement addresses accounting and financial reporting for other postemployment benefits (OPEB) that are provided to the employees of state and local governmental employers through trusts or equivalent arrangements meeting certain criteria. This statement also establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures.

Simultaneously with the adoption of Statement No. 75, the Harbors Division adopted the provisions of GASB Statement No. 85, *Omnibus 2017* (Statement No. 85). The objective of this statement is to address practice issues that have been identified during the implementation and application of certain GASB statements.

As further discussed in Note 2 to the financial statements, the restatement of the comparative financial data for the prior periods presented was not practical due to the unavailability of information from the plan. The cumulative effect of applying the provisions of this statement has been reported as a restatement of the beginning net position for the year ended June 30, 2018. Specifically, the adoption of Statements No. 75 and No. 85 had the effect of decreasing net position as of June 30, 2017 by $16.8 million. In addition, the Harbors Division recorded a deferred outflow of resources of $2.5 million, a net other postemployment benefits liability of $38.0 million, and a deferred inflow of resources of $49,000 as of June 30, 2018 in the accompanying financial statements.

Financial Highlights

- The Harbors Division's net position at June 30, 2018 and 2017 amounted to $890.1 million and $817.8 million, as restated, respectively. Net position increased by $72.3 million in fiscal year 2018, an increase of 8.8%. Net position, as restated, increased by $19.9 million or 2.5% in fiscal year 2017.

- Operating income amounted to $78.5 million in fiscal year 2018, an increase of $29.3 million or 59.6% as compared to 2017. Operating income amounted to $49.2 million in fiscal year 2017, a decrease of $6.6 million or 11.8% as compared to 2016.

A summary of operations and changes in net position for the fiscal years ended June 30, 2018, 2017, and 2016 follows:

Table 1
Condensed Statements of Revenues,
Expenses, and Changes in Net Position
(In Thousands)

	Year Ended June 30			2018-2017		2017-2016	
	2018	2017	2016	Increase (decrease)	% Change	Increase (decrease)	% Change
Operating revenues	$ 165,111	$ 137,621	$ 130,126	$ 27,490	20.0%	$ 7,495	5.8%
Nonoperating revenues	5,488	2,431	1,725	3,057	125.8	706	40.9
Total revenues	170,599	140,052	131,851	30,547	21.8	8,201	6.2
Depreciation expense	27,019	30,869	26,033	(3,850)	(12.5)	4,836	18.6
Other operating expenses	59,601	57,583	48,330	2,018	3.5	9,253	19.1
Nonoperating expenses	11,845	15,160	18,728	(3,315)	(21.9)	(3,568)	(19.1)
Total expenses	98,465	103,612	93,091	(5,147)	(5.0)	10,521	11.3
Income before capital contributions	72,134	36,440	38,760	35,694	98.0	(2,320)	(6.0)
Capital contributions	153	300	-	(147)	(49.0)	300	100.0
Change in net position	72,287	36,740	38,760	35,547	96.8	(2,020)	(5.2)
Net position, beginning of year, as previously reported	834,672	797,932	759,758	36,740	4.6	38,174	5.0
Restatement	(16,825)	-	-	(16,825)	(100.0)	-	0.0
Net position, beginning of year, as restated	817,847	797,932	759,758	19,915	2.5	38,174	5.0
Net position, end of year	$ 890,134	$ 834,672	$ 798,518	$ 55,462	6.6	$ 36,154	4.5

Operating Revenues

Total operating revenues for fiscal year 2018 were $165.1 million compared to $137.6 million for fiscal year 2017. Total operating revenues for fiscal year 2017 were $137.6 million compared to $130.1 million for fiscal year 2016. Operating revenues consist primarily of service revenues and rental revenues, which accounted for 82.4% and 16.8%, respectively, in fiscal year 2018, and 82.2% and 16.6%, respectively, in fiscal year 2017, of the Harbors Division's total operating revenues.

Service Revenues

Service revenues are directly related to cargo and ship operations. Service revenues include wharfage, passenger fees, and other ship related fees. Service revenues in fiscal years 2018 and 2017 were $136.0 million and $113.2 million, respectively.

Service revenues for fiscal year 2018 increased $22.9 million or 20.2% as compared to fiscal year 2017. Wharfage revenue from cargo movements increased by $22.8 million from $95.4 million in fiscal year 2017 to $118.2 million in fiscal year 2018 due primarily to an increase of 15% in tariff rate that took effect on October 1, 2017. This increase was applied to the rates then in effect.

Service revenues for fiscal year 2017 increased $7.2 million or 6.8% as compared to fiscal year 2016. Wharfage revenue from cargo movements increased by $6.7 million from $88.7 million in fiscal year 2016 to $95.4 million in fiscal year 2017 due primarily to two increases in tariff rates that took effect during fiscal year 2017, one increase of 3% on July 1, 2016 and the other increase of 17% on February 1, 2017. Both increases were applied to the rates then in effect. In addition, passenger fees increased by $1.1 million as described below.

Passenger volumes (inbound and outbound) for both fiscal years 2018 and 2017 were approximately 1.08 million passengers. Embark and debark fee remained at $7.50 per passenger in fiscal year 2018.

Passenger fee revenue increased by $1.1 million or 15.7% from $7.0 million in 2016 to $8.1 million in fiscal year 2017, due primarily to the change in the embark and debark fee to $7.50 per passenger, effective July 1, 2016, from that assessed through June 30, 2016 of $7.00 per passenger, and by an increase of approximately 0.08 million passengers in fiscal year 2017.

Rental Revenues

Rental revenues for fiscal year 2018 were $27.7 million, an increase from fiscal year 2017 of approximately $4.8 million, due primarily to a 15% pipeline tariff rate increase, effective October 1, 2017.

Rental revenues for fiscal year 2017 were $22.9 million, a decrease from fiscal year 2016 of approximately $0.4 million, due to a settlement of a tenant dispute.

Operating Expenses

Operating expenses, excluding depreciation expense, for fiscal years 2018 and 2017 amounted to $59.6 million and $57.6 million, respectively. The increase in operating expenses for fiscal year 2018 in comparison to fiscal year 2017 of $2.0 million or 3.5% was due primarily to increases in harbor operations costs $1.8 million and personnel services costs of $431,000.

Operating expenses, excluding depreciation expense, for fiscal years 2017 and 2016 amounted to $57.6 million and $48.3 million, respectively. The increase in operating expenses for fiscal year 2017 in comparison to fiscal year 2016 of $9.3 million or 19.1% was due primarily to increases in harbors operations costs of $5.3 million and personnel services costs of $2.5 million, offset by a decrease in harbor operations costs of $1.5 million.

Harbor operations costs for fiscal year 2018 increased by $1.8 million as compared to fiscal year 2017 due to primarily to an increase in expenses required by Hawaii statutes of $1.6 million. Harbor operations costs for fiscal year 2017 increased by $5.3 million as compared to fiscal year 2016 due primarily to the increases in expenses required by Hawaii statutes of $6.8 million, which was partially offset by a decrease in harbor operating costs of approximately $1.5 million. Harbor operating costs decreased by approximately $1.5 million, due primarily to the non-recurrence of approximately $0.6 million paid to third-party contractors incurred for fiscal year 2016, for the costs of storm drain cleaning costs at facilities located on the island of Oahu, to comply with the 2014 EPA Consent Decree. During fiscal year 2017, these tasks were performed by Harbors Division personnel. Utilities costs, such as electricity, water charges, and sewer fees and waste disposal fees also decreased.

Personnel services costs for fiscal year 2018 increased by $431,000 as compared to fiscal year 2017 due primarily to the increase in OPEB expense with the adoption of GASB Statement Nos. 75 and 85, and an increase in pension expense. In fiscal year 2017, personnel services increased by $2.5 million as compared to fiscal year 2016 due primarily to an increase in pension expense, as well as increases in wages and employee benefits costs attributable to the collective bargaining unit agreements effective April 1, 2017.

Harbors Division
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Management's Discussion and Analysis

June 30, 2018 and 2017

A summary of the Harbors Division's net position at June 30, 2018, 2017, and 2016 are shown below:

Table 2
Condensed Statements of Net Position
(In Thousands)

	As of June 30			2018-2017		2017-2016	
	2018	**2017**	**2016**	**Increase (decrease)**	**% Change**	**Increase (decrease)**	**% Change**
Assets:							
Current and other assets	$ 427,433	$ 446,802	$ 421,321	$ (19,369)	-4.3%	$ 25,481	6.0%
Capital assets, net	921,367	829,720	795,090	91,647	11.0	34,630	4.4
Total assets	1,348,800	1,276,522	1,216,411	72,278	5.7	60,111	4.9
Deferred outflows of resources	13,381	15,574	6,908	(2,193)	(14.1)	8,666	125.4
Liabilities:							
Current liabilities	72,976	57,103	46,709	15,873	27.8	10,394	22.3
Long-term liabilities	398,460	399,699	376,541	(1,239)	(0.3)	23,158	6.2
Total liabilities	471,436	456,802	423,250	14,634	3.2	33,552	7.9
Deferred inflows of resources	611	622	1,551	(11)	(1.8)	(929)	(59.9)
Net position:							
Net investment in capital assets	580,855	528,734	528,706	52,121	9.9	28	0.0
Restricted	204,790	143,999	76,907	60,791	42.2	67,092	87.2
Unrestricted	104,489	161,939	192,905	(57,450)	(35.5)	(30,966)	(16.1)
Total net position	$ 890,134	$ 834,672	$ 798,518	$ 55,462	6.6	$ 36,154	4.5

Net Position

The largest portion of the Harbors Division's net position (65.3% and 63.3% at June 30, 2018 and 2017, respectively), net investment in capital assets, represents its investment in capital assets (e.g., land, wharves, buildings, improvements, and equipment), less related indebtedness outstanding to acquire those capital assets. The Harbors Division uses these capital assets to provide services to its users of the harbors system; consequently, these assets are not available for future spending. Although the Harbors Division's net investment in its capital assets is reported net of related debt, the resources required to repay this debt must be provided annually from operations, since it is unlikely the capital assets themselves will be liquidated to pay for such liabilities.

The restricted portion of the Harbors Division's net position (23.0% and 17.3% at June 30, 2018 and 2017, respectively) represents bond reserve and other funds that are subject to external restrictions on how they may be used.

The unrestricted portion of the Harbors Division's net position (11.7% and 19.4% at June 30, 2018 and 2017, respectively) may be used to meet any of the Harbors Division's ongoing operations or to fund capital improvement projects.

The change in net position is an indicator of whether the overall fiscal condition of the Harbors Division improved or worsened during the fiscal year. The change in net position may serve over time as a useful indicator of the Harbor Division's financial position. Net position or the amount of total assets and deferred outflows of resources that exceed liabilities and deferred inflows of resources amounted to $890.1 million at June 30, 2018, an increase in net position of $72.3 million or 8.8% from 2017. Net position, as restated, amounted to $817.8 million at June 30, 2017, an increase in net position of $19.9 million or 2.5% from 2016. Net position, as restated, amounted to $797.9 million at June 30, 2016.

Capital Assets and Debt Administration

Capital Assets

As of June 30, 2018 and 2017, the Harbors Division had $921.4 million and $829.7 million, respectively invested in capital assets as shown in Table 3. There was a net increase (additions, deductions, and depreciation) of $91.6 million in 2018 from the prior year, and a net increase in 2017 of $34.6 million from 2016.

Table 3
Capital Assets
(In Thousands)

	As of June 30			2018-2017		2017-2016	
	2018	2017	2016	Increase (decrease)	% Change	Increase (decrease)	% Change
Land and land improvements	$ 600,035	$ 566,713	$ 557,918	$ 33,322	5.9%	$ 8,795	1.6%
Wharves	328,693	278,758	269,153	49,935	17.9	9,605	3.6
Other improvements	116,094	91,114	91,114	24,980	27.4	-	-
Buildings	116,912	113,923	110,578	2,989	2.6	3,345	3.0
Equipment	26,526	25,831	20,865	695	2.7	4,966	23.8
Total at cost	1,188,260	1,076,339	1,049,628	111,921	10.4	26,711	2.5
Less accumulated depreciation	(412,532)	(386,017)	(355,149)	(26,515)	6.9	(30,868)	8.7
	775,728	690,322	694,479	85,406	12.4	(4,157)	(0.6)
Construction in progress	145,639	139,398	100,611	6,241	4.5	38,787	38.6
Total capital assets, net	$ 921,367	$ 829,720	$ 795,090	$ 91,647	11.0	$ 34,630	4.4

Depreciation expense amounted to $27.0 million and $30.9 million for the fiscal years 2018 and 2017, respectively, a decrease of $3.9 million.

Major capital asset additions to the statewide harbors system for the fiscal year ended June 30, 2018, included the following:

- $32.8 million Parcel 4 situated in the former Kapalama Military Reservation area
- $5.6 million Shed Modifications/Improvements at Pier 1, Hilo Harbor, Hawaii Island
- $669,000 Substructure Repairs at Pier 34, Honolulu Harbor, Oahu Island
- $163,000, Pavement Repairs at Fort Armstrong, Honolulu Harbor, Oahu Island
- $320,100 Building and Yard Rehabilitation at Piers 34/35, Honolulu Harbor, Oahu Island
- $49.9 million Design and Construction of Pier 4 Inter-island Cargo Terminal Facility, Hilo Harbor, Hawaii Island

In addition to those capital asset additions, the Harbors Division is currently in the process of constructing the following projects statewide:

- $164.0 million, Construction of Kapalama Container Terminal Yard, Honolulu Harbor, Oahu Island
- $26.3 million Installation of Energy Conservation Measures
- $4.0 million Tower Demolition and Water System Improvements, Hilo Harbor, Hawaii Island

Major capital asset additions to the statewide harbors system for the fiscal year ended June 30, 2017, included the following:

- $14.9 million Design and Construction of Piers 12 and 15 Improvements, Honolulu Harbor, Oahu Island
- $1.4 million Piers 31a and 32 Installation of Fire Suppression System, Honolulu Harbor, Oahu Island
- $2.0 million Improvements to a State-wide Maritime Wireless System

The Harbors Division is committed under contracts awarded for capital improvement projects totaling $179.2 million as of June 30, 2018.

Additional information regarding the Harbors Division's capital assets can be found in Note 4 to the financial statements.

Indebtedness

Harbors System Revenue Bonds and Reimbursable General Obligation Bonds

Harbor system revenue bonds have been issued pursuant to the *Certificate of the Director of Transportation Providing for the Issuance of 1997 State of Hawaii Harbor Revenue Bonds* (the 1997 Certificate) and are collateralized by a charge and lien on the Harbors Division's revenues. The proceeds from these bonds are used for harbor and waterfront improvements. As of June 30, 2018 and 2017, outstanding harbor system revenue bonds amounted to $293.6 million and $309.5 million, respectively.

On July 5, 2017, the Harbors Division issued $22,425,000 in Series 2016 D Revenue Refunding Bonds, which bear interest at 3.09% with a maturity date of July 1, 2027. Proceeds were used to refund $22,315,000 of 2007 A Bonds. The refunding of 2007 A Bonds provided net present value savings of approximately $2,959,000.

On December 6, 2016, the Harbors Division issued $14,565,000 in Series 2016 A, $68,535,000 in Series 2016 B, and $8,135,000 in Series 2016 C Refunding Bonds, which bear interest from 1.99% to 2.89% with maturity dates through January 2031. The Series A 2016 Revenue Bonds refunded $16,195,000 of 2004 B Bonds, the Series B 2016 Revenue Bonds refunded $71,625,000 of 2006 A Bonds, and the Series C 2016 Revenue Bonds refunded $7,365,000 of 2007 A Bonds. The refunding of 2004 B, 2006 A, and 2007 A Bonds provided net present value savings of approximately $12,932,000.

Reimbursable general obligation bonds are general obligations of the State, but since the proceeds were used to finance the harbor and waterfront improvements, the Harbors Division is required to reimburse the State's general fund for the payment of principal and interest on such bonds. As of June 30, 2018 and 2017, outstanding reimbursable general obligation bonds amounted to $23.3 million and $25.4 million, respectively. There have been no issuances of reimbursable general obligation bonds to finance the harbor and waterfront improvements during fiscal years 2018 and 2017.

Additional information regarding the Harbors Division's indebtedness can be found in Notes 5, 6, 7, and 8 to the financial statements.

Credit Rating and Bond Insurance

All harbor system revenue bonds issued since 1997 through June 30, 2010 have been issued with bond insurance. A new reserve policy replaced all previously issued surety bonds and the portion of the reserve requirement allocable to the Series B of 2010 Revenue Bonds. The surety policy was amended effective August 2, 2013 to include the reserve requirement allocable to the Series A of 2013 Revenue Refunding Bonds. The Series A of 2010 Revenue Bonds are secured by a cash deposit of $11.5 million.

As of June 30, 2018, the underlying ratings for harbor system revenue bonds were as follows:

- Standard and Poor's AA-
- Moody's Investors Service A1
- Fitch IBCA, Inc. AA-

Ratings made by Standard and Poor's, Moody's Investors Service, and Fitch IBCA, Inc. may be changed, suspended, or withdrawn as a result of changes in, or unavailability of, information. Ratings provided by these rating companies are not "market ratings," as the ratings are not a recommendation to buy, hold, or sell any security.

Bond Covenants

Bond covenants allow the issuance of additional debt, on parity, as to a lien on the net revenues of the Harbors Division provided certain net revenue ratios are met. Net revenues of the Harbors Division must be at least 1.25 times the debt service requirements under the 1997 Certificate.

The Harbors Division coverage ratio as of June 30, 2018 was 4.40 under the 1997 Certificate as compared to the ratio of 3.15 as of June 30, 2017.

Request for Information

The financial report is designed to provide a general overview of the Harbors Division's finances for all interested parties. Questions concerning any of the information provided in this report or requests for additional information should be addressed in writing to the Harbors Administrator, State of Hawaii, Department of Transportation, Harbors Division, 79 S. Nimitz Highway, Honolulu, Hawaii, 96813, or by e-mail to *davis.k.yogi@hawaii.gov.*

Harbors Division

Department of Transportation

State of Hawaii

(An Enterprise Fund of the State of Hawaii)

Statements of Net Position

June 30, 2018 and 2017

Assets:	**2018**	**2017**
Current assets:		
Cash and cash equivalents	$ 185,531,299	$ 208,340,548
Receivables, less allowance for doubtful accounts of $3,663,962 in 2018 and $5,034,493 in 2017	15,059,672	11,521,736
Notes receivable, less allowance for doubtful accounts of $2,976,588 in 2018 and $3,760,600 in 2017	391,814	-
Interest receivable	3,396,636	101,576
Due from other State agencies	680,979	-
Other current assets	1,317,535	8,465,522
	206,377,935	228,429,382
Restricted assets:		
Cash and cash equivalents−restricted for debt service payments and reserve requirements	34,400,642	34,322,403
Total current assets	240,778,577	262,751,785
Noncurrent assets:		
Cash and cash equivalents−restricted for*:*		
Capital improvement projects	170,390,363	167,286,516
Other	16,263,858	16,763,020
	186,654,221	184,049,536
Capital assets:		
Nondepreciable assets	311,813,847	278,993,847
Depreciable assets, net	463,914,689	411,328,207
Construction in progress	145,638,900	139,398,063
Total capital assets, net	921,367,436	829,720,117
Total noncurrent assets	1,108,021,657	1,013,769,653
Total assets	1,348,800,234	1,276,521,438
Deferred Outflows of Resources:		
Related to pension	8,258,975	12,053,213
Related to other postemployment benefits	2,507,481	-
Deferred charge on refunding, net	2,614,579	3,520,610
Total deferred outflows of resources	13,381,035	15,573,823

Liabilities:	**2018**	**2017**
Current liabilities (payable from current assets):		
Accounts payable	$ 6,906,515	$ 7,570,939
Contracts payable, including retainages	2,009,850	1,857,111
Capital lease obligation	812,396	716,734
Accrued interest payable - capital lease obligation	542,199	554,699
Accrued workers' compensation	93,423	258,383
Accrued vacation	751,790	724,575
Due to other State agencies	28,832,198	8,410,930
	39,948,371	20,093,371
Current liabilities (payable from restricted assets):		
Contracts payable, including retainages	5,350,104	9,526,125
Revenue bonds payable, current maturities	16,779,424	16,034,641
General obligation bonds payable, current maturities	2,227,919	2,122,232
Accrued interest payable - revenue bonds	6,190,609	6,899,600
Security deposits	2,479,452	2,426,748
	33,027,508	37,009,346
Total current liabilities	72,975,879	57,102,717
Long-term liabilities:		
Accrued workers' compensation	824,367	382,509
Net pension liability	34,412,958	35,453,242
Net other postretirement benefits liability	38,004,809	18,761,705
Long-term debt, less current maturities:		
Revenue bonds payable, net	276,817,414	293,712,804
General obligation bonds payable	21,026,716	23,254,635
Capital lease obligation	25,463,529	26,275,925
Accrued vacation	1,909,862	1,858,258
Total long-term liabilities	398,459,655	399,699,078
Total liabilities	471,435,534	456,801,795
Deferred Inflows of Resources:		
Related to pension	562,441	621,673
Related to other postemployment benefits	48,856	-
Total deferred inflows of resources	611,297	621,673
Net Position:		
Net investment in capital assets	580,854,616	528,733,989
Restricted - revenue bond requirements	34,400,642	34,322,403
Restricted - for capital improvement projects	170,390,363	109,676,283
Unrestricted	104,488,817	161,939,118
Total net position	$ 890,134,438	$ 834,671,793

See accompanying notes to financial statements.

Harbors Division

Department of Transportation

State of Hawaii

(An Enterprise Fund of the State of Hawaii)

Statements of Revenues, Expenses, and Changes in Net Position

Years Ended June 30, 2018 and 2017

	2018	2017
Operating revenues, net:		
Services	$ 136,039,047	$ 113,161,394
Rentals	27,684,442	22,878,352
Others	1,387,737	1,581,308
	165,111,226	137,621,054
Operating expenses:		
Depreciation	27,019,188	30,868,569
Harbor operations	23,466,534	21,696,225
Personnel services	21,921,585	21,490,091
State of Hawaii, surcharge for central service expenses	6,068,244	4,900,977
Maintenance	4,124,370	3,994,558
General administration	2,685,408	2,944,090
Department of Transportation, general administration expenses	1,335,022	2,557,828
	86,620,351	88,452,338
Operating income	78,490,875	49,168,716
Nonoperating revenues (expenses):		
Interest expense	(11,110,200)	(13,648,896)
Interest income	5,488,391	2,431,114
Amortization of bond premium, discount, and deferred charge on refunding	(725,424)	(797,634)
Loss on disposal of capital assets	(9,657)	(713,542)
	(6,356,890)	(12,728,958)
Income before capital contributions	72,133,985	36,439,758
Capital contributions	153,371	300,000
Change in net position	72,287,356	36,739,758
Net position, beginning of year, as previously reported	834,671,793	797,932,035
Restatement	(16,824,711)	-
Net position, beginning of year, as restated	817,847,082	797,932,035
Net position, end of year	$ 890,134,438	$ 834,671,793

See accompanying notes to financial statements.

Harbors Division

Department of Transportation

State of Hawaii

(An Enterprise Fund of the State of Hawaii)

Statements of Cash Flows

Years Ended June 30, 2018 and 2017

	2018	2017
Cash flows from operating activities:		
Cash received from customers	$ 180,864,468	$ 142,071,368
Cash paid to suppliers	(38,418,050)	(34,997,469)
Cash paid to employees	(18,684,590)	(17,574,166)
Net cash provided by operating activities	123,761,828	89,499,733
Cash flows from capital and related financing activities:		
Acquisition and construction of capital assets	(112,270,285)	(41,186,616)
Principal paid on bonds	(40,407,232)	(107,157,854)
Proceeds from bond issuance	22,425,000	91,235,000
Interest paid on bonds and capital lease obligation	(15,112,233)	(17,637,175)
Principal paid on capital lease obligation	(716,734)	-
Net cash used in capital and related financing activities	(146,081,484)	(74,746,645)
Cash flows provided by investing activities:		
Interest received	2,193,331	2,527,930
Net (decrease) in cash and cash equivalents	(20,126,325)	17,281,018
Cash and cash equivalents at beginning of year	426,712,487	409,431,469
Cash and cash equivalents at end of year	$ 406,586,162	$ 426,712,487

(Continued on following page)

Harbors Division

Department of Transportation

State of Hawaii

(An Enterprise Fund of the State of Hawaii)

Statements of Cash Flows (Continued)

Years Ended June 30, 2018 and 2017

	2018	2017
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$ 78,490,875	$ 49,168,716
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	27,019,188	30,868,569
Provision for doubtful accounts	(1,400,531)	(195,112)
Changes in assets, deferred outflows, liabilities, and deferred inflows:		
Receivables	(3,210,198)	304,595
Other current assets	-	59,872
Deferred outflows of resources	1,176,757	(10,165,287)
Payables	(511,685)	1,133,595
Accrued workers' compensation	276,898	51,402
Accrued vacation	78,819	95,156
Due to other State agencies	20,421,268	5,201,381
Security deposits	52,704	104,451
Net pension liability	(1,040,284)	12,356,505
Other postretirement benefits liability	2,418,393	1,444,618
Deferred inflows of resources	(10,376)	(928,728)
Net cash provided by operating activities	$ 123,761,828	$ 89,499,733

Supplemental disclosure of noncash operating activities:

As described in Note 2, the adoption of the GASB OPEB standards resulted in the restatement of net position ($16,824,711) as of June 30, 2017, and the recording of deferred outflows of resources ($2,507,481), net other postemployment benefits liability ($38,004,809), and deferred inflows of resources ($48,856), as of June 30, 2018.

Supplemental disclosure of noncash capital and related financing activities:	2018	2017
Amounts included in contracts payable for the acquisition of capital assets	$ 5,350,104	$ 9,526,125
Interest capitalized in capital assets	$ 3,280,542	$ 3,919,715
Other assets utilized for the acquisition of capital assets	$ 7,147,987	$ 17,780,042
Capital lease obligation	$ -	$ 26,992,659
Amortization of bond premium, discount, and deferred charge on refunding	$ (725,424)	$ (797,634)
Capital contributions	$ 153,371	$ 300,000

See accompanying notes to financial statements.

1. Financial Reporting Entity

In 1959, the Harbors Division was established within the Department of Transportation of the State of Hawaii (the DOT) effective July 1, 1961. All functions and powers to administer, control, and supervise all State of Hawaii (the State) harbors and water navigational facilities were assigned to the Director of the DOT on that date.

The Harbors Division is part of the DOT, which is part of the executive branch of the State. The State Comptroller maintains the central accounts for all State funds and publishes financial statements for the State annually, which include the Harbors Division's financial activities. The accompanying financial statements present only the activities of the Harbors Division and are not intended to present fairly the financial position of the State and the changes in its financial position and cash flows of its business-type activities.

The "Certificate of the Director of Transportation Providing for the Issuance of 1997 State of Hawaii Harbor Revenue Bonds," dated March 1, 1997 (1997 Certificate), defines the "Undertaking" as all of the harbor and waterfront improvements and other properties under the jurisdiction, control, and management of the Harbors Division, except those principally used for recreation and the landing of fish.

2. Summary of Significant Accounting Policies

The financial statements of the Harbors Division have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Harbors Division's significant accounting policies are described below.

Measurement Focus and Basis of Accounting

An enterprise fund is used to account for the acquisition, operation, and maintenance of government facilities and services that are entirely or predominantly supported by user charges. The Harbors Division's operations are accounted for using the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Cash and Cash Equivalents

Cash and cash equivalents include all cash and investments with original maturities of three months or less and amounts held in State Treasury.

Amounts Held in State Treasury

The State's investments held in the State Treasury are reported at fair value within the fair value hierarchy established by GAAP. Investment earnings are allocated to the pool participants, including the Harbors Division, based upon their equity interest in the pooled monies.

Fair Value Measurements

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

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - Inputs other than quoted market prices included in Level 1 that are observable for an asset or liability, either directly or indirectly.

Level 3 - Unobservable inputs for an asset or liability reflecting the reporting entity's own assumptions. Level 3 inputs are used to measure fair value to the extent that observable Level 1 or 2 inputs are not available.

Restricted Assets

Restricted assets consist primarily of amounts for the principal and interest accumulated to make debt service payments, amounts restricted for capital improvement projects including unspent bond proceeds, amounts restricted for bond reserve requirements, security deposits, and customer advances.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are reported at their gross value when earned, reduced by an allowance for doubtful accounts.

Accounts are written-off upon the approval of the State Department of the Attorney General, when it believes, after considering economic conditions, business conditions, and collection efforts, that the accounts are uncollectible.

The allowance for doubtful accounts is increased by charges to operating income and decreased by charge-offs (net of recoveries). Management's periodic evaluation of the adequacy of the allowance is based on the adverse situations that may affect the customer's ability to repay, historical experience, and current economic conditions. Past due status is determined based on contractual terms.

Risk Management

The Harbors Division is exposed to various risks for losses related to, among other risks, torts; theft of, damage to, or destruction of assets; errors or omissions; natural disasters; and workers' compensation. A liability for a claim for a risk of loss is established if information indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. The estimated reserve for losses and loss adjustment costs includes the accumulation of estimates for losses and claims reported prior to fiscal year-end, nonincremental estimates (based on projections of historical developments) of claims incurred but not reported, and nonincremental estimates of costs for investigating and adjusting all incurred and unadjusted claims. Amounts reported are subject to the impact of future changes in economic and social conditions. The Harbors Division believes that, given the inherent variability in any such estimates, the reserves are within a reasonable and acceptable range of adequacy. Reserves are continually monitored and reviewed and, as settlements are made and reserves adjusted, the differences are reported in current operations.

Capital Assets and Depreciation

Capital assets are stated at cost. Depreciation of capital assets is computed using the straight-line method over the estimated useful lives of the assets. Disposals of assets are recorded by removing the cost and related accumulated depreciation from the accounts with the resulting gain or loss reflected in nonoperating revenues (expenses).

Capital assets and their related estimated useful lives used to compute depreciation are as follows:

	Useful Lives	Capitalization Threshold
Land improvements	10 – 100 years	$ 100,000
Wharves	10 – 100 years	100,000
Buildings	5 – 50 years	100,000
Other improvements	5 – 50 years	100,000
Equipment	5 – 20 years	5,000

Maintenance and repairs, as well as minor replacements, renewals, and betterments, are charged to operations. Major renewals, replacements, and betterments which extend the service lives of the related assets are capitalized in the year incurred. Interest cost is capitalized during the period of construction for capital improvement projects, except those projects funded by grants from the State or the Federal government.

Unamortized Debt Premium (Discount)

Debt premium (discount) is amortized using the effective interest rate method over the term of the related debt, and the unamortized balance is reflected as an addition or deduction to the related liabilities in the statements of net position.

Refunding of Debt

The difference between the reacquisition price and the net carrying amount of the old debt is deferred and amortized as a component of interest expense in a systematic and rational manner over the remaining life of the old debt or the life of the new debt, whichever is shorter. The deferred charge on refunding amounted to $2,614,579 and $3,520,610 at June 30, 2018 and 2017, respectively, and are reported as deferred outflows of resources in the statements of net position.

Deferred Outflows of Resources and Deferred Inflows of Resources

Deferred outflows (inflows) of resources represent a consumption of (benefit to) net position that applies to a future period. The Harbors Division defers recognition of the charge on refunding related to issuance of its revenue bonds and amortizes these costs over the life of the bonds using the effective interest rate method. The deferred outflow of resources related to pensions and other postemployment benefits (OPEB) resulted from changes in assumptions, the net difference between projected and actual earnings on pension plan investments, differences between expected and actual experiences, and changes in proportion and differences between contributions and proportionate share of contributions, which will be amortized over five years, and the Harbors Division's contributions to the pension and OPEB plans subsequent to the measurement date of the actuarial valuations for the pension and OPEB plans which will be recognized as a reduction of the net pension liability and net OPEB liability in the subsequent fiscal year. The deferred inflow of resources related to pension and OPEB resulted from differences between expected and actual experiences, changes in proportion and differences between contributions and proportionate share of contributions, and the net difference between projected and actual earnings on pension and OPEB plan investments, which will be amortized over five years.

Accrued Vacation

The Harbors Division accrues all vacation and compensatory pay at current salary rates, including additional amounts for certain salary-related expenses associated with the payment of compensated absences. Vacation is earned at the rate of 168 hours per calendar year, depending on an employee's date of hire. Accumulation of such vacation credits is limited to 720 hours at calendar year-end and is convertible to pay upon termination of employment.

Net Position

Net position is reported in three categories as follows:

Net investment in capital assets - represents the Harbors Division's investment in capital assets, less related indebtedness outstanding to acquire those capital assets.

Restricted - represents revenue bond reserves and capital project funds that are subject to external restrictions on how they may be used.

Unrestricted - may be used to meet any of the Harbors Division's ongoing operations or fund capital improvement projects.

Operating Revenues

Operating revenues are those that result from providing goods and services and are reported net of bad debt. The recovery of bad debts for the years ended June 30, 2018 and 2017 was approximately $1,400,000 and $195,000, respectively. Operating revenues also exclude revenues related to capital and related financing activities, noncapital financing activities, and investing activities.

As of June 30, 2018, the Harbors Division has pledged its future operating revenues, net of certain operating expenses, to repay $293,610,000 in Harbor Revenue Bonds. Proceeds from the bonds provided financing for the construction of new facilities and the improvement of existing facilities related to the State's commercial harbors. The bonds are payable solely from the Harbors Division's operating revenues and are payable through July 2040.

The total principal and interest remaining to be paid on the bonds is approximately $432,878,000 as of June 30, 2018. Principal and interest paid (as defined by the Harbor revenue bond debt service requirements under the 1997 certificate) and total operating revenues, net of certain operating expenses, were approximately $29,114,000 and $115,599,000 respectively, for the year ended June 30, 2018, and approximately $31,176,000 and $90,440,000 respectively, for the year ended June 30, 2017.

Operating Expenses

All expenses related to operating the Harbors Division are reported as operating expenses. Interest income, interest expense, gain (loss) on disposal of capital assets, and the amortization of bond premium, discount, and deferred charge on refunding are reported as nonoperating revenues (expenses).

When an expense is incurred for which unrestricted and restricted resources are available to pay the expense, it is the Harbors Division's policy to apply the expense to unrestricted resources first, then to restricted resources.

Capital Contributions

The Harbors Division receives federal grants restricted for capital asset acquisition and facility development. Grants are considered earned as the related allowable expenditures are incurred, and are reported in the statements of revenues, expenses, and changes in net position, after nonoperating revenues (expenses) as capital contributions.

Pension

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pension, and pension expense, information about the fiduciary net position of the Harbor Division's participation in the Employees' Retirement System of the State of Hawaii (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. The ERS's investments are reported at fair value.

Other Postemployment Benefits

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 Harbor Division's participation in the Hawaii Employer-Union Health Benefits Trust Fund (the 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 the benefit terms. The EUTF's investments are reported at fair value.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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.

Change in Accounting Principles

Effective July 1, 2017, the Harbors Division adopted the provisions of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (Statement No. 75). This statement addresses accounting and financial reporting for OPEB that are provided to the employees of state and local governmental employers through trusts or equivalent arrangements meeting certain criteria. This statement also establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expenses/expenditures.

Statement No. 75 replaces the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended (Statement No. 45), and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*.

Simultaneously with the adoption of Statement No. 75, the Harbors Division adopted the provisions of GASB Statement No. 85, *Omnibus 2017* (Statement No. 85). The objective of this statement is to address practice issues that have been identified during the implementation and application of certain GASB statements.

The Harbors Division did not restate the financial statements as of and for the year ended June 30, 2017, because the actuarial information from the State did not provide the required information for the prior year. As such, the Harbors Division included the OPEB disclosures under Statement No. 45, for the year ended June 30, 2017. The Harbors Division reported the cumulative effect of the change in accounting principles by restating beginning net position in the accompanying 2018 financial statements. Specifically, the adoption of Statement Nos. 75 and 85 had the effect of decreasing net position as of June 30, 2017 by $16,824,711. In addition, the Harbors Division recorded a deferred outflow of resources of $2,507,481, a net other postemployment benefits liability of $38,004,809, and a deferred inflow of resources of $48,856 as of June 30, 2018 in the accompanying financial statements. Refer to Note 8 for additional information regarding the OPEB plan.

Recently Issued Accounting Pronouncements

GASB Statement No. 83

The GASB issued Statement No. 83, *Certain Asset Retirement Obligations*. This statement provides financial statement users with information about asset retirement obligations that were not addressed in GASB standards by establishing uniform accounting and financial reporting requirements for these obligations. The requirements of this statement are effective for reporting periods beginning after June 15, 2018. The Harbors Division is currently evaluating the impact that this statement will have on its financial statements.

GASB Statement No. 87

The GASB issued Statement No. 87, *Leases*. The objective of this statement is to improve accounting and financial reporting for leases by governments. This statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the provisions of the contract. The requirements of this statement are effective for reporting periods beginning after December 15, 2019. The Harbors Division is currently evaluating the impact that this statement will have on its financial statements.

GASB Statement No. 88

The GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*. The primary objective of this statement is to improve the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt. The requirements of this statement are effective for reporting periods beginning after June 15, 2018. The Harbors Division is currently evaluating the impact that this statement will have on its financial statements.

GASB Statement No. 89

The GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*. This statement replaces Paragraph 5-22 of Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. This statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. The requirements of this statement are effective for reporting periods beginning after December 15, 2019. The Harbors Division is currently evaluating the impact that this statement will have on its financial statements.

Reclassifications

Certain 2017 amounts have been reclassified to conform with the 2018 presentations. Such reclassifications had no effect on the previously reported changes in net position.

3. Cash and Cash Equivalents

Cash and cash equivalents at June 30, 2018 and 2017 consisted of the following:

	2018	2017
Amounts held in State Treasury	$ 403,922,261	$ 424,509,267
Petty cash and other	2,663,901	2,203,220
	$ 406,586,162	$ 426,712,487

Such amounts are reflected in the statements of net position at June 30, 2018 and 2017 as follows:

	2018	2017
Current assets:		
Unrestricted	$ 185,531,299	$ 208,340,548
Restricted:		
Revenue bond debt service payments	22,945,609	22,867,370
Revenue bond cash reserve requirements	11,455,033	11,455,033
Noncurrent assets:		
Restricted:		
Capital improvement projects:		
Construction - special purpose funds	170,390,363	109,676,283
Unspent bond proceeds	-	57,610,233
Other-bond reserve requirements		
and security deposits	16,263,858	16,763,020
	$ 406,586,162	$ 426,712,487

Amounts Held in State Treasury

The Director of Finance of the Department of Budget and Finance, State of Hawaii (B&F), is responsible for the safekeeping of all monies paid into the State Treasury. The Director of Finance pools and invests any monies of the State, which in the Director of Finance's judgment, are in excess of the amounts necessary for meeting the specific requirements of the State. Investment earnings are allocated to the pool participants based upon their equity interest in the pooled monies. Legally authorized investments include obligations of or guaranteed by the U.S. government, obligations of the State, federally-insured savings and checking accounts, time certificates of deposit, and repurchase agreements with federally-insured financial institutions.

At June 30, 2018 and 2017, amounts held in State Treasury by the Harbors Division totaled $403,922,261 and $424,509,267, respectively. The amounts held in State Treasury reported in the accompanying statements of net position reflects the Harbors Division's relative position in the State's investment pool based upon the average monthly investment balance of each participant in the investment pool.

Information relating to the cash and investments in State Treasury is determined on a statewide basis and not for individual departments or agencies. Information regarding the carrying amount and corresponding bank balances of the investment pool and collateralization of the investment pool balances is included in the comprehensive annual financial report (CAFR) of the State.

Cash and Cash Equivalents

The State maintains bank accounts for various purposes at locations throughout the State and the nation. Bank deposits for the State Treasury are under the custody of the Director of Finance. Cash and cash equivalents consist of cash, time certificates of deposit, and money market accounts. Cash and cash equivalents also include repurchase agreements and U.S. government securities with original maturities of three months or less.

Investments

The State holds investments both for its own benefit and as an agent for other parties. Further, the State pools all excess funds into an investment pool that is administered by B&F. The pool's investment options are limited to investments listed in the Hawaii Revised Statutes (HRS).

At the end of each year, B&F allocates the investment pool amount to each of the participants. The allocation is based on the average monthly investment balance of each participant in the investment pool.

The EUTF maintains a separate investment pool. The EUTF board is responsible for safekeeping these monies and has appointed an investment committee responsible for investing EUTF assets in compliance with HRS Sections 87A-24(2) and 88-119. Money is invested in accordance with the EUTF's investment policy.

The following table presents the fair value of the State's investments by level of input at June 30, 2017 (amounts expressed in thousands):

		Fair Value Measurements Using		
	Reported Value	**Quoted Prices in Active Markets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Primary government:				
Investments measured by fair value level:				
U.S. government securities	$ 2,307,970	$ 552,527	$ 1,755,443	$ -
Mutual funds	37,127	37,127	-	-
	2,345,097	$ 589,654	$ 1,755,443	$ -
Investments measured at amortized cost:				
Certificates of deposit	1,242,753			
Total investments	$ 3,587,850			
Fiduciary funds:				
Investments measured by fair value level:				
Equity securities	$ 413,652	$ 413,652	$ -	$ -
U.S. government securities	306,888	47,645	259,243	-
Mutual funds	132,899	132,899	-	-
Derivatives	(148)	-	(148)	-
	853,291	$ 594,196	$ 259,095	$ -
Investments measured by net asset value (NAV):				
Commingled funds:				
Domestic equity	358,322			
International equity	377,205			
Domestic core fixed income	224,097			
Domestic inflation-linked fixed income	52,061			
Alternative investments	74,919			
	1,939,895			
Investments measured at amortized cost:				
Certificates of deposit	107,164			
Total investments	$ 2,047,059			
Invested securities lending collateral at NAV				
Money market fund	$ 27,061			

Information relating to the fair value of investments in the State's investment pool at June 30, 2018 will be included in the State's CAFR when issued.

Cash and Cash Equivalents, Certificates of Deposit, and Repurchase Agreements

The State considers all cash and investments with original maturities of three months or less to be cash equivalents. The carrying amounts for cash equivalents, certificates of deposit, and repurchase agreements are measured at amortized cost.

Debt Securities, Equity Securities, Mutual Funds, Commingled Funds and Alternative Investments, and Money Market Funds

The following methods and assumptions were used by the State in estimating the fair value of its financial instruments:

Debt securities – Debt securities held by the State consist of U.S. government obligations including U.S. Treasury bills and U.S. Treasury notes and bonds. The fair value of these investments are based on quoted prices in active markets or other observable inputs, including pricing matrices. These investments are categorized in either Level 1 or 2 of the fair value hierarchy.

Equity securities – Equity securities held by the State are valued at the closing price reported on the active market on which the individual securities are traded. These investments are categorized in Level 1 of the fair value hierarchy.

Mutual funds – The mutual funds held by the State are open-ended mutual funds that are registered with the Securities Exchange Commission (SEC). The fair value of these mutual funds are valued at the daily closing price as reported by the fund. These funds are required to publish their daily NAV and to transact at that price. These investments are categorized in Level 1 of the fair value hierarchy.

Commingled funds and alternative investments – Investments in commingled funds and alternative investments are valued at the NAV of units of the investment vehicles. The NAV is based on the fair value of the underlying assets held by the fund less its liabilities. The State has no unfunded commitments with regard to these commingled funds and alternative investments.

Money market funds – Investments in money market funds are valued at the NAV of the custodian bank liquid asset portfolio. NAV is based on the fair value of the underlying assets held by the fund less its liabilities.

The preceding measurements described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. The market volatility of equity-based investments is expected to substantially impact the value of such investments at any given time. It is likely that the State's investments have fluctuated since June 30, 2017.

The following table presents the investments by maturity period at June 30, 2017 (amounts expressed in thousands):

	Reported Value	Maturity (in years) Less than 1	1-5	>5
Primary government:				
Certificates of deposit	$ 1,242,753	$ 1,187,710	$ 55,043	$ -
U.S. government securities	2,307,970	704,940	1,603,030	-
	3,550,723	$ 1,892,650	$ 1,658,073	$ -
Mutual funds	37,127			
Total investments	$ 3,587,850			
Fiduciary funds:				
Certificates of deposit	$ 107,164	$ 102,418	$ 4,746	$ -
U.S. government securities	306,888	60,788	246,100	-
Derivatives	(148)	-	(148)	-
	413,904	$ 163,206	$ 250,698	$ -
Equity securities	413,652			
Mutual funds	132,899			
Commingled funds	1,011,685			
Alternative investments	74,919			
Total investments	$ 2,047,059			

Information relating to the State's investment pool by maturity period at June 30, 2018 will be included in the State's CAFR when issued.

Interest Rate Risk

As a means of limiting its exposure to fair value losses arising from rising interest rates, the State's investment policy generally limits maturities on investments to not more than five years from the date of investment.

Credit Risk

The State's investment policy limits its investments in state and U.S. treasury securities, time certificates of deposit, U.S. government or agency obligations, repurchase agreements, commercial paper, banker's acceptances, and money market funds maintaining a Triple-A rating.

Custodial Risk

For an investment, custodial risk is the risk that, in the event of the failure of the counterparty, the State will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The State's investments are held at broker/dealer firms, which are protected by the Securities Investor Protection Corporation (SIPC) up to a maximum amount. Excess-SIPC coverage is provided by the firms' insurance policies. In addition, the State requires the institutions to set aside in safekeeping certain types of securities to collateralize repurchase agreements. The State monitors the market value of these securities and obtains additional collateral when appropriate.

Concentration of Credit Risk

The State's policy provides guidelines for portfolio diversification by placing limits on the amount the State may invest in any one issuer, types of investment instruments, and position limits per issue of an investment instrument.

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. The State's asset allocation and investment policy allows for active and passive investments in international securities. The foreign currency risk exposure to the State arises from the international equity investment holdings, including commingled funds, common stocks, and exchange traded funds.

4. Capital Assets

Capital asset activity for the years ended June 30, 2018 and 2017 were as follows:

	Balance July 1, 2017	Additions	Deductions	Balance June 30, 2018
Nondepreciable assets:				
Land and land improvements	$ 278,993,847	$ 32,820,000	$ -	$ 311,813,847
Depreciable assets:				
Land improvements	287,718,519	502,717	-	288,221,236
Wharves	278,758,332	49,935,018	-	328,693,350
Other improvements	91,114,188	24,979,748	-	116,093,936
Buildings	113,923,478	2,988,706	-	116,912,184
Equipment	25,831,050	1,207,095	(511,675)	26,526,470
Total at cost	1,076,339,414	112,433,284	(511,675)	1,188,261,023
Less accumulated depreciation for:				
Land improvements	108,728,541	9,392,559	-	118,121,100
Wharves	158,036,234	8,322,459	-	166,358,693
Other improvements	56,838,829	4,557,173	-	61,396,002
Buildings	46,328,976	2,753,731	-	49,082,707
Equipment	16,084,780	1,993,266	(504,061)	17,573,985
Total accumulated depreciation	386,017,360	27,019,188	(504,061)	412,532,487
Construction in progress	139,398,063	85,913,728	(79,672,891)	145,638,900
Total capital assets, net	$ 829,720,117	$ 171,327,824	$ (79,680,505)	$ 921,367,436

	Balance July 1, 2016	Additions	Deductions	Balance June 30, 2017
Nondepreciable assets:				
Land improvements	$ 278,993,847	$ -	$ -	$ 278,993,847
Depreciable assets:				
Land improvements	278,923,508	8,795,011	-	287,718,519
Wharves	269,153,315	9,605,017	-	278,758,332
Other improvements	91,114,188	-	-	91,114,188
Buildings	110,577,730	3,345,748	-	113,923,478
Equipment	20,865,200	4,965,850	-	25,831,050
Total at cost	1,049,627,788	26,711,626	-	1,076,339,414
Less accumulated depreciation for:				
Land improvements	99,455,043	9,273,498	-	108,728,541
Wharves	149,907,477	8,128,757	-	158,036,234
Other improvements	48,014,250	8,824,579	-	56,838,829
Buildings	43,452,552	2,876,424	-	46,328,976
Equipment	14,319,469	1,765,311	-	16,084,780
Total accumulated depreciation	355,148,791	30,868,569	-	386,017,360
Construction in progress	100,611,285	65,017,339	(26,230,561)	139,398,063
Total capital assets, net	$ 795,090,282	$ 60,860,396	$ (26,230,561)	$ 829,720,117

5. Long-Term Liabilities

The changes in long-term liabilities were as follows:

	Balance July 1, 2017	Additions	Deductions	Balance June 30, 2018	Current	Noncurrent
Accrued workers' compensation (Note 13)	$ 640,892	$ 370,891	$ 93,993	$ 917,790	$ 93,423	$ 824,367
Accrued vacation	2,582,833	1,167,246	1,088,427	2,661,652	751,790	1,909,862
Capital lease obligation (Note 9)	26,992,659	-	716,734	26,275,925	812,396	25,463,529
Net pension liability (Note 12)	35,453,242	1,044,610	2,084,894	34,412,958	-	34,412,958
Net other postretirement benefits liability (Note 12)	18,761,705	21,186,944	1,943,840	38,004,809	-	38,004,809
General obligation bonds (Note 8)	25,376,867	-	2,122,232	23,254,635	2,227,919	21,026,716
Revenue bonds (Note 6)	309,470,000	22,425,000	38,285,000	293,610,000	16,755,000	276,855,000
Unamortized premium(discount), net	277,445	-	290,607	(13,162)	24,424	(37,586)
Revenue bonds, net	309,747,445	22,425,000	38,575,607	293,596,838	16,779,424	276,817,414
	$ 419,555,643	$ 46,194,691	$ 46,625,727	$ 419,124,607	$ 20,664,952	$ 398,459,655

	Balance July 1, 2016	Additions	Deductions	Balance June 30, 2017	Current	Noncurrent
Accrued workers' compensation (Note 13)	$ 589,490	$ 799,901	$ 748,499	$ 640,892	$ 258,383	$ 382,509
Accrued vacation	2,487,677	1,056,582	961,426	2,582,833	724,575	1,858,258
Capital lease obligation (Note 9)	-	26,992,659	-	26,992,659	716,734	26,275,925
Net pension liability (Note 12)	23,096,737	14,402,263	2,045,758	35,453,242	-	35,453,242
Other postretirement benefits payable (Note 12)	17,317,087	3,388,458	1,943,840	18,761,705	-	18,761,705
General obligation bonds (Note 8)	27,399,721	-	2,022,854	25,376,867	2,122,232	23,254,635
Revenue bonds (Note 6)	323,370,000	91,235,000	105,135,000	309,470,000	15,970,000	293,500,000
Unamortized premium, net	392,844	-	115,399	277,445	64,641	212,804
Revenue bonds, net	323,762,844	91,235,000	105,250,399	309,747,445	16,034,641	293,712,804
	$ 394,653,556	$ 137,874,863	$ 112,972,776	$ 419,555,643	$ 19,856,565	$ 399,699,078

6. Revenue Bonds Payable

Pursuant to authorization from the State Legislature, the Director of DOT issued the 1997 Certificate, which provides for the issuance of bonds at any time and from time-to-time upon compliance with certain conditions of the 1997 Certificate.

The Harbor Revenue Bonds (Revenue Bonds) are collateralized by a charge and lien on the revenues of the Public Undertaking as defined in the 1997 Certificate.

The Revenue Bonds are subject to redemption at the option of the Director of DOT and the State during specific years at prices ranging from 102% to 100% of face value.

On July 5, 2017, the Harbors Division issued $22,425,000 in Series 2016 D Revenue Refunding Bonds, which bear interest at 3.09% with a maturity date of July 1, 2027. Proceeds were used to refund $22,315,000 of 2007 A Bonds. The refunding of 2007 A Bonds provided net present savings of approximately $2,959,000.

On December 6, 2016, the Harbors Division issued $14,565,000 in Series 2016 A, $68,535,000 in Series 2016 B, and $8,135,000 in Series 2016 C Refunding Bonds, which bear interest from 1.99% to 2.89% with maturity dates through January 2031. The Series A 2016 Revenue Bonds refunded $16,195,000 of 2004 B Bonds, the Series B 2016 Revenue Bonds refunded $71,625,000 of 2006 A Bonds, and the Series C 2016 Revenue Bonds refunded $7,365,000 of 2007 A Bonds. The refunding of 2004 B, 2006 A, and 2007 A Bonds provided net present value savings of approximately $12,932,000.

The following is a summary of the Revenue Bonds issued and outstanding at June 30, 2018:

Year of Issue	Final Redemption Date	Interest Rate	Original Amount of Issue	Current: Principal Due July 1, 2018	Current: Principal Due January 1, 2019	Total Current	Noncurrent
2010	July 1, 2040	3.00-5.75%	$ 201,390,000	$ 5,495,000	$ -	$ 5,495,000	$ 160,275,000
2013	July 1, 2029	3.25%	23,615,000	3,105,000	-	3,105,000	16,615,000
2016	January 1, 2031	1.99-3.09%	113,660,000	1,015,000	7,140,000	8,155,000	99,965,000
			$ 338,665,000	$ 9,615,000	$ 7,140,000	16,755,000	276,855,000
					Unamortized premium (discount), net	24,424	(37,586)
						$ 16,779,424	$ 276,817,414

The following is a summary of the Revenue Bonds issued and outstanding at June 30, 2017:

Year of Issue	Final Redemption Date	Interest Rate	Original Amount of Issue	Current: Principal Due July 1, 2017	Current: Principal Due January 1, 2018	Total Current	Noncurrent
2007	July 1, 2027	5.25%	$ 51,645,000	$ 2,215,000	$ -	$ 2,215,000	$ 22,315,000
2010	July 1, 2040	3.00-5.75%	201,390,000	7,165,000	-	7,165,000	165,770,000
2013	July 1, 2029	3.25%	23,615,000	1,050,000	-	1,050,000	19,720,000
2016	January 1, 2031	1.99-2.89%	91,235,000	-	5,540,000	5,540,000	85,695,000
			$ 367,885,000	$ 10,430,000	$ 5,540,000	15,970,000	293,500,000
					Unamortized premium, net	64,641	212,804
						$ 16,034,641	$ 293,712,804

Debt service requirements to maturity for the Revenue Bonds are as follows:

Fiscal Year Ending June 30	Principal	Interest	Total
2019	$ 16,755,000	$ 12,181,451	$ 28,936,451
2020	17,365,000	11,574,998	28,939,998
2021	17,290,000	10,956,248	28,246,248
2022	17,950,000	10,305,832	28,255,832
2023	18,595,000	9,648,188	28,243,188
2024-2028	77,660,000	40,226,754	117,886,754
2029-2033	54,180,000	26,550,606	80,730,606
2034-2038	42,185,000	15,088,291	57,273,291
2039-2041	31,630,000	2,735,438	34,365,438
	$ 293,610,000	$ 139,267,806	$ 432,877,806

The debt service requirements reflect the sum of the amounts to be paid in accordance with the repayment schedules of the bonds issued. Principal and interest payments are required to be funded in the 12-month and 6-month periods, respectively, preceding the date on which the payments are due. Accordingly, the debt service requirements include reserves of $22,945,609 as of June 30, 2018, for principal payments of $9,615,000 and $7,140,000 due on July 1, 2018 and January 1, 2019, respectively, and for interest payments $6,190,609 due on July 1, 2018.

7. Harbor Revenue Bond Requirements

1997 Certificate – Minimum Net Revenue Requirement

Pursuant to Section 6.03 of the 1997 Certificate, the Harbors Division covenants and agrees that so long as any of the Revenue Bonds remain outstanding, it will enforce and collect fees, rates, rents, and charges for the Public Undertaking that will yield net revenue, as defined by the 1997 Certificate, for the immediately ensuing 12 months, in an amount at least sufficient to:

(1) Together with funds legally available, therefore including any amounts on deposit in the harbor reserve and contingency account; an aggregate sum equal to at least 1.25 times the total amount of: (i) the interest payments for such 12 months on all the Revenue Bonds outstanding under the 1997 Certificate, (ii) the principal amount of the Revenue Bonds maturing by their terms during such 12 months and (iii) the minimum sinking fund payments for all Revenue Bonds required to be made during such 12 months; and

(2) Without consideration of other funds, shall be at least equal to 1.00 times the bond service for such 12 months.

The Harbor Revenue Bond debt service requirements, including minimum sinking fund payments during the current fiscal year, computed in accordance with Section 6.03 of the 1997 Certificate totaled $29,113,861. Net revenues of the Public Undertaking, as defined by the 1997 Certificate amounted to $127,964,356 or 4.40 times the minimum net revenue requirement for the fiscal year ended June 30, 2018, and $98,267,034 or 3.15 times the minimum net revenue requirement for the fiscal year ended June 30, 2017.

Harbor Special Fund

All revenues are deposited into this fund and applied in the order of priority set forth under the 1997 Certificate. Section 5.01 of the 1997 Certificate requires that the following accounts be established:

(1) Harbor Interest Account

Equal monthly installments sufficient to pay for the interest next becoming due on the Revenue Bonds are required to be paid into this account. This requirement was met as of June 30, 2018 and 2017.

(2) Harbor Principal Account

Commencing with the first business day of each fiscal year, equal monthly payments are required to be made to this account sufficient to redeem the Revenue Bonds scheduled for redemption on the following July 1 and January 1. This requirement was met as of June 30, 2018 and 2017.

(*3) Harbor Debt Service Reserve Account*

In order to provide a reserve for the payment of the principal and interest on the Revenue Bonds, the Harbors Division is required to deposit in the harbor revenue special fund an amount equal to the lesser of: (a) the average annual bond service on such series and (b) the amount permitted by the Internal Revenue Code of 1986 in order that the interest on such series is excluded from gross income for federal income tax purposes.

Furthermore, the Harbors Division is required to satisfy the reserve requirement of maximum aggregate bond service by no later than the first date on which a principal installment is payable on July 1 or January 1 of each fiscal year.

In lieu of the credit of monies to the harbor debt service reserve account, the Harbors Division may cause to be so credited a surety bond or an insurance policy payable to the Harbors Division for the benefit of the holders of the Revenue Bonds of a series or a letter of credit in an amount equal to the difference between the reserve requirement and the amounts then on credit to the harbor debt service reserve account. In the event a surety bond, insurance policy, or letter of credit is secured to satisfy that portion of the reserve requirement allocable to a series of Revenue Bonds, so long as such surety bond, insurance policy, or letter of credit is in effect, the owners of such series of Revenue Bonds shall not be entitled to payment from or a lien on the funds on deposit in the harbor revenue special fund credited to the harbor debt service reserve account to satisfy that portion of the reserve requirement allocable to other series of Revenue Bonds, nor shall the owners of Revenue Bonds of such other series be entitled to any payment from such surety bond, insurance policy, or letter of credit. The surety bond, insurance policy, or letter of credit shall be payable (upon the giving of notice as required thereunder) on any date on which monies will be required to be applied from the harbor debt service reserve account to the payment of the principal or interest on any Revenue Bonds of such series and such withdrawals may not be made from amounts credited to the harbor debt service reserve account for such series of Revenue Bonds.

Prior to the use of a surety bond, insurance policy, or letter of credit pursuant to the provisions of this paragraph (other than any such use at the time of issuance of the 1997 Series Revenue Bonds), DOT shall receive written confirmation from the rating agency that the rating on the Revenue Bonds outstanding as then in effect shall not be reduced as a result of such use. If a disbursement is made pursuant to a surety bond, an insurance policy, or a letter of credit provided pursuant to this paragraph, the Harbors Division shall be obligated either: (a) to reinstate the maximum limits of such surety bond, insurance policy, or letter of credit or (b) to credit the harbor debt service reserve account, funds in the amount of the disbursement made under such surety bond, insurance policy, or letter of credit, or a combination of such alternatives, as shall provide that the amount credited to the harbor debt service reserve account allocable to a series of Revenue Bonds equals that portion of the reserve requirement allocable to such series; provided, however, a failure to immediately restore such reserve requirement shall not constitute an event of default if the reserve requirement is restored within the time period permitted by Section 11.01(c) (90 days following the required notice). Notwithstanding the provisions of Section 11.01(c), the Harbors Division shall not permit any surety bond, insurance policy, or letter of credit which has been established in lieu of a deposit into the harbor revenue special fund for credit to the harbor debt service reserve account to terminate or expire prior to depositing to such fund for credit to such account the amount satisfied previously by the surety bond, insurance policy, or letter of credit.

(4) Harbor Reserve and Contingency Account

Monies on credit to the harbor reserve and contingency account may be used to make up any deficiency with respect to any series of Revenue Bonds in the harbor interest account, the harbor principal account and the harbor debt service reserve account. To the extent not used to make up any such deficiencies, monies on credit to the harbor reserve and contingency account may be used for any other purpose within the jurisdiction, powers, duties, and functions of the Harbors Division.

8. General Obligation Bonds

In fiscal 2006, the State issued $350,000,000 of General Obligation bonds, Series DI, dated March 23, 2006; in fiscal 2007, the State issued $350,000,000 of General Obligation bonds, Series DJ, dated March 28, 2007; and in fiscal 2008, the State issued $375,000,000 of General Obligation bonds, Series DK, dated May 1, 2008. Interest rates on outstanding Series DI, Series DJ, and Series DK General Obligation bonds range from 4.00% to 5.00%.

Reimbursable general obligation bonds are general obligations of the State, but since the proceeds were used to finance the harbor and waterfront improvements, the Harbors Division is required to reimburse the State's general fund for the payment of principal and interest on such bonds. As of June 30, 2018 and 2017, outstanding reimbursable general obligation bonds amounted to approximately $23,255,000 and $25,377,000, respectively.

Debt service requirements to maturity for the General Obligation bonds are as follows:

Fiscal Year Ending June 30	Principal	Interest	Total
2019	$ 2,227,919	$ 1,152,889	$ 3,380,808
2020	2,336,771	1,044,012	3,380,783
2021	2,450,903	929,861	3,380,764
2022	2,572,554	808,084	3,380,638
2023	2,700,654	680,025	3,380,679
2024-2028	10,965,834	1,349,968	12,315,802
	$ 23,254,635	$ 5,964,839	$ 29,219,474

9. Capital Lease Obligation

The Harbors Division entered into an equipment lease purchase agreement to fund the installation and acquisition of energy conservation measures at selected Harbors Division locations. Proceeds of $26,245,564 were deposited into an acquisition fund held in trust by an acquisition fund custodian to provide for future payments as requested by the Harbors Division. The agreement also provided for the financing of interest expense through October 1, 2016 amounting to $747,095, which applied toward the principal of the capital lease obligation. The capital lease obligation amounted to $26,275,925 and $26,992,659 at June 30, 2018 and 2017, respectively. Annual lease payments will commence on October 1, 2017 and continue through October 1, 2032 at an interest rate of 2.74%. Costs incurred for the installation and acquisition of energy conservation measures through June 30, 2018, which amounted to $26,954,693 including additional capitalized interest of $1,279,569 for the period October 2, 2016 through June 30, 2018, are included in construction in progress. Unused proceeds in the acquisition fund at June 30, 2018 and 2017, amounted to $1,317,535 and $8,465,522, respectively, and are reported as other current assets in the accompanying statements of financial position.

Future minimum lease commitments are as follows:

Fiscal Year Ending June 30	Principal	Interest	Total
2019	$ 812,396	$ 719,960	$ 1,532,356
2020	914,562	697,700	1,612,262
2021	1,023,606	672,642	1,696,248
2022	1,139,923	644,595	1,784,518
2023	1,263,929	613,361	1,877,290
2024-2028	8,480,915	2,471,309	10,952,224
2029-2033	12,640,594	1,076,010	13,716,604
	$ 26,275,925	$ 6,895,577	$ 33,171,502

10. Interest Cost

Total combined interest cost incurred related to Revenue and General Obligation Bonds for the fiscal years ended June 30, 2018 and 2017 amounted to approximately $13,666,000 and $16,267,000, respectively. Of this amount, approximately $2,556,000 and $2,618,000 were capitalized during fiscal years ended June 30, 2018 and 2017, respectively, as part of the construction cost of harbor facilities.

An additional $725,000 and $1,302,000 of interest cost incurred related to the capital lease obligation (see Note 9) was capitalized for the fiscal year ended June 30, 2018 and 2017, respectively.

11. Leasing Operations

The Harbors Division's leasing operations consist principally of the leasing of land, wharf, and building space under revocable permits and long-term leases. The revocable permits provide for tenancy on a month-to-month basis and are renewable annually at the option of the State. The long-term leases, which are classified as operating leases, expire in various years through September 2058. These leases generally call for rental increases every five to ten years based on a step-up or independent appraisals of the fair rental value of the leased property.

The following is a schedule of approximate future minimum lease rentals on noncancelable operating leases as of June 30, 2018:

Fiscal Year Ending June 30	Amount
2019	$ 5,175,000
2020	5,152,000
2021	5,206,000
2022	5,270,000
2023	5,186,000
2024-2028	24,812,000
2029-2033	22,261,000
2034-2038	14,774,000
2039-2043	10,706,000
2044-2048	5,888,000
2049-2053	2,617,000
2054-2058	2,388,000
2059	87,000
	$ 109,522,000

The above schedule does not include estimated future rental revenue for certain leases beyond their first 15 years. An estimate could not be made due to rental reopenings after the 15th year in which rental rates will be based upon the prevailing fair value.

12. Retirement Benefits

Pension Plan

Plan Description

Generally, all full-time employees of the State and counties, which includes the Harbors Division, 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.

Benefits Provided

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

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

The following summarizes the provisions relevant to the largest employee groups of the respective membership class. 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 the time of death with at least ten years of credited service. The surviving spouse/reciprocal beneficiary (until remarriage/reentry into a new reciprocal beneficiary relationship) and dependent children (up to age 18) receive a benefit equal to a percentage of member's accrued maximum allowance unreduced for age or, if the member was eligible for retirement at the time of death, the surviving spouse/reciprocal beneficiary receives 100% joint and survivor lifetime pension and the dependent children receive a percentage of the member's accrued maximum allowance unreduced for age.

Contributory Class for Members Hired Prior to July 1, 2012

Retirement Benefits

General employees' retirement benefits are determined as 2% of average final compensation multiplied by the years of credited service. General employees with five years of credited service are eligible to retire at age 55.

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 firefighters 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.

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 Class for Members Hired After June 30, 2012

Retirement Benefits

General employees' retirement benefits are determined as 1.75% of average final compensation multiplied by the years of credited service. General employees with ten years of credited service are eligible to retire at age 60.

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 25 years of credited service are eligible to retire at age 55, 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 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.

Hybrid Class for Members Hired Prior to July 1, 2012

Retirement Benefits

General employees' retirement benefits are determined as 2% of average final compensation multiplied by the years of credited service. General employees with five years of credited service are eligible to retire at age 62. General employees with 30 years of credited service are eligible to retire at age 55.

Disability Benefits

Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 35% of their average final compensation plus refund of their contributions and accrued interest. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined in the same manner as retirement benefits but are payable immediately, without an actuarial reduction, and at a minimum of 25% of average final compensation.

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.

Hybrid Class for Members Hired After June 30, 2012

Retirement Benefits

General employees' retirement benefits are determined as 1.75% of average final compensation multiplied by the years of credited service. General employees with ten years of credited service are eligible to retire at age 65. Employees with 30 years of credited service are eligible to retire at age 60. 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.

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 years 2018 and 2017 were 28.0% and 25.0%, respectively, for police officers and firefighters, and 18.0% and 17.0%, respectively, for all other employees. Contributions to the ERS from the Harbors Division were $2,227,017 and $2,084,894 for the fiscal years ended June 30, 2018 and 2017, respectively.

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 beginning July 1, 2017. The rate for police and firefighters increases to 31.0% on July 1, 2018; 36.0% on July 1, 2019; and 41.0% on July 1, 2020, and the rate for all other employees increases to 19.0% on July 1, 2018; 22.0% on July 1, 2019; and 24.0% 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.

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

Measurement of the actuarial valuation of the pension liability, pension expense, and deferred outflows of resources and deferred inflows of resources related to pension is made for the State as a whole and is not separately computed for the individual state departments and agencies such as the Harbors Division. The State allocates the pension liability, pension expense, and deferred outflows of resources and deferred inflows of resources related to pension to the various departments and agencies based upon a systematic methodology. Additional disclosures and required supplementary information stipulated by Statement Nos. 68 and 71 pertaining to the State's net pension liability, pension expense, and deferred outflows of resources and deferred inflows of resources related to pension can be found in the State's CAFR.

At June 30, 2018 and 2017, the Harbors Division reported a net pension liability of $34,412,958 and $35,453,242, respectively, for its proportionate share of the State's net pension liability. The net pension liability was measured as of June 30, 2017 and 2016, and the total pension liability used to calculate the net pension liability was determined by actuarial valuations as of those dates.

At June 30, 2018 and 2017, the Harbors Division's share of the State's net pension liability was 0.54% and 0.51%, respectively.

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

For the years ended June 30, 2018 and 2017, the Harbors Division recognized pension expense of \$4,921,738 and \$4,327,549, respectively. At June 30, 2018 and 2017, the Harbors Division reported deferred outflows of resources and deferred inflows of resources related to pension from the following sources:

	Deferred Outflows of Resources	
	2018	**2017**
Contributions subsequent to the measurement date	$ 2,227,017	$ 2,084,894
Changes in assumptions	5,310,788	6,823,098
Net difference between projected and actual earnings on pension plan investments	-	2,298,626
Differences between expected and actual experience	568,232	725,969
Changes in proportion and differences between contributions and proportionate share of contributions	152,938	120,626
	$ 8,258,975	$ 12,053,213

	Deferred Inflows of Resources	
	2018	**2017**
Differences between expected and actual experience	$ 354,197	$ 508,894
Changes in proportion and differences between contributions and proportionate share of contributions	78,384	112,779
Net difference between projected and actual earnings on pension plan investments	129,860	-
	$ 562,441	$ 621,673

The $2,227,017 reported as deferred outflows of resources related to pension at June 30, 2018 resulting from the Harbors Division's contributions subsequent to the measurement date will be recognized as a reduction of net pension liability in the year ended June 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pension at June 30, 2018 will be recognized in pension expense as follows:

Year Ended June 30:	
2019	$ 1,262,497
2020	1,879,097
2021	1,580,197
2022	735,922
2023	11,804
	$ 5,469,517

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 ERS 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% compounded annually including inflation

There were no changes to ad hoc postemployment benefits including cost of living adjustments.

Post-retirement mortality rates are based on the 2017 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 the RP-2014 mortality table based on the occupation of the member.

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 Real Rate of Return
Broad growth	63.00%	5.80%
Principal protection	7.00%	0.20%
Real return	10.00%	3.60%
Crisis risk offset	20.00%	3.10%
	100.00%	

Discount Rate

The discount rate used to measure the net pension liability was 7.00%, consistent with the 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, which includes the Harbors Division, 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.

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

The following presents the Harbors Division's proportionate share of the State's net pension liability calculated using the discount rate of 7.00%, as well as what the Harbors Division's proportionate share of the State's net pension 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%)**
Harbor Division's proportionate share of the State's net pension liability	$ 44,609,739	$ 34,412,958	$ 26,005,191

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 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.

Postemployment Health Care and Life Insurance Benefits

Plan Description

The State provides certain health care and life insurance benefits to all qualified employees. Pursuant to Act 88, SLH 2001, the State contributes to the EUTF, an agent multiple-employer defined benefit plan that replaced the Hawaii Public Employees Health Fund effective July 1, 2003. The EUTF was established to provide single delivery system of health benefits for state and county workers, retirees, and their dependents.

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

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

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

Members Covered by Benefit Terms

At July 1, 2017, the State's plan members covered by benefit terms consisted of the following:

Inactive plan members or beneficiaries currently receiving benefits	35,374
Inactive plan members entitled to but not yet receiving benefits	8,124
Active plan members	50,101
Total plan members	93,599

Contributions

Contributions are governed by HRS Chapter 87A and may be amended through legislation. Contributions to the EUTF from the Harbors Division were $2,507,481 and $1,943,840 for the years ended June 30, 2018 and 2017, respectively. The Harbors Division is required to make all contributions for members.

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

Measurement of the actuarial valuation of the OPEB liability, OPEB expense, and deferred outflows of resources and deferred inflows of resources related to OPEB is made for the State as a whole and is not separately computed for the individual state departments and agencies such as the Harbors Division. The State allocates the OPEB liability, OPEB expense, and deferred outflows of resources and deferred inflows of resources related to OPEB to the various departments and agencies based upon a systematic methodology. Additional disclosures and required supplementary information stipulated by Statement No. 75 pertaining to the State's net OPEB liability, OPEB expense, and deferred outflows of resources and deferred inflows of resources related to OPEB can be found in the State's CAFR.

At June 30, 2018, the Harbors Division reported a net OPEB liability of $38,004,809. The net OPEB liability was measured as of July 1, 2017, and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of that date.

At June 30, 2018, the Harbors Division's proportionate share of the State's net OPEB liability was 0.55%.

There were no changes between the measurement date, July 1, 2017, and the reporting date, June 30, 2018, that are expected to have a significant effect on the Harbors Division's proportionate share of the State's net OPEB liability.

For the year ended June 30, 2018, the Harbors Division recognized OPEB expense of $2,467,248. At June 30, 2018, the Harbors Division 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
Contributions subsequent to the measurement date	$ 2,507,481	$ -
Net difference between projected and actual earnings on OPEB plan investments	-	(48,856)
	$ 2,507,481	$ (48,856)

The $2,507,481 reported as deferred outflows of resources related to OPEB resulting from Harbors Division's contribution subsequent to the measurement date will be recognized as a reduction of the net OPEB liability in the year ending 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:

Year Ended June 30:	
2019	$ 12,214
2020	12,214
2021	12,214
2022	12,214
	$ 48,856

Actuarial Assumptions

The total OPEB liability in the July 1, 2017 actuarial valuation was determined using the following actuarial assumptions adopted by the Board of Trustees of the EUTF, on January 8, 2018, based on the experience study covering the five year period ended June 30, 2015:

Inflation	2.50%
Salary increases	3.50% to 7.00%, including inflation
Investment rate of return	7.00%
Healthcare cost 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 & Base Monthly Contribution (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.

Mortality rates are based on system-specific mortality tables utilizing scale BB to project generational morality improvement.

The long-term expected rate of return on OPEB plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of OPEB 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 asset class are summarized in the following table:

Asset Class	Target Allocation	Long-term Expected Real 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%
	100.00%	

Single Discount Rate

The discount rate used to measure the net OPEB lability was 7.00%, based on the expected rate of return on OPEB plan investments of 7.00% and the municipal bond rate of 3.56% (based on the daily rate closet to but not later than the measurement date of the Fidelity “20-year Municipal GO AA index”). Beginning with the fiscal year 2019 contribution, the State’s funding policy is to pay the recommended actuarially determined contribution, which is based on layered, closed amortization periods. Based on those assumptions, the OPEB plan’s fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive plan members. Therefore, the long-term expected rate of return on OPEB plan investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

OPEB Plan Fiduciary Net Position

The OPEB plan's fiduciary net position has been 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, regardless of the timing of the cash flows. 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 on a trade-date basis. Administrative expenses are financed exclusively with investment income.

There were no significant changes after the report measurement date. Detailed information about the OPEB 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.

Changes in the Harbors Division's Proportionate Share of the State's Net OPEB Liability

The following table represents a schedule of changes in the Harbors Division's proportionate share of the State's 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	$ 39,500,833	$ 1,970,577	$ 37,530,256
Service cost	651,105	-	651,105
Interest on the total OPEB liability	1,977,037	-	1,977,037
Employer contributions	-	1,943,840	(1,943,840)
Net investment income	-	194,620	(194,620)
Benefit payments	(977,481)	(977,481)	-
Administrative expense	-	(498)	498
Other	-	15,627	(15,627)
Net changes	1,650,661	1,176,108	474,553
Ending balance	$ 41,151,494	$ 3,146,685	$ 38,004,809

Sensitivity of the Harbors Division's Proportionate Share of the State's Net OPEB Liability to Changes in the Discount Rate and Healthcare Cost Trend Rates

The following table represents the Harbors Division's proportionate share of the State's net OPEB liability calculated using the discount rate of 7.00%, as well as what the Harbors Division's 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 discount rate:

	1% Decrease (6.00%)	**Discount Rate (7.00%)**	**1% Increase (8.00%)**
Harbor Division's proportionate share of the State's net OPEB liability	$ 44,605,581	$ 38,004,809	$ 32,663,413

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

	1% Decrease	**Healthcare Cost Trend Rate**	**1% Increase**
Harbor Division's proportionate share of the State's net OPEB liability	$ 32,355,860	$ 38,004,809	$ 45,134,418

OPEB Actuarial Valuations and Contributions Under GASB Statement No. 45

For periods prior to June 30, 2017, measurement of the actuarial valuation and the annual required contribution (ARC) was made in accordance with Statement No. 45. The actuarial valuation was performed as of July 1, 2015. The ARC represented a level of funding that, if paid on an ongoing basis, was projected to cover normal cost each year and to amortize any unfunded actuarial liabilities over a period not to exceed 30 years. The State allocated the ARC to the various departments and agencies, including the Harbors Division, based upon a systematic methodology.

The Harbors Division's contributions for the years ended June 30, 2017, 2016, and 2015 were approximately $1,944,000, $1,402,000, and $1,162,000, respectively, which represents 57.4%, 40.9%, and 35.4%, respectively of the Harbors Division's share of the ARC.

The following is a summary of the change in the other postemployment benefits liability during the year ended June 30, 2017:

Annual required contribution	$ 3,389,000
Contribution made	(1,944,000)
Increase in net OPEB obligation	1,445,000
Net OPEB obligation, beginning of the year	17,317,000
Net OPEB obligation, end of the year	$ 18,762,000
Actual contributions made as a percentage of ARC	57.4%

Refer to State's fiscal year 2017 CAFR for the methods and assumptions used by the State, required footnote disclosures, and required supplementary information in accordance with the provisions of Statement No. 45.

Deferred Compensation

The State offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, which is available to all State employees (excluding part-time, temporary, and casual/seasonal), permits employees to defer a portion of their compensation until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

All plan assets are held in a trust fund to protect them from claims of general creditors. The State has no responsibility for loss due to the investment or failure of investment of funds and assets in the plan, but does have the duty of due care that would be required of an ordinary prudent investor. Accordingly, the assets and liabilities of the State's deferred compensation plan are not reported in the State's nor the Harbor Division's financial statements.

13. Risk Management

The Harbors Division is exposed to various risks of loss related to, among other risks, torts; theft of, damage to, or destruction of assets; errors and omissions; and workers' compensation. The Harbors Division records a liability for insurance related losses if it is determined that a loss has been incurred and the amount can be reasonably estimated.

The State purchases policies to provide coverage for all state entities, including the Harbors Division. The State generally retains the first $1,000,000 per occurrence of property losses, the first $4,000,000 with respect to general liability claims, and the first $500,000 of losses due to crime and cyber liability. Losses in excess of those retention amounts are insured with commercial insurance carriers. The limit per occurrence for property losses is $200,000,000, except for terrorism, which is $50,000,000 per occurrence. The annual aggregate limit for general liability losses is $9,000,000 per occurrence, $50,000,000 for cyber liability losses and for crime losses, the limit per occurrence is $10,000,000 with no aggregate limit.

The Harbors Division obtained coverage for certain strategic piers and wharves infrastructure to mitigate its exposure to natural disasters from hurricane, earthquake, and flood (including a tsunami) events. The amount of insurance provided by this difference in conditions policy is $30,000,000 on an annual aggregate basis on a shared perils basis, subject to a $5,000,000 deductible per occurrence.

The State generally self-insures for its automobile no-fault and workers’ compensation losses. A liability for workers’ compensation and general liability claims is established if information indicates that a loss has been incurred as of June 30, 2018, and the amount of the loss can be reasonably estimated. The liability also includes an estimate for amounts incurred but not reported. Accrued workers’ compensation amounted to approximately $918,000 and $641,000 at June 30, 2018 and 2017, respectively.

14. Ceded Lands

In 2006, the Legislature enacted Act 178, SLH 2006 (Act 178), to re-establish a mechanism for OHA to receive a portion of the income and proceeds from the Ceded Lands, for native Hawaiians, under Article XII, Sections 4 and 6 of the Hawaii Constitution. Among other things, Act 178 directs state agencies that collect receipts from the Ceded Lands to annually transfer a total of $15,100,000 in four equal quarterly installments to OHA, and directs the Governor to issue an executive order to establish procedures for this purpose. The Governor issued Executive Order No. 06-06 on September 20, 2006.

Until the Legislature alters the amount or establishes a different means for implementing Article XII, Sections 4 and 6 of the Hawaii Constitution, Act 178 serves as the means for satisfying the State’s obligation to provide OHA with a portion of the income and proceeds from the Ceded Lands, for native Hawaiians.

The Harbors Division transferred $10,000,000 and $13,539,173 to OHA for these expenses required by Hawaii statutes during the fiscal years ended June 30, 2018 and 2017, respectively. The transfers, together with an accrual of $5,100,000 at June 30, 2018, are included in harbor operations costs in the accompanying statements of revenues, expenses and changes in net position for the fiscal years ended June 30, 2018 and 2017.

In fiscal year 2016, B&F transferred approximately $5,254,000 to the Harbors Division to return additional funds B&F collected for this purpose. On November 15, 2018, acting upon the advice of the State Attorney General, B&F notified the Harbors Division that this transfer of approximately $5,254,000 was not authorized and must be returned to B&F. On December 4, 2018, the Harbors Division processed the return of these funds to B&F.

15. Transactions with Other Government Agencies

The State assesses a surcharge of 5% for central service expenses on all receipts of the Harbors Division, after deducting any amounts pledged, charged, or encumbered for the payment of bonds and interest during the fiscal year. The assessments amounted to approximately $6,068,000 and $4,901,000 for the fiscal years ended June 30, 2018 and 2017, respectively.

The Harbors Division is assessed a percentage of DOT's general administration expenses. The assessments amounted to approximately $1,335,000 and $2,558,000 for the fiscal years ended June 30, 2018 and 2017, respectively.

The Hawaii Harbors Task Force was formed in April 2005 by the Governor's office to respond on a priority basis to the pressing demands for infrastructure improvements in Honolulu Harbor. The Aloha Tower Development Corporation (ATDC) was tasked to work in partnership with the Harbors Division with the executive officer of the ATDC serving as the chief executive of the Hawaii Harbors Project Office. The ATDC was assigned to plan and execute major long-term redevelopment projects such as the former Kapalama Military Reservation and various projects at Honolulu Harbor. ATDC was an agency attached to the Department of Business, Economic Development & Tourism (DBEDT).

Act 200, SLH 2008, was enacted to authorize a statewide Harbors Modernization Plan (HMP) to address harbor infrastructure improvements to Kahului Harbor on Maui, Nawiliwili Harbor on Kauai, Hilo and Kawaihae Harbors on Hawaii, and Honolulu and Kalaeloa Harbors on Oahu. In addition to the six commercial harbors included in the plan, the law placed Hana Harbor on Maui under the jurisdiction of the Harbors System and included appropriations for its upgrade. The Act authorizes the DOT to issue harbor revenue bonds to finance the improvements. The cost of the Harbors Modernization Plan, originally estimated at $842 million, was revised to $618 million in 2008. Act 200 also designated the ATDC as the entity responsible for the management and implementation of the HMP under the direction of the DOT.

The State Legislature in its 2009 legislative session questioned ATDC's role and effectiveness and provided operational funding for only FY2010 of the FY2009-2011 biennium. In its 2010 legislative session, the Legislature did not restore operating funds to ATDC for FY2011, effectively terminating its operations on June 30, 2010. Contracts executed by ATDC for HMP projects were assigned to the Harbors Division, which assumed management and implementation responsibilities for the HMP. The modernization projects have been integrated into the administration's Harbors Modernization Program, a capital improvements program comprised of priority public works projects critical to create jobs and jumpstart the economy.

In the 2011 legislative session, Act 152, SLH 2011 was enacted to remove ATDC from DBEDT and place the agency under the Department of Transportation for administrative purposes, redefine the boundaries of the Aloha Tower complex and repealed references to the HMP, effective July 1, 2011. Act 152 provides that ATDC is headed by a three-member board comprised of the Directors of Transportation and DBEDT and the Deputy Director of Harbors. The Director of DBEDT chairs the board and the Deputy Director of Harbors serves as the acting Chief Executive Officer for the ATDC. Act 152 also provided that the unencumbered and unexpended fund balance in the Aloha Tower Fund shall lapse to the credit of the Harbor Special Fund to be used for operating expenses for the ATDC. DBEDT transferred the balance of approximately $2.8 million to the Harbor Special Fund pursuant to Act 152. The $2.8 million offset a portion of the $7.8 million balance owed by ATDC to the Harbors Division for losses in revenue, obligations which were operating expenses for ATDC.

16. Aloha Tower Complex Development

The ATDC is a state agency established under HRS Chapter 206J, primarily to redevelop the Aloha Tower complex. The complex originally encompassed Piers 5 to 23 of Honolulu Harbor, but its boundaries were redefined by Act 152, SLH 2011. In September 1993, the Harbors Division entered into a lease with ATDC for certain portions of the Aloha Tower complex. ATDC is required annually to reimburse the Harbors Division for any losses in revenues during the term of the lease caused by any action of ATDC or the developer and to provide replacement facilities for maritime activities at no cost to the Harbors Division.

In September 1993, the ATDC subleased lands surrounded by Piers 8 and 9 and a portion of land surrounded by Pier 10 to a developer. The sublease required the developer to construct, at the developer's cost, various facilities including a Marketplace. The developer and the Harbors Division entered into a capital improvements, maintenance, operations, and securities agreement (Operations Agreement). The Operations Agreement allows the Harbors Division to operate the harbor facilities.

The developer later went into bankruptcy. The subsequent operator of the Marketplace assumed the obligations of the sublease and the Operations Agreement in March 1998. This replacement operator has also gone through a bankruptcy proceeding and there is a new operator who has assumed the same obligations. Although the Marketplace construction was substantially completed, several items on a Harbors Division construction punch list have yet to be completed and were pursued with the new operator. Many of the items were completed by the Harbors Division and the actual cost to complete the punchlist items were in dispute. A settlement was reached with the new operator to satisfy the punchlist obligations which have a total value of $3.5 million, depending upon when actual payments are made by the operator within a six-year timeframe.

On January 18, 2006, an Agreement amending the Aloha Tower Project Memorandum of Understanding and Aloha Tower Ground Lease was executed, effective as of June 30, 2005, and retroactive to July 1, 2004 (the Amendment). The Amendment required ATDC to pay $225,000 as a minimum annual base payment for losses in revenues owing in the fiscal year beginning July 1, 2004. From July 1, 2005, subject to the approval of the Deputy Director for the Harbors Division, the base payment of $225,000 was to be reduced by expenses incurred by ATDC for the Hawaii Harbors Project Office. The Amendment also required an equity participation payment to be made in an amount of 50% of the difference between the total revenues and total operating expenses of ATDC for a fiscal year (the equity payment), provided that if the equity payment exceeds two and one-half times the actual operating expenses of ATDC. These payments were to be applied to reduce the amount owed to the Harbors Division for losses in revenues by ATDC prior to July 1, 2004. The balance owed to the Harbors Division by ATDC under this Amendment as of June 30, 2018 and 2017 was approximately $3,368,000 and $3,761,000, respectively, and is included in notes receivable, net of allowance for doubtful accounts for approximately $2,977,000 and $3,761,000 as of June 30, 2018 and 2017, respectively, in the accompanying statements of net position.

At its meeting on July 13, 2011, the ATDC Board approved the transfer of the leasehold interest of the Marketplace to a new operator, Hawaii Lifestyle Retail Properties, (HLRP). HLRP is a limited liability company that consisted at that time of two legal entities, Lifestyle Retail Properties LLC (LRP) and Hawaii Downtown Holdings LLC (HDH); HDH being solely owned by Hawaii Pacific University (HPU). After the transfer of the lease to HLRP in mid 2011, ATDC discussed various development proposals with HLRP culminating in a memorandum of understanding (MOU) dated December 15, 2011. In the 2012 Hawaii Legislative Session, HPU received legislative support for the issuance of special purpose revenue bonds for improvements to their facilities. In mid 2012, a dispute arose among the owners of HLRP which ultimately resulted in HDH buying out LRP’s interest in HLRP and HDH taking control of the leasehold interest in late 2012. The terms of ATDC’s MOU with HLRP, which were performance-based and had not been met, terminated on January 1, 2014. Since the resolution of the owners’ dispute within HLRP, HLRP has been reformulating its plans for improvements to the Marketplace leasehold property.

Subsequent to the year ended June 30, 2014, the State, by its Interim Director of the DOT, entered into a successor MOU with the ATDC and HLRP whereby ATDC agreed to abate rent under the lease between ATDC and HLRP for the period retroactive to July 1, 2014 to June 30, 2015 in consideration for the construction of HLRP improvements to create student and faculty residences and various university spaces for Hawaii Pacific University and to memorialize the understanding of the parties with respect to various aspects of its agreement.

The successor memorandum of understanding also amended the punchlist obligations owed to the Harbors Division which had a total value of $3.5 million, depending upon when actual payments are made by the operator within a six year timeframe ending June 2017. The amendment provided that in consideration of ATDC's issuance of any renewed leases, HLRP shall pay the Harbors Division the sum of $1,750,000 on or before December 31, 2021.

17. Kapalama Land Development

Plans for the development of the Kapalama Military Reservation (KMR) site involve the creation of a new cargo container yard and vessel berthing piers, a key priority under the Harbor's Modernization Plan. During the fiscal year ended June 30, 2017, the Airports Division and Harbors Division continued discussions to resolve the use of approximately 11.344 acres of ceded lands under management and control of the Airports Division that are located near the KMR site of which a portion is planned for inclusion into the KMR container yard development.

On December 12, 2017, an agreement was executed between the Airports Division and the Harbors Division, which effectively conveyed the control and management of the subject 11.344 acres to the Harbors Division for an appraised value of $32,820,000. In accordance with the agreement, the Harbors Division made a payment of $16,410,000 to the Airports Division in June 2018. The remaining $16,410,000 is due to the Airports Division on June 30, 2019, and is included in the accompanying statements of net position as due to other State agencies as of June 30, 2018. The total release price of $32,820,000 is included in nondepreciable capital assets as of June 30, 2018 in the accompanying statements of net position. The agreement also provided for the payment of $4,159,350 from the Harbors Division to the Airports Division for rental income collected by the Harbors Division. This amount was paid on August 7, 2018 and was included in due to other State agencies as of June 30, 2017 and June 30, 2018.

18. Arbitrage

The Harbors Division is required to annually calculate rebates to the U.S. Treasury on the Revenue Bonds issued from 1986. In accordance with the requirements of Section 148 of Internal Revenue Code of 1986, as amended, rebates are calculated by bond series based on the amount by which the cumulative amount of investment income exceeds the amount that would have been earned had funds been invested at the bond yield. In the opinion of management, rebates payable as of June 30, 2018 and 2017, if any, are not material to the financial statements. Accordingly, no rebates payable have been recorded in the accompanying financial statements.

19. Commitments and Contingencies

Construction and Other Contracts

The Harbors Division is committed under contracts awarded for construction and other services. These commitments amounted to approximately $198,865,000 and $62,578,000 at June 30, 2018 and 2017, respectively.

Accumulated Sick Leave Pay

Employees earn sick leave credits at the rate of 14 hours for each month of service depending on the employee’s hire date. Unused sick leave may be accumulated without limitation and is not convertible to pay upon termination of employment. Accordingly, no liability for sick pay is recorded. However, for public employees who retire or leave government service in good standing with sixty days or more of unused sick leave, the unused sick leave is converted to additional retirement service credit at the rate of one additional month of service for each 20 days of unused sick leave. The accumulated sick leave liabilities as of June 30, 2018 and 2017 were approximately $6,146,000 and $6,057,000, respectively.

Environmental Issues

Iwilei District Participating Parties

The Harbors Division is subject to laws and regulations relating to the protection of the environment. The Harbors Division has been identified by the State Department of Health as a potentially responsible party for petroleum contamination in the Honolulu Harbor/Iwilei area. Pursuant thereto, the Harbors Division entered into a voluntary agreement with the Department of Health and other third parties to share in the responsibility for the investigation and potential remediation of petroleum contamination in the Iwilei District. This group of potentially responsible parties, known as the Iwilei District Participating Parties (IDPP), has conducted various investigations to determine potential contamination in the Iwilei area from 1997 to present, which investigations have determined the existence of petroleum contamination at various locations. The remediation alternative selected involves the management of the contamination in-place with limited extraction, plume monitoring, active institutional controls including education/awareness and outreach of landowners, potential developers and utility operators, and reimbursement of future incremental project costs attributable to the contamination. However, the project has not yet advanced to the stage where total costs to the IDPP can reasonably be estimated due to: (1) the extent of the environmental impact, (2) the undetermined allocation among the potentially responsible parties, and (3) the continued discussion with the regulatory authorities. Although it is not possible to reasonably estimate the Harbors Division cost liability until these items have been resolved, the Harbors Division, in accordance with GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations* (GASB 49), accrued only for the estimated cost of the studies and investigations allocated to the Harbors Division of approximately $2,599,000 as of June 30, 2018.

Environmental Protection Agency

During December 2008, the United States Environmental Protection Agency (EPA) conducted an audit to determine Harbors Division's compliance with its Storm Water Environmental Permits (SWMP). As a follow up to this audit, on June 18, 2009, the EPA issued an Administrative Order directing the Harbors Division to revise its Storm Water Management Plan, upgrade environmental inspections and procedures, improve documentation of environmental inspections and follow up actions, establish "Best Management Practices" (BMPs) standards, and include the use of permanent BMPs in any construction projects that are undertaken on Harbor Division premises.

In July 2012, the EPA and the U.S. Department of Justice provided a Compliance Measures draft for the Harbors Division's review and comment. The Compliance Measures draft is intended to be the Injunctive Relief portion of the comprehensive Consent Decree between the United States, the State of Hawaii Department of Health and the Department of Transportation.

On September 18, 2014, the U.S. Department of Justice lodged a proposed Consent Decree with the United States District Court for the District of Hawaii in the lawsuit entitled United States et al. v. Hawaii Department of Transportation, Civil Case No. 14-00408. The Department agreed to correct federal Clean Water Act violations at Honolulu and Kalaeloa Barbers Point Harbors on Oahu, modify departmental administrative and operational procedures and pay a civil penalty of $600,000 plus interest to the U.S. Department of Justice and $600,000 plus interest to the Hawaii Department of Health. Under the conditions of the Consent Decree, the Department is required to implement structural changes to management and a comprehensive stormwater management plan over the life of the Consent Decree. The Consent Decree was entered on November 5, 2014 and payments of $600,160 were remitted accordingly to each party.

The Harbors Division entered into an agreement with Weston Solutions, Inc., an international environmental consulting firm, to assist in negotiating the Compliance Measures for a cost of approximately $600,000, which was amended during fiscal year 2015 to $900,000, of which has been fully paid as of June 30, 2017. The Harbors Division has also entered into an agreement with EnviroServices and Training Center LLC, a Hawaii environmental consulting firm, to assist the Harbors Division in implementing the Compliance Measures at a cost of approximately $400,000 which was later amended to $800,000, of which approximately $380,000 has been paid as of June 30, 2018.

Other

The Harbors Division accrued the estimated cost of approximately $997,000 for the Nawiliwili harbor storage tank removal and related environmental remediation as of June 30, 2018.

Litigation

The Harbors Division is subject to a number of lawsuits arising in the ordinary course of its operations. While the ultimate liabilities, if any, in the disposition of these matters are presently difficult to estimate, it is management's belief that the outcomes are not likely to have a material adverse effect on the Harbors Division's financial position. Accordingly, no provisions for any liabilities that might result have been made in the accompanying financial statements.

20. Subsequent Events

The Harbors Division has evaluated subsequent events from the statements of net position date through December 6, 2018 the date at which the financial statements were available to be issued, and determined that there are no other items to disclose.

SUPPLEMENTARY INFORMATION

Harbors Division
Department of Transportation
State of Hawaii
(An Enterprise Fund of the State of Hawaii)

Cash and Cash Equivalents of the Public Undertaking

June 30, 2018

Unrestricted cash and cash equivalents	$ 185,531,299
Restricted cash and cash equivalents:	
For construction−special purpose funds	170,390,363
For revenue bond debt service payments	22,945,609
For cash reserve requirement for Series A of 2010 revenue bonds	11,455,033
For revenue bond harbors reserve and contingency account	10,897,658
For security deposits	3,010,919
For risk management and other	2,355,281
	221,054,863
	$ 406,586,162

With Director of Finance, State of Hawaii	$ 403,922,261
On hand	2,663,901
	$ 406,586,162

See accompanying independent auditors' report.

Harbors Division
Department of Transportation
State of Hawaii
(An Enterprise Fund of the State of Hawaii)

Revenue Bonds of the Public Undertaking

June 30, 2018

	Final Redemption Date	Interest Rate	Original Amount of Issue	Balance at June 30, 2018		
				Current	Noncurrent	Total
Issue of 2010	July 1, 2040	3.00-5.75%	$ 201,390,000	$ 5,495,000	$ 160,275,000	$ 165,770,000
Issue of 2013	July 1, 2029	3.25%	23,615,000	3,105,000	16,615,000	19,720,000
Issue of 2016 Series A	January 1, 2024	1.99%	14,565,000	1,995,000	10,630,000	12,625,000
Issue of 2016 Series B	January 1, 2031	2.46-2.89%	68,535,000	5,145,000	59,790,000	64,935,000
Issue of 2016 Series C	July 1, 2020	2.34%	8,135,000	1,000,000	7,135,000	8,135,000
Issue of 2016 Series D	July 1, 2027	3.09%	22,425,000	15,000	22,410,000	22,425,000
			$ 338,665,000	$ 16,755,000	$ 276,855,000	$ 293,610,000

See accompanying independent auditors' report.

Schedule 3

Harbors Division
Department of Transportation
State of Hawaii
(An Enterprise Fund of the State of Hawaii)

Income from Operations Before Depreciation

Year Ended June 30, 2018

		District									
		Oahu		**Hawaii**		**Maui**			**Kauai**		
	Statewide	**Honolulu**	**Kalaeloa**	**Hilo**	**Kawaihae**	**Kahului**	**Kaunakakai**	**Kaumalapau**	**Nawiliwili**	**Port Allen**	**Total**
Operating revenues, net:											
Services:											
Wharfage	$ -	$ 92,015,725	$ 4,057,962	$ 4,311,654	$ 5,067,346	$ 8,073,985	$ 299,565	$ 371,765	$ 3,970,255	$ -	$ 118,168,257
Pax debark/embark	-	3,285,795	-	2,173,170	5,303	1,075,575	5,318	-	1,619,145	-	8,164,306
Dockage	-	3,713,965	730,260	283,552	61,946	449,630	14,663	5,969	429,541	2,892	5,692,418
Demurrage	-	824,821	-	386,152	122,234	92,287	11,764	346	34,648	-	1,472,252
Mooring charges	-	693,763	114,477	77,536	37,776	92,846	9,529	5,212	78,552	2,791	1,112,482
Port entry	-	332,885	-	13,350	34,574	513	2,322	-	-	713,850	1,097,494
Cleaning charges	-	306,588	-	-	-	-	-	-	-	-	306,588
Other services	-	5,580	150	3,959	3,858	462	-	-	374	10,867	25,250
Total services	-	101,179,122	4,902,849	7,249,373	5,333,037	9,785,298	343,161	383,292	6,132,515	730,400	136,039,047
Rentals:											
Wharf space and land	-	10,251,108	2,255,475	74,016	415,741	190,253	28,153	300	405,268	242,698	13,863,012
Storage	-	4,630,548	88,537	310,694	491,825	660,829	3,250	558	302,510	19,809	6,508,560
Automobile parking	-	1,075,845	1,452	115,946	10,147	168,010	479	-	67,652	9,401	1,448,932
Pipeline water	-	138,002	4,193	53,880	1,216	109,384	-	-	84,973	-	391,648
Other pipeline	-	1,236,446	1,641,638	866,124	156,223	1,082,241	11,725	-	334,552	143,341	5,472,290
Total rentals	-	17,331,949	3,991,295	1,420,660	1,075,152	2,210,717	43,607	858	1,194,955	415,249	27,684,442
Others:											
Sale of utilities	-	132,948	111,615	38,132	1,469	156,359	62	-	77,227	8,435	526,247
Miscellaneous	-	862,992	(12,930)	11,046	3,997	(14,691)	926	-	9,661	489	861,490
Total others	-	995,940	98,685	49,178	5,466	141,668	988	-	86,888	8,924	1,387,737
Total operating revenues	-	119,507,011	8,992,829	8,719,211	6,413,655	12,137,683	387,756	384,150	7,414,358	1,154,573	165,111,226
Operating expenses before depreciation expenses:											
Harbor operations	15,133,897	5,061,644	631,121	569,678	456,582	934,289	19,875	830	624,057	34,561	23,466,534
Personal services	9,517,882	8,576,184	234,615	1,086,661	52,155	1,256,244	31,401	5,527	1,104,938	55,978	21,921,585
State of Hawaii, surcharge for central service expenses	6,068,244	-	-	-	-	-	-	-	-	-	6,068,244
Maintenance	362,823	1,593,093	11,899	117,987	46,846	712,340	95,779	12,702	1,039,857	131,044	4,124,370
General administration	2,303,599	89,801	2,021	26,453	71,301	17,364	786	10	172,696	1,377	2,685,408
Department of Transportation, general administration expenses	1,335,022	-	-	-	-	-	-	-	-	-	1,335,022
Subtotal	34,721,467	15,320,722	879,656	1,800,779	626,884	2,920,237	147,841	19,069	2,941,548	222,960	59,601,163
Allocation of statewide expenses (1)	(34,721,467)	25,131,294	1,891,114	1,833,575	1,348,736	2,552,450	81,542	80,783	1,559,176	242,797	-
Total operating expenses before depreciation expense	-	40,452,016	2,770,770	3,634,354	1,975,620	5,472,687	229,383	99,852	4,500,724	465,757	59,601,163
Income (loss) from operations before depreciation expense	$ -	$ 79,054,995	$ 6,222,059	$ 5,084,857	$ 4,438,035	$ 6,664,996	$ 158,373	$ 284,298	$ 2,913,634	$ 688,816	$ 105,510,063

Note (1): Statewide expenses are allocated to the Harbors Division based upon their respective current year operating revenues to total current year operating revenues for all Harbors.

See accompanying independent auditors' report.

Harbors Division
Department of Transportation
State of Hawaii
(An Enterprise Fund of the State of Hawaii)

Harbor Revenue Bonds 1997 Certificate – Minimum Net Revenue
Requirement of the Public Undertaking

Year Ended June 30, 2018

Net revenues, as defined by the 1997 Certificate:	
Operating income before depreciation expense	$ 105,510,063
Add:	
Interest income	5,488,391
State of Hawaii, surcharge for central service expenses	6,068,244
Cash available in the harbor reserve and contingency account	10,897,658
	$ 127,964,356
Harbor revenue bond debt service requirements under the 1997 Certificate, including minimum sinking fund payments	$ 29,113,861
Ratio of net revenues to harbor revenue bond debt service requirements	4.40

See accompanying independent auditors' report.

PART III

INTERNAL CONTROL AND COMPLIANCE SECTION

Independent Auditors' 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*

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 statements of net position of the Harbors Division, Department of Transportation, State of Hawaii (the Harbors Division), as of June 30, 2018 and 2017, and the related statements of revenues, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to financial statements, which collectively comprise the Harbors Division's basic financial statements, and have issued our report thereon dated December 6, 2018.

Internal Control over Financial Reporting

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

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

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

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Harbors Division'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*.

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.

KKDLY LLC

Honolulu, Hawaii
December 6, 2018