

State of Hawai‘i
Department of Hawaiian Home Lands

Financial and Compliance Audit
June 30, 2018



AKAMINE, OYADOMARI & KOSAKI
CPA'S, INC.

State of Hawai‘i
Department of Hawaiian Home Lands

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Part I

Financial Section





Independent Auditor's Report

The Auditor
State of Hawai'i

The Hawaiian Homes Commission
Department of Hawaiian Home Lands

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Department of Hawaiian Home Lands, State of Hawai'i (the "Department"), as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Department's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Department'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 Department's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

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

Emphasis of Matter

As discussed in Note A, the financial statements of the Department include only the governmental activities, each major fund, and the aggregate remaining fund information of the Department, and are not intended to present fairly the financial position of the State of Hawai'i (the "State") as of June 30, 2018, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America. 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 and budgetary comparison information on pages 7 through 15 and pages 22 through 23, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

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

The combining non-major fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such



information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining non-major fund financial statements and the schedule of expenditures of federal awards are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 5, 2019 on our consideration of the Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Department's internal control over financial reporting and compliance.

Akamine, Oyadomari & Kosaki CPAs, Inc.

Honolulu, Hawai'i
March 5, 2019



State of Hawai‘i
Department of Hawaiian Home Lands
Management’s Discussion and Analysis (Unaudited)
June 30, 2018

The following Management’s Discussion and Analysis (“MD&A”) is designed to provide an overview of the financial performance of the State of Hawai‘i, Department of Hawaiian Home Lands (the “Department”) for the fiscal year ended June 30, 2018. Please read it in conjunction with the Department’s financial statements, which follow this section.

Financial Highlights for Fiscal Year 2018

- The Department’s net position, the amount of assets exceeding liabilities, totaled \$867.6 million. Of this amount, \$273.9 million is unrestricted, \$152.3 million is restricted, and \$441.4 million is net investment in capital assets.
- The Department’s net position increased \$47.2 million over the course of this year’s operations.
- In fiscal year 2018, the Department’s revenues exceeded expenses (before transfers) by \$43.2 million. In fiscal year 2017, the revenues exceeded expenses (before transfers) by \$8.6 million.
- The total revenues of the Department increased by \$40.5 million, or 65%.
- The total fund balance of the Department’s governmental funds increased by \$48.1 million.

Overview of the Financial Statements

This MD&A serves as an introduction to the Department’s basic financial statements. The basic financial statements are comprised of three components: (1) department-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report also contains other supplementary information (combining financial statements – non-major governmental funds) in addition to the basic financial statements.

The first two statements are department-wide financial statements that provide both long-term and short-term information about the Department’s overall financial status and operations.

The fund financial statements focus on individual parts of the Department, reporting the Department’s status and operations in more detail than the department-wide financial statements. These statements detail how general departmental services were financed in the short-term as well as what remains for future spending.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

Department-Wide Financial Statements

The department-wide financial statements provide a broad view of the Department’s operations. The statements provide both short-term and long-term information about the Department’s financial position and activities, which assists in assessing the Department’s economic condition at the end of the fiscal year and operations for the year then ended. These statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting.

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The department-wide financial statements include two statements:

- The statement of net position presents all of the Department’s assets and liabilities. The difference between the assets and liabilities is reported as net position.
- The statement of activities presents information showing how the Department’s net position changed during the fiscal year. This statement presents a comparison between direct expenses and program revenues for each division of the Department.

The activities of the Department are mostly supported by state appropriation, rental income from commercial land leases, and intergovernmental revenues. The Department’s basic services fall under these types of activities.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Department uses fund accounting to ensure and demonstrate compliance with legal requirements.

The fund financial statements provide more detailed information about the Department’s status and operations. Certain of the Department’s funds were established under State of Hawai‘i (“State”) Law or by bond covenants. Other funds of the Department are established by the Hawaiian Homes Commission Act. These funds manage money for particular purposes.

The Department only has governmental funds which finance the Department’s basic services. Governmental funds are used to account for essentially the same functions reported as governmental activities in the department-wide financial statements. However, unlike the department-wide financial statements, the fund financial statements focus on near-term inflows and outflows of spendable resources as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the Department’s short-term financing requirements.

Because the focus of fund financial statements is narrower than that of the department-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the department-wide financial statements. By doing so, readers may better understand the long-term impact of the Department’s short-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The Department has 15 governmental funds, ten of which are separately disclosed as major funds for presentation purposes. Each major fund is presented in a separate column in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures and changes in fund balance.

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These funds are briefly described as follows:

- **General Fund** – The General Fund is authorized and appropriated by the State Legislature each year for planning, development, management and general support for the Hawaiian Homestead Program.
- **Hawaiian Home General Loan Fund** – Act 249, SLH 1986, amended this revolving loan fund and consolidated all loan funds other than the Hawaiian Home Loan Fund in 1986. The major source of receipts for this fund is through principal repayment. The Department can make loans from the revolving funds for the construction of homes, home repairs or additions, or for the development and operation of a farm, ranch or agriculture operation.
- **Hawaiian Home Lands Trust Fund** – This fund was established by Act 14, Special Session 1995, which settles all claims made on behalf of the Hawaiian Home Land Trust against the State between August 21, 1959 and July 1988. It requires that the State make twenty annual deposits of \$30 million or their discounted equivalent into the Hawaiian Home Lands Trust Fund. Proceeds of the fund may be used by the Department for capital improvements and other purposes undertaken in furtherance of the Hawaiian Homes Commission Act of 1920, as amended.
- **Hawaiian Home Operating Fund** – This fund was established through a merger of the Hawaiian Home Development Fund and Hawaiian Home Operating Fund in 1986. Any interest or earnings arising out of investments from the Hawaiian Home Loan Fund are to be credited to and deposited into the Hawaiian Home Operating Fund. All monies received by the Department from any other source, other than those prescribed in other funds of the Hawaiian Homes Commission Act, are deposited into this fund. The Department uses the fund for the construction, operation and maintenance of revenue-producing activities that are intended to serve principally occupants on Hawaiian home lands. The fund is also used to finance improvements and developments necessary to serve present and future occupants of Hawaiian home lands.
- **Hawaiian Home Receipts Fund** – All interest monies from loans or investments received by the Department from any fund, except the Hawaiian Home Loan Fund, Hawaiian Home Administration Account, Native Hawaiian Rehabilitation Fund, Department of Hawaiian Home Lands Revenue Bond Special Fund and Hawaiian Home Lands Trust Fund, are deposited into this fund. This fund serves as a clearing fund at the end of each quarter. All monies in this fund are transferred to other funds as authorized by the Hawaiian Homes Commission Act.
- **Hawaiian Home Administration Account** – The revenue sources of this fund are the entire receipts from any leasing or other dispositions of “available lands” and any interest or other earnings arising out of investments from this fund. The Department expends the monies for salaries and all other administrative expenses of the Department, excluding capital improvements, in the absence of general funds appropriated for operating and administrative costs.
- **Federal Grants** – The Department is the recipient of an annual block grant under the Native American Housing Assistance and Self-Determination Act of 1996 (“NAHASDA”). The U.S. Department of Housing and Urban Development (“HUD”) is the cognizant entity of the NAHASDA grant in carrying out affordable housing activities for Native Hawaiian families qualified for this program.

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- **Hawaiian Home Trust Fund** – Monies deposited into this fund are available for transfers into any other fund or account authorized by the Act or for any public purpose to further the purposes of the Act. Public purpose includes using the Hawaiian Home Trust Fund as a reserve for loans insured or guaranteed by the HUD Federal Housing Administration, Veteran Administration or any other federal agency authorized to insure or guarantee loans. A major portion in the Hawaiian Home Trust Fund is the reserve for loans insured by the HUD Federal Housing Administration.
- **Hawaiian Home Lands Bond Fund** – The Bond Funds are funded through budget bills passed by the State Legislature and approved by Governor. The appropriations can be used for construction projects and GIAs (Grant-in-Aid) Projects.
- **Department of Hawaiian Home Lands Revenue Bond Special Fund** – This fund serves as DHHL’s debt service fund and accounts for the accumulation of resources for payment of general long-term debt principal and interest. The principal sources of funds are transfer of funds from revenues from available lands, interest earned and funds from OHA for debt service payment.

The accompanying notes to the financial statements are part of the financial statements. The notes provide additional information that is essential to gain a full understanding of the information provided in the department-wide and fund financial statements.

In addition to the basic financial statements and accompanying notes, this report also presents other supplementary information consisting of the combining balance sheet and combining statement of revenues, expenditures and changes in fund balances in connection with non-major governmental funds and schedule of expenditures of federal awards.

Financial Analysis of the Department as a Whole

Net Position

The Department’s total net position increased by \$43.2 million to \$867.6 million between fiscal years 2018 and 2017, primarily due to an increase in intergovernmental revenues along with the appropriation of general funds and bond funds for CIP related projects and grant-in-aid (GIA) the Department received during fiscal year 2018. A large portion of the Department’s net position (50%) reflects its investment in capital assets such as land, buildings, infrastructure, furniture and equipment, and construction-in-progress. The Department uses these capital assets to provide improvements on a special class of public lands, which are leased to native Hawaiians; consequently, these assets cannot be sold. Although the Department’s investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets cannot be used to liquidate these liabilities.

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The following is a comparative statement of net position:

Summary of Statement of Net Position
(in millions)

	2018	2017	Increase (Decrease)
Current and other assets	\$ 477.3	\$ 440.5	\$ 36.8
Capital assets	494.1	507.3	(13.2)
Deferred outflows of resources	3.5	-	3.5
Total assets and deferred outflows of resources	<u>\$ 974.9</u>	<u>\$ 947.8</u>	<u>\$ 27.1</u>
Long-term liabilities	\$ 53.3	\$ 58.7	\$ (5.4)
Other liabilities	54.0	64.7	(10.7)
Total liabilities	<u>\$ 107.3</u>	<u>\$ 123.4</u>	<u>\$ (16.1)</u>
Net position			
Net investment in capital assets	\$ 441.4	\$ 446.1	\$ (4.7)
Restricted	152.3	155.5	(3.2)
Unrestricted	273.9	222.8	51.1
Total net position	<u>\$ 867.6</u>	<u>\$ 824.4</u>	<u>\$ 43.2</u>

Change in Net Position

The Department’s total program revenues increased from \$45.4 million in fiscal year 2017 to \$51.8 million in fiscal year 2018 (see statement of activities). Approximately 18.5% of the Department’s program revenues came from interest income, 43.05% came from grants and contributions, 34.2% came from the general lease program, and 4.25% came from other sources. Total general revenues increased by 206% to \$50.6 million due to a increase in general fund and bond fund appropriations received in fiscal year 2018 as compared to fiscal year 2017 for construction projects and grants-in-aid funding for community organizations.

Statement of Activities

The statement of activities presents how the Department’s net position changed during the current fiscal year. Revenues and expenses are reported as soon as the underlying event occurs, regardless of the timing of the related cash flows. As such, the statement includes information for some items that will result in cash flows in future fiscal periods (e.g., uncollected lease payments).

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The following is a comparative summary of changes in net position:

Summary of Changes in Net Position
(in millions)

	<u>2018</u>	<u>2017</u>	<u>Increase (Decrease)</u>
Revenues			
Program revenue			
Administration and support services	\$ 6.0	\$ 3.8	\$ 2.2
Homestead services	5.6	5.2	0.4
Land development	-	-	-
Home construction	0.2	0.2	-
Land management	17.7	16.8	0.9
Intergovernmental revenues	22.3	19.4	2.9
Appropriations, net of lapses and transfers	<u>50.6</u>	<u>16.5</u>	<u>34.1</u>
Total revenues	<u>102.4</u>	<u>61.9</u>	<u>40.5</u>
Expenses			
Administration and support services	\$ 13.6	\$ 12.5	\$ 1.1
Homestead services	31.3	29.7	1.6
Land development	7.7	3.2	4.5
Home construction	2.1	4.8	(2.7)
Land management	<u>4.5</u>	<u>3.1</u>	<u>1.4</u>
Total expenses	<u>59.2</u>	<u>53.3</u>	<u>5.9</u>
Excess of revenues over expenses	43.2	8.6	34.6
Net position			
Beginning of year	<u>824.4</u>	<u>815.8</u>	<u>8.6</u>
End of year	<u>\$ 867.6</u>	<u>\$ 824.4</u>	<u>\$ 43.2</u>

As noted, net position increased by \$43.2 million from operations, a 5.2% growth this year, compared to an increase of \$8.6 million, a 1.1% growth in fiscal year 2017. The fiscal year 2018 increase is primarily due to an increase in bond funds received for various construction projects and Grant-In-Aid (GIA) projects which DHHL is the pass-through agency.

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Financial Analysis of the Department’s Governmental Funds

Governmental Funds

The focus of the Department’s governmental funds is to provide information on short-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Department’s financing requirements. In particular, unassigned fund balances may serve as a useful measure of a government’s net resources available for spending at the end of the fiscal year.

As of the end of fiscal year 2018, the Department’s governmental funds reported a combined increase in fund balance of \$48.1 million. The changes in fund balance for the governmental funds differ from the change in net position for governmental activities. The differences relate to certain financial resources and expenditures such as debt financing and capital outlays that are included in the changes in fund balances but are not reported in the changes in net position.

Comparison of Balance Sheet
(in millions)

	Assets			Liabilities			Fund Balances		
	2018	2017	Change	2018	2017	Change	2018	2017	Change
General Fund	\$ 5.4	\$ 4.3	\$ 1.1	1.0	0.9	0.1	4.4	3.4	1.0
General Loan Fund	104.1	105.2	(1.1)	35.7	38.9	(3.2)	68.4	66.3	2.1
Land Trust Fund	155.5	155.1	0.4	1.5	0.9	0.6	154.0	154.2	(0.2)
Operating Fund	51.9	36.5	15.4	4.6	1.4	3.2	47.3	35.1	12.2
Receipts Fund	7.5	6.5	1.0	4.3	4.0	0.3	3.2	2.5	0.7
Administration Account	44.6	50.5	(5.9)	3.2	4.3	(1.1)	41.4	46.2	(4.8)
Federal Grants	36.7	38.1	(1.4)	6.5	20.1	(13.6)	30.2	18.0	12.2
Trust Fund	46.5	43.8	2.7	34.3	31.6	2.7	12.2	12.2	-
Bond Fund	37.1	10.0	27.1	1.8	0.2	1.6	35.3	9.8	25.5
Revenue Bond	13.2	14.0	(0.8)	0.8	0.8	-	12.4	13.2	(0.8)
Other Funds	14.0	14.0	-	2.5	2.7	(0.2)	11.5	11.3	0.2
Total	<u>\$ 516.5</u>	<u>\$ 478.0</u>	<u>\$ 38.5</u>	<u>\$ 96.2</u>	<u>\$ 105.8</u>	<u>\$ (9.6)</u>	<u>\$ 420.3</u>	<u>\$ 372.2</u>	<u>\$ 48.1</u>

Comparison of Statement of Revenues, Expenditures, and Changes in Fund Balances
(in millions)

	Revenues			Expenditures			Other Financing Sources and Lapsed Appropriations			Fund Balances		
	2018	2017	Change	2018	2017	Change	2018	2017	Change	2018	2017	Change
General Fund	\$ 17.9	\$ 17.1	\$ 0.8	13.9	11.9	2.0	(3.0)	(1.9)	(1.1)	1.0	3.3	(2.3)
General Loan Fund	-	-	-	2.2	0.9	1.3	4.4	4.7	(0.3)	2.2	3.8	(1.6)
Land Trust Fund	2.7	1.7	1.0	2.9	6.0	(3.1)	-	-	-	(0.2)	(4.3)	4.1
Operating Fund	1.9	1.1	0.8	9.8	2.5	7.3	20.0	-	20.0	12.1	(1.4)	13.5
Receipts Fund	5.2	5.2	-	-	-	-	(4.4)	(4.7)	0.3	0.8	0.5	0.3
Administration Account	19.1	16.5	2.6	4.3	3.5	0.8	(19.4)	1.3	(20.7)	(4.6)	14.3	(18.9)
Federal Grants	17.8	19.7	(1.9)	5.6	10.8	(5.2)	-	-	-	12.2	8.9	3.3
Trust Fund	-	-	-	-	-	-	-	-	-	-	-	-
Bond Fund	34.4	-	34.4	8.8	2.0	6.8	(0.2)	-	(0.2)	25.4	(2.0)	27.4
Revenue Bond	5.2	0.1	5.1	6.3	3.0	3.3	0.4	-	0.4	(0.7)	(2.9)	2.2
Other Funds	0.4	0.6	(0.2)	0.5	0.3	0.2	-	-	-	(0.1)	0.3	(0.4)
Total	<u>\$ 104.6</u>	<u>\$ 62.0</u>	<u>\$ 42.6</u>	<u>\$ 54.3</u>	<u>\$ 40.9</u>	<u>\$ 13.4</u>	<u>\$ (2.2)</u>	<u>\$ (0.6)</u>	<u>\$ (1.6)</u>	<u>\$ 48.1</u>	<u>\$ 20.5</u>	<u>\$ 27.6</u>

Overall, the assets for the Department increased by \$38.5 million, liabilities decreased by \$9.6 million, and fund balance increased by \$48.1 million.

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Budgetary Highlights

In fiscal year 2018, the General Fund Account received appropriations amounting to \$17.9 million. This amount was expended according to the budget except \$1,600,218 was lapsed.

In the Hawaiian Home Administration Account, the actual revenue exceeded the budgeted amount by \$14.2 million and expenditures were \$2.3 million more than the budgeted amount. The overall favorable variance of \$11.9 million was created by expenditure control measures.

Capital Asset and Debt Administration

Capital Assets

At the end of fiscal year 2018, the Department had invested \$820.7 million in a broad range of capital assets, including land, building and improvements, furniture and equipment, and infrastructure. This amount represents a net increase (including additions, deductions and reclassifications) of \$11.1 million, or 1.4%, over last year.

Capital Assets
(in millions)

	2018	2017	Increase (Decrease)
Buildings and improvements	\$ 29.2	\$ 29.2	\$ -
Furniture and equipment	5.6	5.6	-
Motor vehicles	1.4	1.4	-
Infrastructure	693.9	691.8	2.1
Total depreciable assets	730.1	728.0	2.1
Less: Accumulated depreciation	(326.6)	(302.3)	(24.3)
Net depreciable assets	403.5	425.7	(22.2)
Land	41.8	41.8	-
Land improvements	33.4	33.4	-
Construction in progress	15.4	6.4	9.0
Total capital assets	<u>\$ 494.1</u>	<u>\$ 507.3</u>	<u>\$ (13.2)</u>

In fiscal year 2018, the Department expended \$9.7 million for various capital projects, including \$5.4 million for Papakolea Sewer Improvements, \$0.8 million for Hoolehua Water System Improvements, \$0.6 million for Anahola Farm Lots Water System Improvements and \$2.8 million for various other projects.

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Long-Term Debt

In 2009, the Department issued Revenue Bonds, Series 2009, to fund the planning, design and construction projects on the Hawaiian Home Lands. In August 2017, the Department advance refunded the Series 2009 Revenue Bonds with the Series 2017 Revenue Bonds. The Department also has a note payable to reimburse the Housing and Community Development Corporation of Hawaii for infrastructure costs over a 15-year period.

Outstanding Debt
(in millions)

	2018	2017	Increase (Decrease)
Notes payable	\$ 4.7	\$ 6.4	\$ (1.7)
Capital lease obligation	16.6	18.5	(1.9)
Bonds payable, net	34.9	36.3	(1.4)
Total outstanding debt	<u>\$ 56.2</u>	<u>\$ 61.2</u>	<u>\$ (5.0)</u>

Economic Factors and Next Year’s Budgets

Revenues generated from general leases, revocable permits, licenses and right of entry agreements are projected to total \$19.5 million. This represents a decrease of 0.010% from the prior fiscal year projection. The decrease is due to cancellation of several accounts and/or rent adjustments or fees.

Currently Known Facts or Decisions

As stewards of the Hawaiian Home Lands Trust, the Department remains focused on the core mission of returning native Hawaiians to the land, as envisioned by founder Prince Jonah Kuhio Kalaniana‘ole.

In the ongoing effort to effectively manage the trust, the Department spent much of this fiscal year laying the foundation of rules and policies that will have profound impacts on the future of the trust and the beneficiaries we serve.

At the top of the list of priorities is stabilizing department funding in light of the *Nelson v. Hawaiian Homes Commission* ruling. In FY 2018, the Department received another record-setting appropriation of general funds from the State Legislature of \$23.5 million.

In addition to stabilizing department funding, accomplishments this fiscal year included the beginning of a phased reorganization of DHHL staff to better meet demands of beneficiaries and right-fit positions and functions; the establishment of Planning Office Rules as a comprehensive method to systematically coordinate decisions to include regular engagement, predictability and consistency; and finalizing a Hawaiian Homes Commission approved endowment policy to set the DHHL on a course toward fiscal sustainability.

State of Hawai‘i
Department of Hawaiian Home Lands
Statement of Net Position
June 30, 2018

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES

ASSETS

Cash in State Treasury (Note C)	\$ 349,384,804
Receivables	
Loans, net of allowance for losses of \$16,106,000 (Note D)	95,423,435
Accrued interest	6,326,817
General leases and licenses, net of allowance for losses of \$3,435,000	3,370,788
Due from developers	10,000,000
Other, net of allowance for losses of \$345,000	6,475,921
Inventory of homes purchased from former lessees (Note E)	3,522,430
Inventory of homes for sale and development	169,554
Restricted cash and short-term investments held outside of State Treasury (Note F)	2,442,346
Prepaid expenses	81,357
Capital assets, net (Note G)	494,142,400
	<hr/>
Total assets	971,339,852

DEFERRED OUTFLOWS OF RESOURCES

Deferred loss on refunding	3,535,495
	<hr/>
Total assets and deferred outflows of resources	\$ 974,875,347

LIABILITIES AND NET POSITION

LIABILITIES

Vouchers and contracts payable	\$ 5,693,228
Interest payable	467,500
Temporary deposits payable	34,346,232
Other liabilities	4,083,250
Unearned revenue	843,146
Due to Federal agency	4,047,123
Due within one year	
Notes payable (Note I)	1,700,000
Capital lease obligation (Note J)	750,000
Bonds payable (Note K)	1,575,000
Accrued vacation	436,315
Due in more than one year	
Notes payable (Note I)	3,000,000
Capital lease obligation, net of premium (Note J)	15,890,129
Bonds payable, net of premium (Note K)	33,308,055
Accrued vacation	1,108,162
	<hr/>
Total liabilities	107,248,140

Commitments and contingencies (Note N)

NET POSITION

Net investment in capital assets	441,454,711
Restricted for	
Capital projects	51,893,444
Debt reserve agreements	2,442,346
Loans and loan commitments	95,423,435
Guaranteed and insured loans	2,500,000
Unrestricted	273,913,271
	<hr/>
Total net position	867,627,207
	<hr/>
Total liabilities and net position	\$ 974,875,347

The accompanying notes are an integral part of the financial statements.



State of Hawai‘i
Department of Hawaiian Home Lands
Statement of Activities
for the year ended June 30, 2018

Functions/Programs	Program Expenses	Program Revenue		Net (Expense) Revenue and Changes in Net Position
		Charges for Services	Operating Grants and Contributions	
Administration and support services	\$ 13,627,901	\$ 6,040,315	\$ 22,313,142	\$ 14,725,556
Homestead services	31,354,748	5,563,216	-	(25,791,532)
Land development	7,660,592	-	-	(7,660,592)
Home construction	2,129,811	187,900	-	(1,941,911)
Land management	4,506,429	17,723,062	-	13,216,633
Total governmental activities	<u>\$ 59,279,481</u>	<u>\$ 29,514,493</u>	<u>\$ 22,313,142</u>	<u>\$ (7,451,846)</u>
General revenues:				
State appropriations, net of lapsed appropriations of \$1,783,717				50,610,667
Transfers and adjustments, net				<u>1,001</u>
Total general revenues				50,611,668
Change in net position				43,159,822
Net position at July 1, 2017				<u>824,467,385</u>
Net position at June 30, 2018				<u>\$ 867,627,207</u>

The accompanying notes are an integral part of the financial statements.



State of Hawai'i

Department of Hawaiian Home Lands

Balance Sheet

Governmental Funds

June 30, 2018

	General Fund	Hawaiian Home General Loan Fund	Hawaiian Home Lands Trust Fund	Hawaiian Home Operating Fund	Hawaiian Home Receipts Fund	Hawaiian Home Administration Account	Federal Grants	Hawaiian Home Trust Fund	Hawaiian Home Lands Bond Funds	Department of Hawaiian Home Lands Revenue Bond Special Fund	Other Funds	Total
ASSETS												
Cash in State Treasury	\$ 5,412,551	\$ 28,147,405	\$ 150,703,813	\$ 50,687,062	\$ 1,465,375	\$ 39,341,310	\$ 68,469	\$ 12,199,530	\$ 37,070,632	\$ 12,021,668	\$ 12,266,989	\$ 349,384,804
Receivables	-	-	-	-	-	-	-	-	-	-	-	-
Due from other funds	-	1,038,700	-	-	-	-	4,047,123	34,346,232	-	-	-	39,432,055
Loans, net of allowance for losses of \$16,106,000	-	71,264,431	-	-	-	-	22,549,369	-	-	-	1,609,635	95,423,435
Accrued interest	-	-	-	31,282	6,029,361	-	71,380	-	-	119,020	75,774	6,326,817
General leases and licenses, net of allowances for losses of \$3,435,000	-	-	-	-	-	-	-	-	-	-	-	-
Due from developers	3,876	150,214	4,595,885	1,163,597	18,169	519,322	10,000,000	-	-	-	-	10,000,000
Other	-	-	-	-	-	-	24,858	-	-	-	-	6,475,921
Inventory of homes purchased from former lessees	-	3,522,430	-	-	-	-	-	-	-	-	-	3,522,430
Inventory of homes for sale and development	-	-	169,554	-	-	-	-	-	-	-	-	169,554
Restricted cash and short-term investments held outside of State Treasury	-	-	-	-	-	1,417,214	-	-	-	1,025,132	-	2,442,346
Total assets	\$ 5,416,427	\$ 104,123,180	\$ 155,469,252	\$ 51,881,941	\$ 7,512,905	\$ 44,648,634	\$ 36,761,199	\$ 46,545,762	\$ 37,070,632	\$ 13,165,820	\$ 13,952,398	\$ 516,548,150
LIABILITIES AND FUND BALANCES												
LIABILITIES												
Vouchers and contracts payable	\$ 994,159	\$ -	\$ 410,188	\$ 875,109	\$ -	\$ 722,181	\$ 1,445,454	\$ -	\$ 1,820,764	\$ 752,425	\$ 34,198	\$ 7,054,478
Due to other funds	-	34,148,092	1,047,123	3,198,140	-	-	1,038,700	-	-	-	-	39,432,055
Due to Federal agency	-	-	-	-	-	-	4,047,123	-	-	-	-	4,047,123
Temporary deposits payable	-	-	-	-	-	-	-	34,346,232	-	-	-	34,346,232
Other liabilities	-	1,531,546	-	-	-	-	-	-	-	-	2,551,704	4,083,250
Unearned revenue	-	-	-	508,683	4,279,377	2,441,272	-	-	-	-	-	7,229,332
Total liabilities	994,159	35,679,638	1,457,311	4,581,932	4,279,377	3,163,453	6,531,277	34,346,232	1,820,764	752,425	2,585,902	96,192,470
FUND BALANCES												
Restricted for												
Debt agreements	-	-	-	-	-	1,417,214	-	-	-	1,025,132	-	2,442,346
Guaranteed and insured loans	-	150,000	-	-	-	-	-	2,350,000	-	-	-	2,500,000
Federal loan programs	-	-	-	-	-	-	30,229,922	-	-	-	-	30,229,922
Assigned to												
Home loans and homestead services	-	75,187,842	-	-	3,233,528	-	-	9,849,530	-	-	4,639,495	92,910,395
Land management	5,431,284	-	-	47,300,009	-	40,067,967	-	-	-	-	-	92,799,260
Home construction and land development	-	-	154,011,941	-	-	-	-	-	35,249,868	11,388,263	6,727,001	207,377,073
Unassigned	(1,009,016)	(6,894,300)	-	-	-	-	-	-	-	-	-	(7,903,316)
Total fund balances	4,422,268	68,443,542	154,011,941	47,300,009	3,233,528	41,485,181	30,229,922	12,199,530	35,249,868	12,413,395	11,366,496	420,355,680
Total liabilities and fund balances	\$ 5,416,427	\$ 104,123,180	\$ 155,469,252	\$ 51,881,941	\$ 7,512,905	\$ 44,648,634	\$ 36,761,199	\$ 46,545,762	\$ 37,070,632	\$ 13,165,820	\$ 13,952,398	\$ 516,548,150

The accompanying notes are an integral part of the financial statements.



State of Hawai‘i
Department of Hawaiian Home Lands
Reconciliation of the Governmental Funds Balance Sheet
to the Statement of Net Position
June 30, 2018

Total fund balances - governmental funds \$ 420,355,680

Amounts reported for governmental activities in the statement of net position
are different because:

- (1) Capital assets used in governmental activities are not financial resources and therefore are not reported in the governmental funds. These assets consist of:

Infrastructure assets	\$ 693,862,070	
Land	41,824,231	
Land improvements	33,406,582	
Buildings and improvements	29,188,835	
Construction-in-progress	15,354,787	
Other capital assets	7,058,456	
Accumulated depreciation	<u>(326,552,561)</u>	
		494,142,400

- (2) Prepaid expenses are not current financial resources and therefore are not reported in the government funds. 81,357

- (3) Deferred loss on refunding of bonds payable is not reported in the governmental funds, but are reported in the statement of net position net of accumulated amortization as deferred outflows of resources. 3,535,495

- (4) Certain revenues not collected within 60 days after the end of the year are deferred in the funds. 6,386,186

- (5) Accrued interest payable is not recognized in governmental funds. (467,500)

- (6) Long-term debt payment accruals are included as an expenditure for governmental funds but are included in bonds payable and capital lease obligation in the statement of net position. 1,361,250

- (7) Some long-term liabilities and deferred charges are not due and payable in the current period and therefore are not reported in the funds, including:

Notes payable	\$ (4,700,000)	
Capital lease obligation	(16,640,129)	
Bonds payable	(34,883,055)	
Accrued vacation	<u>(1,544,477)</u>	
		<u>(57,767,661)</u>

Total net position \$ 867,627,207

The accompanying notes are an integral part of the financial statements.



State of Hawai'i

Department of Hawaiian Home Lands

Statement of Revenues, Expenditures, and Changes in Fund Balances

Governmental Funds

for the year ended June 30, 2018

	Hawaiian General Fund	Hawaiian Home General Loan Fund	Hawaiian Home Lands Trust Fund	Hawaiian Home Operating Fund	Hawaiian Home Receipts Fund	Hawaiian Home Administration Account	Federal Grants	Hawaiian Home Trust Fund	Hawaiian Home Lands Bond Funds	Department of Hawaiian Home Lands Revenue Bond Special Fund	Other Funds	Total
Revenues												
State appropriations	\$ 17,944,384	-	\$ -	-	\$ -	\$ -	\$ -	-	\$ 34,450,000	\$ -	\$ -	\$ 52,394,384
General leases	-	-	-	-	-	14,635,551	-	-	-	-	-	14,635,551
Licenses and permits	-	-	-	-	-	3,512,814	-	-	-	-	-	3,512,814
Interest from loans and note receivable	-	-	-	35,016	4,737,527	-	377,907	-	-	-	-	5,150,450
Investment income	-	-	-	547,701	431,716	652,621	-	-	-	184,783	110,469	4,429,489
Intergovernmental revenues	-	-	2,502,199	-	-	-	17,325,922	-	-	4,987,220	-	22,315,496
Real property sold	-	-	2,354	-	-	-	-	-	-	-	-	187,900
Other	-	-	187,900	-	-	249,812	129,726	-	-	-	304,684	1,982,286
Total revenues	17,944,384	-	2,692,453	1,880,781	5,169,243	19,050,798	17,833,555	-	34,450,000	5,172,003	415,153	104,608,370
Expenditures												
Current:												
Administration and support services	6,593,161	-	-	1,053,422	-	2,176,518	2,449,308	-	1,418,000	-	271,280	13,961,689
Homestead services	3,053,857	2,242,782	123	1,200,279	-	135,352	284,390	-	-	-	93,000	7,009,783
Land development	1,751,964	-	1,219,060	4,422,705	-	127,262	85,581	-	-	-	-	7,606,572
Land management	2,299,689	-	94,759	99,054	-	1,844,401	130,198	-	-	-	-	4,468,101
Capital outlay	182,090	-	1,561,486	2,976,251	-	73,778	2,681,920	-	7,392,209	-	-	14,867,734
Debt service	-	-	-	-	-	-	-	-	-	1,271,250	-	1,271,250
Principal	-	-	-	-	-	-	-	-	-	715,697	-	715,697
Interest	-	-	-	-	-	-	-	-	-	308,189	-	308,189
Cost of issuance	-	-	-	-	-	-	-	-	-	4,049,115	-	4,049,115
Payment to refunding escrow	-	-	-	-	-	-	-	-	-	-	-	-
Total expenditures	13,880,761	2,242,782	2,875,428	9,751,711	-	4,357,311	5,631,397	-	8,810,209	6,344,251	364,280	54,258,130
Excess (deficiency) of revenues over (under) expenditures	4,063,623	(2,242,782)	(182,975)	(7,870,930)	5,169,243	14,693,487	12,202,158	-	25,639,791	(1,172,248)	50,873	50,350,240
Other financing sources (uses)												
Transfers in	-	4,400,000	-	21,501,890	-	1,627,443	360,638	-	-	3,238,019	2,501	31,130,491
Transfers out	(1,399,666)	-	-	(1,500,000)	(4,400,000)	(20,260,647)	(359,638)	-	(1,417)	(3,208,122)	-	(31,129,490)
Proceeds of long-term debt	-	-	-	-	-	15,125,000	-	-	-	30,940,000	-	46,065,000
Premium on long-term debt	-	-	-	-	-	2,613,724	-	-	-	5,347,044	-	7,960,768
Payment to refunding escrow	-	-	-	-	-	-	-	-	-	(35,960,670)	-	(35,960,670)
Refunding of certificates of participation	-	-	-	-	-	(18,475,000)	-	-	-	-	-	(18,475,000)
Total other financing sources (uses)	(1,399,666)	4,400,000	-	20,001,890	(4,400,000)	(19,369,480)	1,000	-	(1,417)	356,271	2,501	(408,901)
Excess (deficiency) of revenues over and other financing sources	2,663,957	2,157,218	(182,975)	12,130,960	769,243	(4,675,993)	12,203,158	-	25,638,374	(815,977)	53,374	49,941,339
over (under) expenditures and other financing uses	(1,600,218)	-	-	-	-	-	-	-	(183,499)	-	-	(1,783,717)
Lapsed appropriations												
Net change in fund balances	1,063,739	2,157,218	(182,975)	12,130,960	769,243	(4,675,993)	12,203,158	-	25,454,875	(815,977)	53,374	48,157,622
Fund balances at July 1, 2017	3,358,529	66,286,324	154,194,916	35,169,049	2,464,285	46,161,174	18,026,764	12,199,530	9,794,993	13,229,372	11,313,122	372,198,058
Fund balances at June 30, 2018	\$ 4,422,268	\$ 68,443,542	\$ 154,011,941	\$ 47,300,009	\$ 3,233,528	\$ 41,485,181	\$ 30,229,922	\$ 12,199,530	\$ 35,249,868	\$ 12,413,395	\$ 11,366,496	\$ 420,355,680

The accompanying notes are an integral part of the financial statements.



State of Hawai‘i
Department of Hawaiian Home Lands
Reconciliation of the Governmental Funds Statement of Revenues,
Expenditures, and Changes in Fund Balances to the Statement of Activities
for the year ended June 30, 2018

Change in fund balances - governmental funds \$ 48,157,622

Amounts reported for governmental activities in the statement of activities are different because:

- (1) Capital outlays are reported as expenditures in governmental funds; however, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these transactions are:

Capital outlay	\$ 11,049,195	
Depreciation expense	(24,191,887)	
Excess of depreciation expense over capital outlay		(13,142,692)

- (2) Repayment of notes payable is reported as an expenditure in governmental funds, but the payment reduces notes payable in the statement of net position. 1,700,000

- (3) The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, is reported on the statement of activities. Also, governmental funds report the effect of premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities:

Net increase in prepaid bond insurance	\$ 81,357	
Net increase in deferred loss on refunding	3,535,495	
Net decrease in capital lease obligation	1,834,871	
Net decrease in bonds payable	1,378,119	
		6,829,842

- (4) The governmental funds report revenues only if they are collected within 60 days after the end of the year. The statement of activities reports revenues when earned, regardless of when it is collected. This measurement difference causes timing of revenue recognition differences for interest income. (386,754)

- (5) The net increase in accrued vacation is reported in the statement of activities and does not require the use of current financial resources and therefore is not reported as expenditures in governmental funds. (69,445)

- (6) Long-term debt payment accruals are included as an expenditure for governmental funds but are included in bonds payable and capital lease obligation in the statement of net position. 71,249

Change in net position \$ 43,159,822

The accompanying notes are an integral part of the financial statements.



State of Hawai‘i
Department of Hawaiian Home Lands
Statement of Revenues and Expenditures – Budget and Actual (Budgetary Basis)
General Fund (Unaudited)
for the year ended June 30, 2018

	<u>Budgeted Amounts</u> <u>Original and Final</u>	<u>Actual</u> <u>(Budgetary Basis)</u>	<u>Variance with</u> <u>Final Budget -</u> <u>Favorable</u> <u>(Unfavorable)</u>
State appropriations	\$ 25,120,731	\$ 17,944,384	\$ (7,176,347)
Expenditures:			
Administration and support services	13,684,234	7,968,103	5,716,131
Homestead services	5,572,172	3,120,656	2,451,516
Land development	3,456,352	1,974,436	1,481,916
Land management	<u>2,407,973</u>	<u>1,906,311</u>	<u>501,662</u>
Total expenditures	<u>25,120,731</u>	<u>14,969,506</u>	<u>10,151,225</u>
Excess of appropriations over expenditures	<u>\$ -</u>	<u>\$ 2,974,878</u>	<u>\$ 2,974,878</u>

The accompanying notes are an integral part of the financial statements.



State of Hawai‘i
Department of Hawaiian Home Lands
Statement of Revenues and Expenditures – Budget and Actual (Budgetary Basis)
Hawaiian Home Administration Account (Unaudited)
for the year ended June 30, 2018

	<u>Budgeted Amounts Original and Final</u>	<u>Actual (Budgetary Basis)</u>	<u>Variance with Final Budget - Favorable (Unfavorable)</u>
Revenues	\$ 4,824,709	\$ 19,050,798	\$ 14,226,089
Expenditures:			
Administration and support services	1,662,405	4,739,066	(3,076,661)
Homestead services	516,350	189,594	326,756
Land development	359,000	19,326	339,674
Land management	<u>2,286,954</u>	<u>2,205,772</u>	<u>81,182</u>
Total expenditures	<u>4,824,709</u>	<u>7,153,758</u>	<u>(2,329,049)</u>
Excess of revenues over expenditures	<u>\$ -</u>	<u>\$ 11,897,040</u>	<u>\$ 11,897,040</u>

The accompanying notes are an integral part of the financial statements.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity

The Department of Hawaiian Home Lands, State of Hawai‘i (the “Department”) is headed by the Hawaiian Homes Commission (HHC). The Department was established by Section 24 of Act 1 (the Hawaii State Government Reorganization Act of 1959), Second Special Session Laws of Hawaii 1959, and is responsible for the administration of the Hawaiian Homes Commission Act of 1920 enacted by the United States Congress. The Hawaiian Homes Commission Act (HHCA) sets aside certain public lands as Hawaiian home lands to be utilized in the rehabilitation of native Hawaiians. The financial statements include the public trusts controlled by the HHC.

The Department is part of the executive branch of the State of Hawai‘i (the State). The Department’s financial statements are intended to present the financial position and the changes in financial position, of only that portion of the governmental activities, each major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the Department. The State Comptroller maintains the central accounts for all State funds and publishes financial statements for the State annually which includes the Department’s assets, liabilities, net position, and financial activities.

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

Department-Wide Financial Statements

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

The statement of activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges to customers who purchase, use or directly benefit from goods or services provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function.

Appropriations and other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues.

Net position is restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

Governmental Fund Financial Statements

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Department considers revenues to be available if they are collected within 60 days of the current fiscal year end. Principal revenue sources considered susceptible to accrual include lease payments, sales, interest on loans and investments, and interest receivable. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences, claims, and judgments are recorded only when payment is due.

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

As of June 30, 2018, fund balances of the governmental funds are classified as follows:

- **Nonspendable** – Amounts that cannot be spent because they are either in nonspendable form or they are legally or contractually required to be maintained intact.
- **Restricted** – Amounts that are restricted for specific purposes due to constitutional provisions or enabling legislation or constraints that are externally imposed by creditors, grantors, contributors, or laws or regulations of other governments.
- **Committed** – Amounts that can be used only for specific purposes determined by a formal action of the State Legislature. The State Legislature is the highest level of decision-making authority for the Department. Commitments may be established, modified or rescinded only through formal acts by the State Legislature.
- **Assigned** – Amounts that do not meet the criteria to be classified as restricted or committed but that are intended to be used for specific purposes. Under the Department’s adopted policy, only the HHC may assign amounts for specific purposes.
- **Unassigned** – All other spendable amounts.

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



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

Fund Accounting

The accounts of the Department are organized on the basis of funds, each of which is considered a separate accounting entity. The Department uses fund accounting to report on its financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.

The financial activities of the Department that are reported in the accompanying governmental fund financial statements have been classified into the following major governmental funds:

General Fund

The General Fund is used to account for all financial resources except those required to be accounted for in another fund. The annual operating budget as authorized by the State Legislature provides the basic framework within which the resources and obligations of the General Fund are accounted for.

Special Revenue Funds

Special revenue funds are used to account for proceeds of specific revenue sources that are restricted to expenditures for specified purposes. Revenues are primarily from general leases, licenses and permits granted for commercial, residential, agricultural and pastoral uses, and interest and investment income. The Department’s major special revenue funds are as follows:

- **Hawaiian Home General Loan Fund** – The Hawaiian Home General Loan Fund is used to account for Department loans made to native Hawaiian homesteaders.
- **Hawaiian Home Lands Trust Fund** – The Hawaiian Home Lands Trust Fund accounts for funds from the State to be expended by the Department, as provided by law upon approval by the Commission and used for capital improvements and other purposes undertaken in furtherance of the Hawaiian Homes Commission Act of 1920.
- **Hawaiian Home Operating Fund** – The Hawaiian Home Operating Fund is used to account for operations of the Department and is funded by monies transferred from the Hawaiian Home Receipts Fund.
- **Hawaiian Home Receipts Fund** – The Hawaiian Home Receipts Fund is used to account for receipts of investment interest and loan interest payments from the Department loans to homesteaders.
- **Hawaiian Home Administration Account** – The Hawaiian Home Administration Account is used to account for commercial general leases, revocable permits and licenses of “available” lands as defined under the HHCA. Lease revenues are used to fund operations of the Department.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

Fund Accounting (continued)

- **Federal Grants** – The Federal Grants fund is used to account for grants the Department has with the Federal Government.
- **Hawaiian Home Trust Fund** – The Hawaiian Home Trust Fund is used to account for the loan principal and interest payments the Department collects on assumed loans from the Department of Housing and Urban Development (HUD) as part of the mortgage loan insurance agreement. The amounts maintained in this fund provide for payment of any mortgage insurance claims and expenditures incurred by HUD in connection with the lessee borrowings.
- **Hawaiian Home Lands Bond Funds** – The Hawaiian Home Lands Bond Funds are authorized and appropriated by the State Legislature for construction projects or grant-in-aid funds for projects or grants which benefit the trust’s beneficiaries or community organizations.
- **Department of Hawaiian Home Lands Revenue Bond Special Fund** – The Department of Hawaiian Home Lands Revenue Bond Special Fund accounts for proceeds and debt service payments on revenue bonds issued by the Department.

Appropriations

An appropriation is an authorization granted by the State Legislature permitting a State agency, within established fiscal and budgetary controls, to incur obligations and to make expenditures. Appropriations are allotted quarterly. The allotted appropriations lapse if not expended by or encumbered at the end of the fiscal year, except for allotted appropriations related to capital projects.

Encumbrances

Encumbrance accounting, under which purchase orders, contracts, and other commitments for the expenditure of monies are recorded in order to reserve that portion of the applicable appropriation, is employed as an extension of formal budgetary integration in the governmental fund types.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

Encumbrances (continued)

Encumbrances at June 30, 2018 for the Department’s governmental funds were as follows:

	Contracts	Claims
General Fund	\$ 3,573,000	\$ 1,854,000
Land Trust Fund	7,385,000	664,000
Operating Fund	4,952,000	3,153,000
Administration Account	991,000	1,816,000
Federal Grants	6,061,000	2,056,000
Bond Fund	20,127,000	-
Revenue Bond Special Fund	-	243,000
Other Funds	546,000	83,000
Total	<u>\$ 43,635,000</u>	<u>\$ 9,869,000</u>

Cash in State Treasury

Cash in State Treasury reported in the statement of net position and the governmental funds balance sheet represents the Department’s equity in cash and investments held by the State Treasury (see Note C).

The State Director of Finance is responsible for the safekeeping of all cash in the State Treasury in accordance with State laws. Currently, separate accounts are not maintained in the State Treasury for the Department’s general operating and capital appropriations. Although these appropriations are available to the Department to expend, custody and ownership of the funds remains with the State. Unspent general and capital appropriations that continue to be available to the Department for expenditure at the end of the fiscal year are reported as cash in State Treasury in the accompanying fund and department-wide financial statements.

Restricted Cash and Investments

Cash held with an escrow agent and invested until the repayment of certain obligations have been classified as restricted assets.

The Department invests funds held by the Bank of New York Mellon related to the capital lease obligation and revenue bonds in U.S. Treasury money market funds. The investments are carried at fair value and are valued at the last reported sale price on the last business day of the year or at the last bid price if no sale was reported on that date. Unrealized gains are considered investment income and the funds are restricted to funding future capital lease or revenue bond payments.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair Value Measurements

For financial assets reported at fair value, the Department defines fair value as the price that would be received to sell an asset in the principal or most advantageous market in an orderly transaction between market participants. The Department measures fair value using assumptions developed based on market data obtained from independent external sources and the reporting entity’s own assumptions. The hierarchy is broken down into levels based on the reliability of the inputs as follows:

- **Level 1** – Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- **Level 2** – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- **Level 3** – Unobservable inputs for an asset or liability reflecting management’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.

Inventory of Homes for Sale and Development

Inventory of homes for sale and development are stated at the lower of cost or estimated net realizable value and includes the costs of land development and home construction, capitalized interest, real estate taxes, and direct overhead costs incurred during development and home construction.

Intrafund and Interfund Transactions

Transfers of financial resources between activities and appropriations included within the same fund are eliminated. Transfers of revenues from funds authorized to receive them to funds authorized to expend them have been recorded as operating transfers in the financial statements. Interfund balances of \$1,038,700 and \$4,047,123 represent loans and construction, respectively, temporarily funded with cash balances from other funds.

All interfund transfers are reflected in the governmental fund financial statements but are eliminated in the department-wide financial statements.

Capital Assets

Capital assets, which include land, buildings, improvements, equipment, and infrastructure assets, are reported in the department-wide financial statements. The capitalization thresholds are \$5,000 for equipment and \$100,000 for infrastructure, and buildings and improvements with estimated useful lives of greater than one year. Maintenance and repairs are charged to operations when incurred. Purchased and constructed capital assets are valued at historical cost or estimated historical cost. Donated fixed assets are recorded at their fair market value at the date of donation.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

Capital Assets (continued)

Capital assets are depreciated on the straight-line method over the assets' estimated useful life as follows:

Vehicles	5 years
Machinery and equipment	5 - 7 years
Buildings and improvements	15 - 40 years
Infrastructure	15 - 30 years

The Department also has land in various parts of the State, some of which were transferred to it at no cost or at nominal cost.

Deferred Outflows of Resources

Deferred outflows of resources represent a consumption of net position that applies to a future period. The Department defers recognition of the loss on debt refunding related to issuance of its revenue bonds and amortizes these costs over the life of the bonds using the straight-line method.

Temporary Deposits Payable

As part of the mortgage loan insurance agreement, the Department assumes delinquent mortgage loans from HUD. The temporary deposits payable balance represents the amount of loans assumed, less any payments made to HUD, for the payment of future mortgage insurance claims.

Compensated Absences

It is the State's policy to permit employees to accumulate earned but unused vacation and sick leave benefits. There is no liability for unpaid accumulated sick leave since sick leave is not convertible to pay upon termination of employment. Accumulated sick leave as of June 30, 2018 was approximately \$5,373,000. All vacation pay is accrued when incurred in the department-wide financial statements. A liability for these amounts is reported in the governmental fund financial statements only if they have matured, for example, as a result of employee resignations and retirements.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

Lease Rents and Interest Income

The Department’s governmental fund financial statement recognizes lease rent and mortgage interest of its governmental funds as revenues when they are measurable and available. The available criterion is satisfied when revenues are collectible during the period or soon enough thereafter to pay liabilities of the current period. Amounts not collected within 60 days after the end of the year approximated \$6,386,000 as of June 30, 2018, and are recorded as deferred revenue in the governmental funds balance sheet. The departmental financial statements present lease rents and mortgage interest under the accrual method of accounting.

Use of Estimates

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

New Accounting Pronouncements

GASB Statement No. 75

During fiscal year 2018, the Department implemented GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Statement No. 75 establishes standards of accounting and financial reporting for defined benefit Other Postemployment Benefits (OPEB) and defined contribution OPEB that are provided to the employees of state and local governmental employers through OPEB plans that are administered through trusts or equivalent arrangements in which:

- Contributions from employers and nonemployer contributing entities to the OPEB plan and earnings on those contributions are irrevocable.
- OPEB plan assets are dedicated to providing OPEB to plan members in accordance with the benefit terms.
- OPEB plan assets are legally protected from the creditors of employers, nonemployer contributing entities, and the OPEB plan administrator. If the plan is a defined benefit OPEB plan, plan assets also are legally protected from creditors of the plan members.

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

This Statement did not have a material effect on the Department’s financial statements. Refer to Note L for more information regarding the State’s OPEB.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

New Accounting Pronouncements (continued)

GASB Statement No. 81

During fiscal year 2018, the Department implemented GASB Statement No. 81, *Irrevocable Split-Interest Agreements*. The objective of this Statement is to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. This Statement did not have a material effect on the Department’s financial statements.

GASB Statement No. 83

The GASB issued Statement No. 83, *Certain Asset Retirement Obligations*. The objective of this Statement is to provide financial statement users with information about asset retirement obligations that were not previously 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 Department has not yet determined the effect this Statement will have on its financial statements.

GASB Statement No. 84

The GASB issued Statement No. 84, *Fiduciary Activities*. The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018. The Department has not yet determined the effect this Statement will have on its financial statements.

GASB Statement No. 85

During fiscal year 2018, the State implemented GASB Statement No. 85, *Omnibus 2017*. The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement did not have a material effect on the Department’s financial statements.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

New Accounting Pronouncements (continued)

GASB Statement No. 86

During fiscal year 2018, the Department implemented GASB Statement No. 86, *Certain Debt Extinguishment Issues*. The primary objective of this Statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources, which are resources other than the proceeds of refunding debt, are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance. This Statement did not have a material effect on the Department’s financial statements.

GASB Statement No. 87

The GASB issued Statement No. 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. The Statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows 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 Department has not yet determined the effect 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 Department has not yet determined the effect this Statement will have on its financial statements.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE A - SIGNIFICANT ACCOUNTING POLICIES (continued)

New Accounting Pronouncements (continued)

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 Department has not yet determined the effect this Statement will have on its financial statements.

GASB Statement No. 90

The GASB issued Statement No. 90, *Majority Equity Interests – an amendment of GASB Statements No. 14 and No. 61*. The primary objectives of this Statement are to improve the consistency and comparability of reporting a government’s majority equity interest in a legally separate organization and improve the relevance of financial statement information for certain component units. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018. The Department has not yet determined the effect this Statement will have on its financial statements.

NOTE B - BUDGETING AND BUDGETARY CONTROL

The Department’s annual budget is prepared on the cash basis utilizing encumbrance accounting. Revenue estimates are provided to the State Legislature at the time of budget consideration and are revised and updated throughout the fiscal year. Amounts reflected by the Department as budgeted revenues are those estimates as compiled by the State Director of Finance. Budgeted expenditures for the Department’s General Fund and the Hawaiian Homes Administration Account, a special revenue fund, are provided to the Department of Budget and Finance, State of Hawai‘i, for accumulation with budgeted amounts of the other State agencies and included in the Governor’s executive budget that is subject to legislative approval. In addition, the budget for all expenditures of the Department’s funds is also presented annually to the HHC for approval. Budgetary information for funds other than the General Fund and Hawaiian Homes Administration Account are not subject to legislative approval, therefore, budgetary reconciliations for those funds are not included in the financial statements.

To the extent not expended or encumbered, General Fund appropriations generally lapse at the end of the fiscal year for which the appropriations were made. The State Legislature specifies the lapse date and any other particular conditions which may terminate the authorization for other appropriations.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE B - BUDGETING AND BUDGETARY CONTROL (continued)

For purposes of budgeting, the Department’s budgetary fund structure and accounting principles differ from those utilized to present the financial statements in conformity with GAAP.

Since the budgetary basis differs from GAAP, budget and actual amounts in the statements of revenues and expenditures – budget and actual – general fund and the Hawaiian Home Administration Account, are presented on the budgetary basis. A reconciliation of the General Fund and the Hawaiian Home Administration Account revenues in excess of expenditures on a budgetary basis for the year ended June 30, 2018, to revenues in excess of expenditures presented in conformity with GAAP is set forth below.

Under Hawai‘i Revised Statutes (HRS) Section 78-13, staff salaries and wages amounting to approximately \$655,000 in the General Fund, for the period from June 16, 2018 through June 30, 2018, are to be funded with monies budgeted for fiscal year 2019. Accordingly, these amounts are excluded from the statements of revenues and expenditures – budget and actual of the General Fund, but are included in the departmental and governmental fund financial statements in accordance with GAAP.

Salaries and wages amounting to approximately \$568,000 in the General Fund, for the period from June 16, 2017 to June 30, 2017, were funded with monies budgeted for fiscal year 2018. Accordingly, these amounts are included in the statements of revenues and expenditures – budget and actual of the General Fund, for the year ended June 30, 2018.

The following schedule reconciles the budgetary amounts of the General Fund and the Hawaiian Home Administration Account to the amounts presented in accordance with GAAP:

	General Fund	Hawaiian Home Administration Account
Excess of revenues over expenditures - actual on budgetary basis	\$ 2,974,878	\$ 11,897,040
Current year's appropriations encumbered at June 30, 2018	3,772,399	1,816,345
Current year's encumbrances included in vouchers payable	(335,721)	(103,354)
Expenditures for liquidation of prior year's encumbrances	(2,260,923)	(1,205,561)
Fiscal 2017 expenditures funded by fiscal 2018 budget	568,088	-
Fiscal 2018 expenditures funded by fiscal 2019 budget under Section 78-13 HRS	(655,098)	-
Excess of revenues over expenditures - GAAP basis	<u>\$ 4,063,623</u>	<u>\$ 12,404,470</u>



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE C - CASH IN STATE TREASURY

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

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

GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, requires disclosures over common deposit and investment risks related to credit risk, interest rate risk, and foreign currency risk. Investments can be categorized by type, maturity, and custodian to determine the level of interest rate, credit and custodial risk assumed by the Department. However, as these funds are held in the State cash pool, the Department does not manage these investments and the types of investments and related interest rate, credit and custodial risks are not determinable at the Department level. The risk disclosures of the State’s cash pool are included in the State’s Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2018. The State’s CAFR can be found at the Department of Accounting and General Services’ (DAGS) website: <http://ags.hawaii.gov/accounting/annual-financial-reports/>.

NOTE D - LOANS RECEIVABLE

Loans receivable consist of approximately 1,375 loans made to native Hawaiian lessees for the purposes specified in the HHCA. Loans are for a maximum amount of approximately \$354,000 and for a maximum term of 30 years. Loan payments expected to be collected within the next fiscal year approximates \$3,007,000. Interest rates on outstanding loans range up to 10%. The Department’s loan portfolio consists of loans that the Department has originated and that generally are collateralized by improvements on the leased properties located in the State. Loan commitments as of June 30, 2018 were approximately \$401,000. The Department has provided an allowance for loan losses of approximately \$16,106,000 as of June 30, 2018. The allowance for loan losses is a valuation reserve, which has been provided through charges to operations in the department-wide financial statements. The reserve is based on management’s assessment of loan balances deemed uncollectible as of June 30, 2018.

NOTE E – INVENTORY OF HOMES PURCHASED FROM FORMER LESSEES

Through June 30, 2018, the Department constructed and sold a total of 583 homes to native Hawaiians in various locations throughout Hawai‘i.

Under certain circumstances, the Department purchases homes from former lessees due to voluntary and involuntary cancellations of land leases. The homes are subsequently resold to



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE E – INVENTORY OF HOMES PURCHASED FROM FORMER LESSEES (continued)

qualified lessees. As of June 30, 2018, the Department purchased homes from former lessees with book value aggregating approximately \$3,522,000.

NOTE F – RESTRICTED CASH AND SHORT-TERM INVESTMENTS HELD OUTSIDE STATE TREASURY

Restricted investments held outside of the State Treasury consist of money market funds held at a financial institution outside of the State of Hawai‘i. At June 30, 2018, the fair value of these investments was approximately \$2,442,000 and was determined using Level 1 inputs.

NOTE G - CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2018 was as follows:

	Beginning Balance July 1, 2017	Additions	Disposals/ Transfers	Ending Balance June 30, 2018
Capital assets not being depreciated -				
Land	\$ 41,824,231	\$ -	\$ -	\$ 41,824,231
Land improvements	33,406,582	-	-	33,406,582
Works of art, historical treasures	29,426	-	-	29,426
Construction in progress	6,412,421	10,984,092	(2,041,726)	15,354,787
Total capital assets, not being depreciated	81,672,660	10,984,092	(2,041,726)	90,615,026
Capital assets, being depreciated -				
Buildings and improvements	29,188,835	-	-	29,188,835
Infrastructure	691,820,344	-	2,041,726	693,862,070
Furniture and equipment	5,623,430	20,379	-	5,643,809
Motor vehicles	1,340,497	44,724	-	1,385,221
Total capital assets, being depreciated	727,973,106	65,103	2,041,726	730,079,935
Less: accumulated depreciation for -				
Buildings and improvements	(11,947,662)	(929,843)	-	(12,877,505)
Infrastructure	(284,053,090)	(23,079,709)	-	(307,132,799)
Furniture and equipment	(5,329,350)	(78,446)	-	(5,407,796)
Motor vehicles	(1,030,572)	(103,889)	-	(1,134,461)
Total accumulated depreciation	(302,360,674)	(24,191,887)	-	(326,552,561)
Total capital assets, being depreciated, net	425,612,432	(24,126,784)	2,041,726	403,527,374
Capital assets, net	\$ 507,285,092	\$ (13,142,692)	\$ -	\$ 494,142,400



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE G - CAPITAL ASSETS (continued)

Depreciation expense for the year ended June 30, 2018 was charged to functions of the Department as follows:

Administration and support services	\$ 1,077,779
Homestead services	23,079,707
Land development	5,784
Land management	28,617
Total depreciation	<u>\$ 24,191,887</u>

NOTE H - LONG-TERM OBLIGATIONS

For the year ended June 30, 2018, changes in long-term obligations were as follows:

	Notes Payable	Capital Lease Obligation	Bonds Payable, Net	Accrued Vacation
Balances at July 1, 2017	\$ 6,400,000	\$ 18,475,000	\$ 36,261,174	\$ 1,475,032
Increase	-	17,738,724	36,287,044	633,589
Decrease	(1,700,000)	(19,573,595)	(37,665,163)	(564,144)
Balances at June 30, 2018	<u>\$ 4,700,000</u>	<u>\$ 16,640,129</u>	<u>\$ 34,883,055</u>	<u>\$ 1,544,477</u>

Obligations for accrued vacation are generally liquidated by the General Fund, the Hawaiian Home Operating Fund, and the Hawaiian Home Administration Account.

NOTE I - NOTES PAYABLE

In December 2004, the Department entered into a transfer agreement with the Hawaii Housing Finance and Development Corporation (HHFDC), State of Hawai‘i, in connection with the acquisition of approximately 1,800 acres of land consisting of four properties on three islands by the Department. A portion of the land is partially developed and is intended to be utilized for 3,500 homes for native Hawaiians.

As part of the transfer agreement, the Department must pay \$2.2 million a year for 15 years, for a total of \$33 million, in the form of a note, to reimburse the HHFDC, for infrastructure costs at three of the properties. This note is noninterest bearing. At June 30, 2018, the Department owed \$4,700,000 to HHFDC. The note will be repaid with monies in the Department’s Hawaiian Home Land Trust Fund. In July 2013, the Department executed an amendment that reduced the annual payments to \$1.7 million through 2020 and the final payment totaling \$1.3 million is due in 2021.



State of Hawai‘i
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Notes to Financial Statements
June 30, 2018

NOTE I - NOTES PAYABLE (continued)

The annual payment requirements of the notes are as follows:

Year ending June 30,	Purchase Note Payable
2019	\$ 1,700,000
2020	1,700,000
2021	1,300,000
	<u>\$ 4,700,000</u>

NOTE J - CAPITAL LEASE OBLIGATION

In December 2006, the Department entered into a 25-year facility lease agreement with Wells Fargo Bank, National Association, to lease an office facility which was constructed and completed in April 2008.

In August 2017, Wells Fargo Bank transferred the lease by assignment to The Bank of New York Mellon Trust Company, National Association (BNY Mellon). The Department and BNY Mellon amended the lease payment schedule resulting in present value savings to the Department of approximately \$4,061,000. The Department is required to make semi-annual interest payments and annual principal payments through 2021. Interest on the outstanding balance accrues at various rates between 2% and 5%. Upon expiration of the lease, the title of the facility will be transferred from the lessor to the Department. The following is a schedule of future minimum lease payments related to this agreement:

Year ending June 30,	
2019	\$ 1,392,000
2020	1,399,000
2021	1,396,000
2022	1,398,000
2023	1,399,000
Thereafter	<u>12,571,000</u>
Total minimum lease payments	19,555,000
Less: Amount representing interest	(5,380,000)
Unamortized premium on certificates of participation	<u>2,465,000</u>
Present value of minimum lease payments	16,640,000
Less: Current portion	<u>(750,000)</u>
Long-term portion	<u>\$ 15,890,000</u>



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE J - CAPITAL LEASE OBLIGATION (continued)

The cost basis and accumulated depreciation of the leased assets at June 30, 2018 was as follows:

Cost	\$ 25,513,266
Less: Accumulated depreciation	<u>(11,581,512)</u>
	<u>\$ 13,931,754</u>

NOTE K - BONDS PAYABLE

In August 2017, the Department issued \$30,940,000 in refunding bonds to redeem on April 1, 2019 all outstanding Revenue Bonds Series 2009 maturing on or after May 1, 2019 and pay principal and interest on the outstanding Revenue Bonds Series 2009 until that redemption date.

Net proceeds of \$35,960,670 (after payment of underwriter fees and other issuance costs) and existing assets of \$4,049,115 were deposited in an irrevocable trust with an escrow agent. The funds were then used to purchase obligations that are unconditionally guaranteed by the U.S. government to provide for all future debt service payments and for redemption of the Revenue Bonds Series 2009. The refunding provided present value savings of approximately \$12,422,000.

The Series 2017 Revenue Bonds bear interest at 3% to 5% per annum and mature in annual increments on April 1, 2018 through 2032. Series 2017 Revenue Bonds maturing on or after April 1, 2028 may be redeemed by the Department on or after April 1, 2027. The revenue bonds are payable from and secured by the Department’s revenues generated from general leases and available lands.

The Department considers these transactions to be an in-substance defeasance of the Revenue Bonds Series 2009. As a result, neither the liability for those bonds nor the escrowed assets are reported in the financial statements. Defeased debt of \$35,750,000 was outstanding at June 30, 2018. The difference between the reacquisition price and the net carrying amount of the Revenue Bonds Series 2009 is reported as a deferred outflow of resources on the statement of net position and is amortized over the life of the Series 2017 Revenue Bonds.

Details of the Department’s revenue bonds as of June 30, 2018 are as follows:

\$30,940,000 revenue bonds dated August 25, 2017;	
due in annual principal installments of \$1,100,000	
to \$2,770,000 from April 1, 2018 through April 1,	
2032; interest at 3% to 5% payable semi-annually.	\$ 29,840,000
Unamortized premium on revenue bonds	<u>5,043,055</u>
	<u>\$ 34,883,055</u>



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE K - BONDS PAYABLE (continued)

The annual requirements of the revenue bonds are as follows:

Year ending June 30,	Interest	Principal	Total
2019	\$ 1,435,000	\$ 1,575,000	\$ 3,010,000
2020	1,372,000	1,655,000	3,027,000
2021	1,306,000	1,695,000	3,001,000
2022	1,221,000	1,790,000	3,011,000
2023	1,131,000	1,875,000	3,006,000
2024-2028	4,645,000	13,405,000	18,050,000
2029-2032	708,000	7,845,000	8,553,000
	\$ 11,818,000	\$ 29,840,000	\$ 41,658,000

NOTE L - EMPLOYEE BENEFIT PLANS

Substantially all employees of the Department participate in the State’s various employee benefit plans, including the Employees’ Retirement System (ERS) of the State of Hawai‘i, postemployment healthcare and life insurance plan, and a deferred compensation plan. For more information on the State’s benefit plans, refer to the State of Hawai‘i and ERS’ CAFR. The State’s CAFR can be found at the DAGS website: <http://ags.hawaii.gov/accounting/annual-financial-reports/>. The ERS CAFR can be found at the ERS website: <http://ers.ehawaii.gov/resources/financials>.

Employees’ Retirement System

The ERS is a cost-sharing, multiple-employer defined benefit public employee retirement plan. The ERS provides retirement benefits as well as death and disability benefits. All contributions, benefits, and eligibility requirements are established by HRS Chapter 88 and can be amended by legislative action.

- **State Policy** – The actuarial valuation of the ERS does not provide pension information by department or agency. Accordingly, the State’s policy on the accounting and reporting for pension benefits is to allocate a portion of the net pension liability, pension expense, and deferred inflows and outflows of resources required under GASB Statement No. 68 only to component units and proprietary funds that are reported separately in stand-alone departmental financial statements or in the State’s CAFR. The basis for the allocation is the number of covered employees for each component unit and proprietary fund for pension benefits.
- **Contributions** – Contributions are established 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. Contributions by the Department to the pension plan were approximately \$1,143,000 for the year ended June 30, 2018.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE L - EMPLOYEE BENEFIT PLANS (continued)

Employees’ Retirement System (continued)

- **Required Supplementary Information and Disclosures** – The State’s CAFR includes the required footnote disclosures and supplementary information on the State’s pension plan.

Deferred Compensation Plan

The State offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all eligible State employees, permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or an unforeseeable emergency.

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

Postemployment Healthcare and Life Insurance Benefits

The State contributes to the Hawai‘i Employer-Union Health Benefits Trust Fund (EUTF), an agent multiple-employer defined benefit plan. The EUTF was established to provide a single delivery system of health benefits for state and county workers, retirees, and their dependents. The eligibility requirements for retiree health benefits are based on date of hire.

- **State Policy** – The actuarial valuation of the EUTF does not provide OPEB information by department or agency. Accordingly, the State’s policy on the accounting and reporting for OPEB is to only allocate a portion of the State’s Annual Required Contribution (ARC), interest, and any adjustment to the ARC, to component units and proprietary funds that are reported separately in stand-alone departmental financial statements or in the State’s CAFR. The basis for the allocation is the number of covered employees for each component unit and proprietary fund.
- **Contributions** – Contributions are financed on a pay-as-you-go basis. Contributions by the Department to the EUTF for the years ended June 30, 2018, 2017 and 2016 were approximately \$1,574,000, \$1,252,000 and \$1,138,000, respectively.
- **Required Supplementary Information and Disclosures** – The State’s CAFR includes the required footnote disclosures and supplementary information on the State’s OPEB plan.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE M - GENERAL LEASES AND LICENSES

The Department’s general leasing operations (Section 204 of Hawaiian Homes Commission Act of 1920, as amended) consist principally of the leasing of its Hawaiian home lands. The general leases have varying terms extending through July 2084.

The future minimum lease income from general leases as of June 30, 2018 is as follows:

<u>Year ending June 30,</u>	
2019	\$ 15,914,000
2020	16,000,000
2021	16,651,000
2022	16,922,000
2023	15,414,000
2024 - 2028	75,390,000
2029 - 2033	74,971,000
2034 - 2038	70,215,000
2039 - 2043	69,613,000
2044 - 2048	64,025,000
2049 - 2053	64,791,000
2054 - 2058	62,839,000
2059 - 2063	58,013,000
2064 - 2068	56,853,000
2069 - 2073	43,813,000
2074 - 2078	40,439,000
2079 - 2083	15,711,000
2084	1,547,000
	<u>\$ 779,121,000</u>

NOTE N - COMMITMENTS AND CONTINGENCIES

Litigation

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

For purposes of securing information about the Hawaiian Home Lands Trust Individual Claims discussed as a separate note in prior audits of the Department, please see the discussion about Individual Claims and the lawsuits relating to them, including the claims against the State and the Department in *Kalima v. State of Hawai‘i*, Civil No. 99-4771-12, in the State’s CAFR on the DAGS website.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE N - COMMITMENTS AND CONTINGENCIES (continued)

Insurance

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

Guaranteed and Insured Loans

As of June 30, 2018, the Department was contingently liable for approximately \$33,996,000 in loans originated primarily by the U.S. Department of Agriculture Rural Development for which the Department has guaranteed repayment. Approximately \$5,786,000 of these loans have been reported delinquent as of June 30, 2018.

The Department is also a party to a mortgage loan insurance agreement with the HUD. The agreement provides that HUD will perform underwriting processing for the insurance program and will administer an insurance fund for mortgages originated and held by HUD-approved lenders. The Department will maintain and provide the necessary and proper funds for payment of any mortgage insurance claims and expenditures incurred by HUD in connection with the lessee borrowers. The Department has reserved cash of approximately \$12,200,000 in the trust fund and has deposited \$150,000 with HUD. As of June 30, 2018, loans outstanding totaled approximately \$431,537,000 under this agreement, of which approximately \$23,589,000 has been reported as delinquent.

The Department is also a party to a Native Hawaiian Home Loan Guarantee Program (HUD Section 184) agreement with HUD. The agreement provides that HUD will guarantee certain loans in which homestead leases issued by the Department pursuant to the Hawaiian Homes Commission Act is used as collateral for the loan. As of June 30, 2018, loans outstanding totaled approximately \$102,002,000 under this agreement, of which approximately \$3,918,000 has been reported as delinquent.

As of June 30, 2018, the Department was also contingently liable for approximately \$4,304,000 in loans originated by financial institutions and other lenders for which it had guaranteed repayment. Approximately \$1,604,000 of these loans has been reported delinquent as of June 30, 2018.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to Financial Statements
June 30, 2018

NOTE N - COMMITMENTS AND CONTINGENCIES (continued)

Guaranteed and Insured Loans (continued)

As of June 30, 2018, the Department paid approximately \$7,785,000 for delinquent mortgage loan payments of lessees. These payments are carried as loans receivable from lessees and bear similar terms as stipulated in the lessees' mortgage notes with the lenders.

The Department has certain loans for which the collateral for the loans is not covered by casualty insurance. The number of such loans was not known as of June 30, 2018.

Other

In December 2008, the Department entered into a collaborative financing arrangement with the Office of Hawaiian Affairs, State of Hawai‘i (OHA) in which OHA will provide funds for the Department's use in the planning, design, and construction of infrastructure for homesteads for native Hawaiians on properties owned and controlled by the Department. Under the agreement, OHA will pay the Department on an annual basis the lesser of \$3,000,000 or the debt service of the revenue bonds issued by the Department in 2009. As of June 30, 2018, the Department received approximately \$28,987,000 from OHA.

NOTE O - ASSESSMENTS FOR CENTRAL SERVICE AND ADMINISTRATIVE EXPENSES

The State of Hawai‘i has asserted that the Department is liable for its pro rata share of central service and administrative expenses incurred by the State in accordance with Sections 36-27 and 36-30, Hawai‘i Revised Statutes. Pursuant to Section 36-31, Hawai‘i Revised Statutes, the Department maintains that their funds are trust funds and are not subject to the special fund assessments. Accordingly, no provision for any liability has been made in the accompanying financial statements.

Effective July 1, 1998, Act 27, SLH 1998 amended Section 213 of the Hawaiian Homes Commissions Act and reclassified certain special funds as trust funds.

As of June 30, 2018, the Department's estimate of the accumulated asserted assessments since the inception of the aforementioned law approximated \$24,543,000.



Supplemental Information



State of Hawai‘i
Department of Hawaiian Home Lands
Combining Balance Sheet
Non-Major Governmental Funds
June 30, 2018

Supplemental Information

	Hawaiian Home Loan Fund	Native Hawaiian Rehabilitation Fund	Protocol Funds	Temporary Deposits	East West Collector Road Fund	Total Other Governmental Funds
ASSETS						
Cash in State Treasury	\$ 3,032,057	\$ 6,683,075	\$ 5,870	\$ 2,543,637	\$ 2,350	\$ 12,266,989
Receivables						
Loans, net of allowance for losses of \$16,000	1,609,635	-	-	-	-	1,609,635
Accrued interest	-	75,774	-	-	-	75,774
Total assets	\$ 4,641,692	\$ 6,758,849	\$ 5,870	\$ 2,543,637	\$ 2,350	\$ 13,952,398
LIABILITIES AND FUND BALANCES						
LIABILITIES						
Vouchers and contracts payable	\$ -	\$ 34,198	\$ -	\$ -	\$ -	\$ 34,198
Other liabilities	8,067	-	-	2,543,637	-	2,551,704
Total liabilities	8,067	34,198	-	2,543,637	-	2,585,902
FUND BALANCES						
Assigned to						
Home loans and homestead services	4,633,625	-	5,870	-	-	4,639,495
Home construction and land development	-	6,724,651	-	-	2,350	6,727,001
Total fund balances	4,633,625	6,724,651	5,870	-	2,350	11,366,496
Total liabilities and fund balances	\$ 4,641,692	\$ 6,758,849	\$ 5,870	\$ 2,543,637	\$ 2,350	\$ 13,952,398



State of Hawai'i
Department of Hawaiian Home Lands
Combining Statement of Revenues, Expenditures and Changes in Fund Balances
Non-Major Governmental Funds
for the year ended June 30, 2018

Supplemental Information

	Hawaiian Home Loan Fund	Native Hawaiian Rehabilitation Fund	Protocol Funds	Temporary Deposits	East West Collector Road Fund	Total Other Governmental Funds
REVENUES						
Investment income	\$ -	\$ 110,469	\$ -	\$ -	\$ -	\$ 110,469
Other	57,152	247,532	-	-	-	304,684
Total revenues	57,152	358,001	-	-	-	415,153
EXPENDITURES						
Current:						
Administration and support services	-	271,280	-	-	-	271,280
Homestead services	93,000	-	-	-	-	93,000
Total expenditures	93,000	271,280	-	-	-	364,280
Excess (deficiency) of revenues over (under) expenditures	(35,848)	86,721	-	-	-	50,873
OTHER FINANCING SOURCES						
Transfers in	-	-	2,501	-	-	2,501
Total other financing uses	-	-	2,501	-	-	2,501
Excess (deficiency) of revenues over (under) expenditures and other financing uses	(35,848)	86,721	2,501	-	-	53,374
Net change in fund balances	(35,848)	86,721	2,501	-	-	53,374
FUND BALANCES AT JULY 1, 2017	4,669,473	6,637,930	3,369	-	2,350	11,313,122
FUND BALANCES AT JUNE 30, 2018	\$ 4,633,625	\$ 6,724,651	\$ 5,870	\$ -	\$ 2,350	\$ 11,366,496



Schedule of Expenditures of Federal Awards



State of Hawai‘i
Department of Hawaiian Home Lands
Schedule of Expenditures of Federal Awards
for the year ended June 30, 2018

Federal Grantor/Pass-through Grantor/Program Title	Federal CFDA Number	Pass-Through Identifying Number	Total Federal Expenditures
U.S. Department of Housing and Urban Development			
Native Hawaiian Housing Block Grant, Year 11	14.873	12HBGHI0001	\$ 5,172,599
Native Hawaiian Housing Block Grant, Year 12	14.873	13HBGHI0001	12,265,786
Native Hawaiian Housing Block Grant, Year 13	14.873	14HBGHI0001	989,774
Total CFDA 14.873			<u>18,428,159</u>
Total Expenditures of Federal Awards			<u>\$ 18,428,159</u>

See notes to the schedule of expenditures of federal awards.



State of Hawai‘i
Department of Hawaiian Home Lands
Notes to the Schedule of Expenditures of Federal Awards
June 30, 2018

1. Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Department and is presented on the cash basis of accounting. The information on this schedule is presented in accordance with the requirements of the Uniform Guidance. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

2. Loans Outstanding

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

<u>Program Title</u>	<u>CFDA Number</u>	<u>Amount Outstanding</u>
U.S. Department of Housing and Urban Development		
Native Hawaiian Housing Block Grant	14.783	\$ <u>23,106,446</u>

3. Indirect Costs

The Department has elected not to use the 10% de minimis indirect cost rate allowed under the Uniform Guidance.



Part II

Government Auditing Standards





**Report of Independent Auditors 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 Hawai'i

The Hawaiian Homes Commission
Department of Hawaiian Home Lands

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the State of Hawai'i, Department of Hawaiian Home Lands (the "Department") as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Department's basic financial statements, and have issued our report thereon dated March 5, 2019.

Internal Control Over Financial Reporting

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

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 Department's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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 Department'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 Department's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Akamine, Oyadomari & Kosaki CPAs, Inc.

Honolulu, Hawai'i
March 5, 2019





**Report of Independent Auditors on Compliance for
Each Major Program and on Internal Control Over Compliance
Required by the Uniform Guidance**

The Auditor
State of Hawai'i

The Hawaiian Homes Commission
Department of Hawaiian Home Lands

Report on Compliance for Each Major Federal Program

We have audited the State of Hawai'i, Department of Hawaiian Home Lands' (the "Department") compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on the Department's major federal program for the year ended June 30, 2018. The Department's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts and grants applicable to its federal program.

Auditors' Responsibility

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

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

Opinion on Each Major Federal Program

In our opinion, the Department complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2018.

Report on Internal Control Over Compliance

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

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

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

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

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the governmental activities, each major fund, and the aggregate remaining fund information of the financial statements of the Department as of and for the year ended June 30, 2018, and the related notes to the financial statements which collectively comprise the Department's basic financial statements. We have issued our report thereon dated March 5, 2019, which contained unmodified opinions on those financial statements. Our audit was conducted for



the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the basic financial statements. Such 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. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditure of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Akamine, Oyadomari & Kosaki CPAs, Inc.

Honolulu, Hawai'i
March 5, 2019



Part III

Schedule of Findings and Questioned Costs



State of Hawai‘i
Department of Hawaiian Home Lands
Schedule of Findings and Questioned Costs
for the year ended June 30, 2018

Section I – Summary of Auditors’ Results

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP:

Unmodified

Internal control over financial reporting

- Material weaknesses identified? yes X no
- Significant deficiencies identified? yes X none reported

Noncompliance material to financial statements noted?

 yes X no

Federal Awards

Internal control over major programs:

- Material weaknesses identified? yes X no
- Significant deficiencies identified? yes X none reported

Type of auditors’ report issued on compliance for major programs:

Unmodified

Any audit findings disclosed that are required to be reported in accordance with the Uniform Guidance?

 yes X no

Identification of major federal program:

CFDA

Number	Name of Federal Program or Cluster
14.873	Native Hawaiian Housing Block Grant

Dollar threshold used to distinguish between type A and type B programs:

\$750,000

Auditee qualified as low-risk auditee?

 X yes no



State of Hawai‘i
Department of Hawaiian Home Lands
Schedule of Findings and Questioned Costs (continued)
for the year ended June 30, 2018

Section II – Financial Statement Findings

None noted.

Section III – Federal Award Findings and Questioned Costs

None.

Section IV – Status of Prior Year Findings and Questioned Costs

Internal Control over Financial Reporting

No matters reported.

Federal Award Finding and Questioned Costs

Finding 2017-001 Earmarking (Control Deficiency)

Condition:

There was one instance where the Department did not comply with the earmarking requirement set forth by the Native Hawaiian Housing Block Grant agreement.

Recommendation:

The Department should implement procedures such as tracking all administrative and planning disbursements to ensure the earmarking requirement is met.

Current status:

Improvements were noted. No similar finding reported in 2018.

