



## MINUTES

**Government Affairs/Audit/Legal Matters Committee  
Kapolei Hale, Conference Room B  
1000 Uluohia Street, Kapolei, Hawaii  
Thursday, December 18, 2014 9:00 am**

PRESENT:	Robert "Bobby" Bunda Ivan Lui-Kwan Michael Formby	Carrie Okinaga Donald G. Horner
ALSO IN ATTENDANCE: (Sign-In Sheet and Staff)	Daniel Grabauskas Wils Choy Robert Freitas Diane Arakaki Bruce Sakihama	Joyce Oliveira Gary Takeuchi Cindy Matsushita Andrea Tantoco Jeanne Mariani-Belding

I. Call to Order by Chair

Government Affairs/Audit/Legal Matters Committee Chair Robert "Bobby" Bunda called the meeting to order at 9:00 a.m.

II. Public Testimony on All Agenda Items

Mr. Bunda called for public testimony. There was none.

III. Approval of Minutes of the November 21, 2013 Government Affairs/Audit/Legal Matters Committee Meeting

Mr. Bunda called for the approval of the minutes of the November 21, 2013 meeting of the Government Affairs/Audit/Legal Matters Committee.

Committee member Carrie Okinaga said that the minutes referenced the drafting of management's response to an audit finding, which would contain policies and grant procedures to ensure timely receipt of revenues. HART Chief Financial Officer Diane Arakaki confirmed that those steps were taken as corrective action.

There being no further questions, the minutes were approved as circulated.

IV. Report on the Independent Financial Audit

Ms. Arakaki reminded the Committee that the accounting firm KMH LLP had completed its first year performing HART's financial audit. KMH had been assigned the financial audit contract by former auditor PKF Pacific Hawaii LLP. She introduced Audit Partner Wils Choy and Audit Manager Robert Freitas from KMH, who would present the results of the independent financial audit, a copy of which is attached hereto as Attachment A.

Mr. Choy gave a brief background of KMH, which was founded by partners from national accounting firms 12 years prior. KMH serves both the business and government community, and had been contracted to audit HART as of June 30, 2014.

Mr. Choy reported that KMH had issued an unqualified opinion in accordance with Generally Accepted Accounting Principles. He went on to report that no material or significant control deficiencies had been found in HART. He explained that control deficiencies exist 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 misstatements on a timely basis. Mr. Choy reported that KMH had confirmed that corrections had been made regarding the comment made in the previous year's audit regarding receivables for federal funds.

Mr. Choy said that Mr. Freitas would report on items of note in the Statement on Auditing Standards 114, otherwise referred to as the governance letter. Mr. Freitas started by pointing out that the audit had been performed in accordance with government auditing standards. The letter also noted changes in accounting policies. Lastly, the letter reports on management's judgment in accounting estimates, which identifies areas of risk because of the fact that estimates are involved, such as in the recognition of federal grants. Mr. Freitas concluded by saying that it was a clean audit.

Mr. Choy brought items of note to the committee's attention regarding new or potential changes in government accounting standards. General Accounting Standards Bureau (GASB) Statement Number 68 would significantly change the way in which government entities account for pension obligations beginning the following year. Currently, government entities are not required to account for future projected benefit obligations, as for-profit entities do. However, it is likely that one will be adopted in the future that takes a similar stance on future benefit obligations.

Ms. Okinaga asked Mr. Grabauskas whether the GASB statements would result in any deviation by HART from the City and County of Honolulu's accounting practices. Mr. Grabauskas said that he did not expect that would occur. Mr. Choy added that he understood that the Employee Retirement System was addressing the matter, and would disseminate its findings to the government entities. Ms. Arakaki said that HART had requested a separate actuarial statement apart from the City for budgeting purposes. Mr. Choy said that the amount recorded will not necessarily be a cash requirement, but that it would be accounted for as a future liability. He distinguished that from the annual cash requirements paid into the retirement fund.

Government Affairs/Audit/Legal Matters Committee Minutes  
December 18, 2014

Mr. Bunda said that the impacts to HART would be minimal, as it had a relatively young staff. Mr. Choy agreed that the age demographic of HART staff, which was different from the rest of the City, would affect the calculation. Thus, he agreed with Ms. Arakaki's request for the HART-specific actuarial statement.

Committee member Michael Formby clarified that the reporting period ended on June 30, 2014, and Mr. Choy confirmed.

Ms. Okinaga thanked HART staff for the clean audit.

Mr. Bunda expressed his appreciation to KMH for taking on the financial audit from PKF. Mr. Choy thanked Ms. Arakaki and her staff for their cooperation in getting the audit done within the specified time frame.

Mr. Bunda called for a vote to recommend the audit report be forwarded to the full Board. Committee member Ivan Lui-Kwan so moved, and Mr. Formby seconded the motion. All being in favor, the motion carried unanimously.

V. Executive Session

There was no need for executive session.

VI. Adjournment

There being no further business before the committee, Mr. Bunda adjourned the meeting at 9:18 a.m.

Respectfully Submitted,



Cindy Matsushita  
Board Administrator

Approved:



Terrence Lee  
Chair, Government Affairs/Audit/Legal  
Matters Committee

SEP 24 2015  
Date

## ATTACHMENT A

Financial Statements and Independent Auditor's Report

**Honolulu Authority for Rapid Transportation**  
**(a component unit of the City and County of Honolulu)**

June 30, 2014 and 2013



A Hawaii Limited Liability Partnership

To the Board of Directors  
Honolulu Authority for Rapid Transportation  
City and County of Honolulu

We have completed our financial audit of the Honolulu Authority for Rapid Transportation, a component unit of the City and County of Honolulu, (HART) as of and for the fiscal year ended June 30, 2014. The audit was performed in accordance with our agreement dated July 16, 2014.

**Objective of the Audit**

The primary purpose of our audit was to form an opinion on the fairness of the presentation of HART's financial statements as of and for the fiscal year ended June 30, 2014.

**Scope of the Audit**

Our audit was performed 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. The scope of our audit included an examination of the transactions and accounting records of HART for the fiscal year ended June 30, 2014.

**Organization of the Report**

This report is organized into three parts:

PART I. FINANCIAL STATEMENTS

PART II. SUPPLEMENTARY INFORMATION

PART III. REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

We would like to take this opportunity to express our appreciation to the personnel of the HART for the cooperation and assistance extended to us during our audit. We shall be pleased to discuss any questions that you or your associates may have regarding our reports.

*KMH LLP*

KMH LLP

Honolulu Hawaii  
December 18, 2014

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**PART I**  
**FINANCIAL STATEMENTS**



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A Hawaii Limited Liability Partnership

## **Independent Auditor's Report**

To the Board of Directors  
Honolulu Authority for Rapid Transportation  
City and County of Honolulu

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Honolulu Authority for Rapid Transportation (HART), a component unit of the City and County of Honolulu, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise HART'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 an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Honolulu Authority for Rapid Transportation, as of June 30, 2014, and the changes in its financial position and its cash flows 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 1, the financial statements present only the Honolulu Authority for Rapid Transportation and do not purport to, and do not, present fairly the financial position of the City and County of Honolulu as of June 30, 2014, and the changes in its financial position or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

### **Other Matters**

#### ***2013 Financial Statements***

The financial statements of HART, as of and for the year ended June 30, 2013, were audited by other auditors whose report dated on November 15, 2013 expressed an unmodified opinion on those statements.

#### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the schedule of funding progress for the Hawaii Employer-Union Health Benefits Trust Fund on pages 7 through 12 and page 34, 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 Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated December 18, 2014 on our consideration of the HART'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 HART's internal control over financial reporting and compliance.

KMH LLP

KMH LLP

Honolulu, Hawaii  
December 18, 2014

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2014 and 2013

The Honolulu Authority for Rapid Transportation (HART) is a semi-autonomous government unit of the City and County of Honolulu (City), which came into being on July 1, 2011 pursuant to a 2010 amendment to the Revised Charter of the City and County of Honolulu (RCH). HART consists of a board of directors (Board), executive director, and staff. HART is authorized under the RCH to "develop, operate, maintain and expand the city fixed guideway system..."

The Honolulu Rail Transit Project (the Project) consists of design and construction of a 20-mile, grade-separated fixed rail system from East Kapolei to the Ala Moana Center in Honolulu, Hawaii. The Project begins in East Kapolei, proceeds to the University of Hawaii at West Oahu, then turns east to Pearl Harbor and the Honolulu International Airport, and ends at Kona Street adjacent to the Ala Moana Center. The Project will operate in an exclusive right-of-way and will be elevated except for a 0.6-mile, at-grade section near Leeward Community College. The Project includes 21 transit stations; a maintenance and storage facility; 80 light metro fully automated (driverless) rail vehicles and associated core systems; and four park-and-ride facilities at several locations.

This section presents the management's discussion and analysis of HART's financial condition and activities for the fiscal years ended June 30, 2014 and 2013. This summary is designed to provide an introduction to the financial statements and the financial condition of HART. This information should be read in conjunction with the financial statements. Prior to July 1, 2011, the financial position and results of operations of the Project were reported as a governmental fund in the City's Comprehensive Annual Financial Reports.

### **Overview of the Financial Statements**

The financial statements are presented using the economic resources measurement focus and the accrual basis of accounting, whereby revenues and expenses are recognized in the period earned or incurred.

The basic financial statements include statements of net position, statements of revenues, expenses and changes in net position, statements of cash flows, and notes to the financial statements. The statements of net position present the resources and obligations of HART at June 30, 2014 and 2013, respectively. The statement of revenues, expenses and changes in net position present information showing how HART's net position changed during the past two fiscal years.

The statements of cash flows present changes in cash and cash equivalents resulting from operating, investing, capital and related financing activities, and non-capital financing activities.

The notes to the financial statements provide required disclosures and other information necessary for the fair presentation of the financial statements. The notes detail information about HART's significant accounting policies, account balances, related party transactions, employee benefit plans, commitments, contingencies, and other significant events. Supplementary information on post-employment benefits is also included.

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2014 and 2013

**Financial Highlights**

**Condensed Statements of Revenues, Expenses and Changes in Net Position**

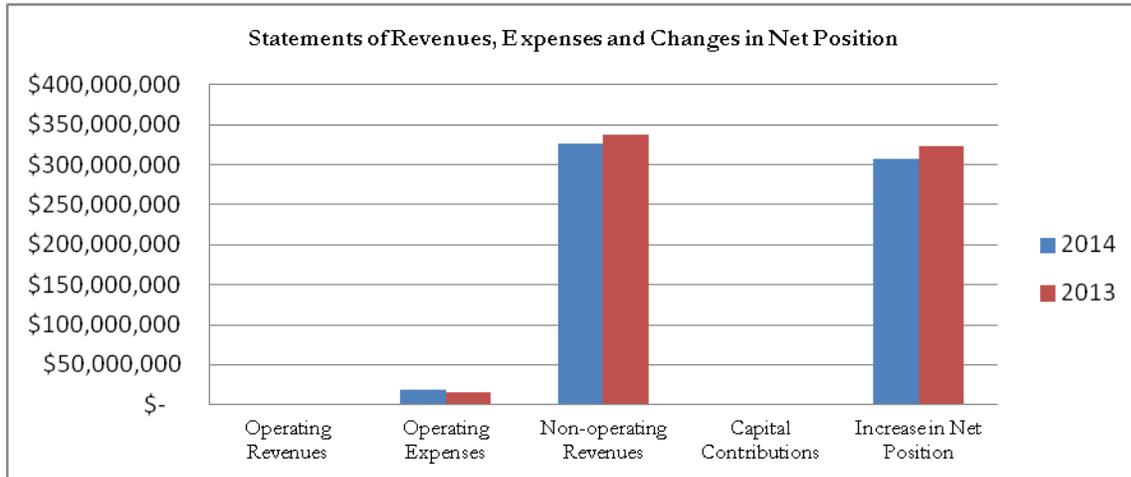
	2014	2013	Increase (decrease)	% Change
Operating expenses				
Administration and general	\$ 12,015,351	\$ 8,491,401	\$ 3,523,950	42%
Fringe benefits	3,835,579	2,927,337	908,242	31%
Contractual services	1,145,619	1,943,572	(797,953)	-41%
Insurance	1,909,200	1,864,032	45,168	2%
Other operating expense	511,031	197,990	313,041	158%
Total operating expenses	<u>19,416,780</u>	<u>15,424,332</u>	<u>3,992,448</u>	26%
Operating loss	(19,416,780)	(15,424,332)	(3,992,448)	26%
Non-operating revenues and expenses				
Intergovernmental revenue	218,390,853	173,822,505	44,568,348	26%
Federal grants	107,116,948	164,053,218	(56,936,270)	-35%
Net interest income & other	1,074,954	359,875	715,079	199%
Total non-operating revenues	<u>326,582,755</u>	<u>338,235,598</u>	<u>(11,652,843)</u>	-3%
INCREASE IN NET POSITION	307,165,975	322,811,266	(15,645,291)	-5%
Net position at beginning of year	<u>1,285,208,198</u>	<u>962,396,932</u>	<u>322,811,266</u>	N/A
Net position at end of year	<u>\$ 1,592,374,173</u>	<u>\$ 1,285,208,198</u>	<u>\$ 307,165,975</u>	<u>24%</u>

Honolulu Authority for Rapid Transportation  
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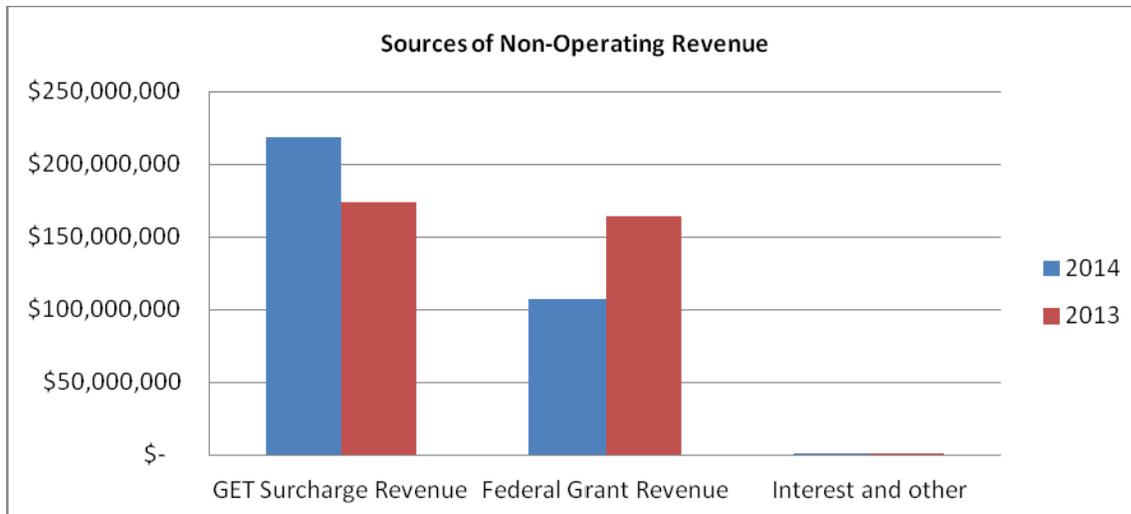
MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2014 and 2013

**Financial Highlights (continued)**



HART's primary non-operating revenue sources are the 0.5% county surcharge on the State of Hawaii's General Excise Tax (GET) and grant assistance from the U.S. Department of Transportation's Federal Transit Administration (FTA). Pursuant to Section 248-2.6 of the Hawaii Revised Statutes, the State Department of Taxation remits 90% of the surcharge to the City on a quarterly basis. During FY 2014 and FY 2013, HART recognized \$218,390,853 and \$173,822,505, respectively, from the GET county surcharge. In FY 2014 and FY 2013 HART also recognized \$107,116,948 and \$164,053,218, respectively, in FTA grant assistance.



Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

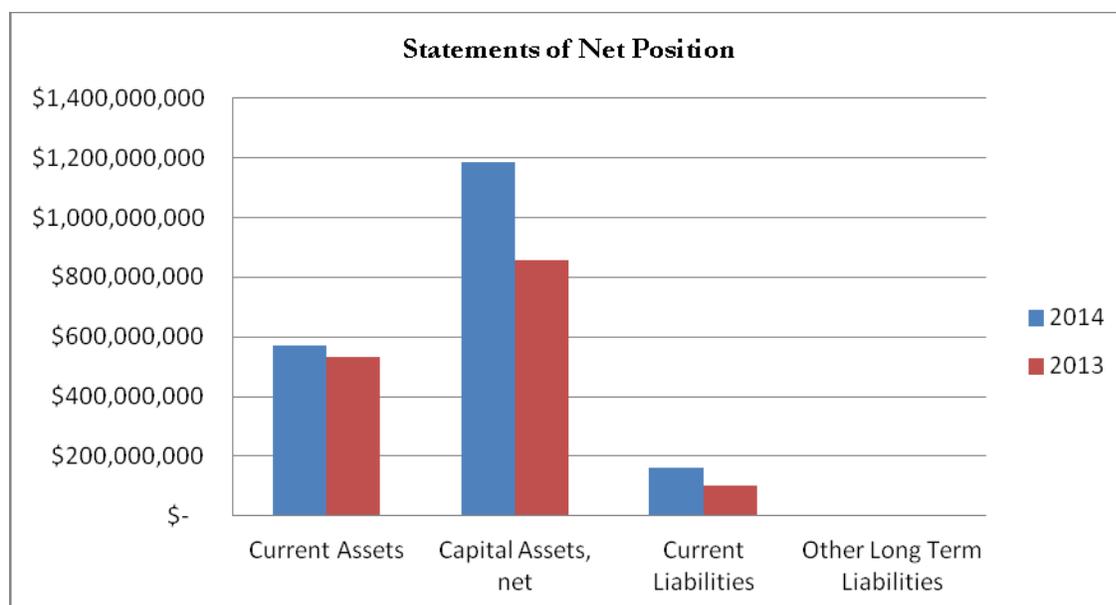
MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2014 and 2013

**Financial Highlights (continued)**

**Condensed Statements of Net Position**

	2014	2013	Increase (decrease)	%
<b>Assets</b>				
Current assets				
Cash and cash equivalents	\$ 441,011,319	\$ 393,709,711	\$ 47,301,608	12%
Receivables	129,991,834	134,269,096	(4,277,262)	-3%
Prepaid expenses	1,217,390	3,066,374	(1,848,984)	-60%
Capital assets, net	<u>1,184,636,596</u>	<u>857,964,509</u>	<u>326,672,087</u>	<u>38%</u>
Total assets	<u>\$ 1,756,857,139</u>	<u>\$ 1,389,009,690</u>	<u>\$ 367,847,449</u>	<u>26%</u>
<b>Liabilities</b>				
Current liabilities	\$ 161,882,407	\$ 101,472,751	\$ 60,409,656	60%
Other long-term liabilities-noncurrent	<u>2,600,559</u>	<u>2,328,741</u>	<u>271,818</u>	<u>12%</u>
Total liabilities	<u>164,482,966</u>	<u>103,801,492</u>	<u>60,681,474</u>	<u>58%</u>
<b>Net position</b>	<u>1,592,374,173</u>	<u>1,285,208,198</u>	<u>307,165,975</u>	<u>24%</u>
Total liabilities and net position	<u>\$ 1,756,857,139</u>	<u>\$ 1,389,009,690</u>	<u>\$ 367,847,449</u>	<u>26%</u>



Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2014 and 2013

**Financial Highlights (continued)**

Total assets at year-end FY 2014 and FY 2013 were \$1,756,857,139 and \$1,389,009,690, respectively. Total liabilities at year-end FY 2014 and FY 2013 were \$164,482,966 and \$103,801,492, respectively. Net position increased by \$307,165,975 primarily due to intergovernmental revenues and federal grants.

Construction on the Project was suspended on August 24, 2012 after a ruling by the Hawaii Supreme Court requiring the completion of the Archaeological Inventory Survey (AIS) in the Kaleikini v. Formby et al litigation. During the suspension period final design work continued on all contracts that were awarded prior to the Supreme Court ruling. HART has completed the AIS requirements and construction was restarted on September 16, 2013.

The Project has executed \$2,486,920,607 in contracts since October 2009 to date for the planning, design, and construction of the Project. This amounts to 56.7% of the anticipated total project cost.

The Project will affect an estimated 217 parcels of real property. As of June 30, 2014, HART has acquired title to or use of 66 parcels of real property.

As of June 30, 2014, 9.3% of the utilities have been relocated. Utility relocations are performed by the respective companies owning the equipment.

Overall design progress is 77% based on the weighted average progress of the individual final design contracts and the design levels of effort of the Design-Build (DB) and Design-Build-Operate-Maintain (DBOM) construction contracts.

The construction of the west guideway aerial structure from East Kapolei Station to Leeward Community College (LCC) is well underway as part of the West Oahu/Farrington Highway (WOFH) Guideway design-build project. Additionally, the Kamehameha Highway (KHG) Guideway design-build project continues with wet and dry utility relocations as well as roadway widening work in preparation for the production drilled shaft and segmented guideway construction from LCC to Aloha Stadium. As of August 8th, 2014 completed elements of segmented guideway work for the initial 10 miles include the following:

<b>Structure Element</b>	<b>Total to Date</b>	<b>% Complete</b>
Shafts	141	53.0%
Transition Zones	121	45.5%
Columns	113	42.5%
Segment Casting	920	29.1%
Segment Erection	240	7.6%
Span Stressed	20	7.6%

The design-build construction of the HART Maintenance and Storage Facility (MSF) is ongoing with the commencement of tilt-up precast concrete panel construction for the OSB and the completion of structural steel erection activities. Site work excavation and grading is also making significant progress in area 8 to balance out the fill sections with native material in area 4, as well as locating of existing utilities, excavation and installation of drainage elements along the detention pond.

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2014 and 2013

**Capital Assets and Long-Term Debt**

As of the end of FY 2014, HART had \$1,185 million invested in capital assets. This amount represents an increase (including additions and deductions) of just over \$326 million, or 38%, over last year.

	2014	2013
Equipment and machinery	\$ 86,500	\$ 96,151
Land	65,268,559	50,163,534
Construction in progress	1,119,281,537	807,704,824
Total	<u>\$ 1,184,636,596</u>	<u>\$ 857,964,509</u>

HART has not issued any long-term bonds. Additional information on HART's capital assets and long-term liabilities can be found in note D and F to the financial statements.

**Risks**

On June 29, 2012, HART submitted the City's request to the FTA for a Full Funding Grant Agreement (FFGA) which was awarded on December 19, 2012. The maximum Federal New Starts financial contribution under the FFGA is \$1.55 billion for the Project; however the annual appropriation amounts may be reduced and appropriated over a longer period than planned.

The project faces the normal risks associated with a multi-year, major construction project that includes unanticipated construction delays, cost inflation over the period of construction, and economic downturns that impact revenues.

HART is party to various legal proceedings arising in the normal course of business. Further information regarding these legal proceedings can be found in note I to the financial statements.

**Request for Information**

This financial report is designed to provide a general overview of HART's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Honolulu Authority for Rapid Transportation, 1099 Alakea Street, Suite 1700, Honolulu, Hawaii 96813.

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

STATEMENTS OF NET POSITION

June 30, 2014 and 2013

	2014	2013
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 441,011,319	\$ 393,709,711
Receivables	129,991,834	134,269,096
Prepaid expenses	1,217,390	3,066,374
Total current assets	572,220,543	531,045,181
Capital assets		
Equipment and machinery	171,540	144,569
Accumulated depreciation	(85,040)	(48,418)
	86,500	96,151
Land	65,268,559	50,163,534
Construction work in progress	1,119,281,537	807,704,824
Capital assets, net	1,184,636,596	857,964,509
TOTAL ASSETS	\$ 1,756,857,139	\$ 1,389,009,690
LIABILITIES AND NET POSITION		
CURRENT LIABILITIES		
Accounts payable	\$ 115,552,902	\$ 52,131,044
Accrued liabilities	46,234,491	49,296,717
Other long-term liabilities - current portion	95,014	44,990
Total current liabilities	161,882,407	101,472,751
Other long-term liabilities - noncurrent portion	2,600,559	2,328,741
Total liabilities	164,482,966	103,801,492
NET POSITION		
Net investment in capital assets	1,069,158,564	806,171,143
Unrestricted	523,215,609	479,037,055
Total net position	1,592,374,173	1,285,208,198
TOTAL LIABILITIES AND NET POSITION	\$ 1,756,857,139	\$ 1,389,009,690

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

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

Years ended June 30, 2014 and 2013

	2014	2013
Operating expenses		
Administration and general	\$ 12,015,351	\$ 8,491,401
Fringe benefits	3,835,579	2,927,337
Contractual services	1,145,619	1,943,572
Insurance	1,909,200	1,864,032
Utilities	221,445	89,990
Materials and supplies	245,541	77,703
Depreciation	36,622	18,529
Maintenance	7,423	11,768
Total operating expenses	19,416,780	15,424,332
Operating loss	(19,416,780)	(15,424,332)
Non-operating revenues and (expenses)		
Intergovernmental revenues	218,390,853	173,822,505
Federal grants	107,116,948	164,053,218
Interest income	298,748	310,597
Interest expense	-	(452,106)
Other revenue	776,206	501,384
Total nonoperating revenues	326,582,755	338,235,598
INCREASE IN NET POSITION	307,165,975	322,811,266
Net position at beginning of year	1,285,208,198	962,396,932
Net position at end of year	\$ 1,592,374,173	\$ 1,285,208,198

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

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

STATEMENTS OF CASH FLOWS

Years ended June 30, 2014 and 2013

	2014	2013
Cash flows from operating activities		
Cash payments to suppliers for goods and services	\$ (10,594,843)	\$ (4,217,842)
Cash payments to employees	(11,566,726)	(9,927,965)
Net cash used in operating activities	(22,161,569)	(14,145,807)
Cash flows from noncapital financing activities		
Intergovernmental revenues, federal grants and others	332,188,472	252,391,530
Net cash provided by noncapital financing activities	332,188,472	252,391,530
Cash flows from capital and related financing activities		
Acquisition and construction of capital assets	(326,708,709)	(309,364,744)
Non-operating revenue	63,684,666	46,626,928
Net cash used in capital and related financing activities	(263,024,043)	(262,737,816)
Cash flows from investing activities		
Interest on cash and cash equivalents	298,748	245,053
Net cash provided by investing activities	298,748	245,053
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	47,301,608	(24,247,040)
Cash and cash equivalents at beginning of year	393,709,711	417,956,751
Cash and cash equivalents at end of year	\$ 441,011,319	\$ 393,709,711

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

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

STATEMENTS OF CASH FLOWS (continued)

Years ended June 30, 2014 and 2013

	2014	2013
Reconciliation of operating loss to net cash used in operating activities		
Operating loss	\$ (19,416,780)	\$ (15,424,332)
Adjustments to reconcile operating loss to net cash used in operating activities		
Depreciation	36,622	18,529
Changes in assets and liabilities		
Increase in receivables	(1,627,203)	(55,591)
Decrease in prepaid expenses	1,848,984	1,840,321
Decrease in accounts payable	(262,808)	(382,372)
Decrease in other long-term liabilities	(2,740,384)	(142,362)
Total adjustments	(2,744,789)	1,278,525
Net cash used in operating activities	\$ (22,161,569)	\$ (14,145,807)

Non-cash capital financing activities:

During the year ended June 30, 2014 and 2013, HART accrued additional costs as construction in progress of \$63,684,666 and \$46,613,544, respectively.

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

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Operations

The Revised Charter of the City and County of Honolulu authorizes the Honolulu Authority for Rapid Transportation (HART) to develop, operate, maintain and expand the city fixed guideway system. HART is a semi-autonomous government unit of the City and County of Honolulu (City). It is a component unit of the City. HART is in the process of developing the rail transit system and has not begun revenue operations.

2. Financial Statement Presentation

The accounting policies of HART conform to accounting principles generally accepted in the United States of America as applicable to enterprise activities of governmental units, as promulgated by the Government Accounting Standards Board (GASB).

In March 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This Statement clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resource to ensure consistency in financial reporting. The provisions of this Statement are effective for periods beginning after December 15 2012. The adoption of GASB 65 did not have a material impact on HART's financial statements.

In March 2012, GASB issued Statement No. 66, *Technical Correction-2012, an amendment of GASB Statements No. 10 and No. 62*. This Statement enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The provisions for this Statement are effective for the periods beginning after December 15, 2012. The adoption of GASB 66 did not have a material impact on HART's financial statements.

In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions*, replacing the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, and Statement No. 50, *Pension Disclosures*, as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. Moreover, this Statement requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. The provisions for this Statement are effective for periods beginning after June 15, 2014. HART has not yet determined the effect this Statement will have on its financial statements.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2. Financial Statement Presentation (continued)

In November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68*. The objective of this statement is to address an issue regarding application of the transition provisions of Statement No. 68, Accounting and Financial Reporting for Pensions. The provisions of this Statement are required to be applied simultaneously with the provisions of Statement 68 and are effective for periods beginning after June 15, 2014. HART has not yet determined the effect this Statement will have on its financial statements.

3. Basis of Accounting

The accompanying financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

The operating revenues of HART are the result of providing services in connection with the delivery of transportation services of the rail system, which is not yet operational. The operating expenses of HART include the cost of services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

4. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Specifically, management has made estimates based on assumptions for intergovernmental receivables and construction delay claims. Actual results could differ from those estimates.

5. Revenue Recognition

Revenue sources that are considered susceptible to accrual when earned include a county surcharge on the State of Hawaii's General Excise Tax (GET) and grant assistance from the U.S. Department of Transportation's Federal Transit Administration (FTA). GET revenue is recognized when earned. Revenues on cost reimbursement contracts are recognized when allowable and reimbursable expenses are incurred, and upon meeting the legal and contractual requirements of the funding source. No allowance for doubtful accounts was recorded as of June 30, 2014 and 2013.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

6. Cash and Cash Equivalents

HART considers all cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition to be cash and cash equivalents.

7. Capital Assets

Capital assets are generally those assets with an individual price in excess of \$5,000 for equipment and machinery and \$100,000 for infrastructure, buildings, and structures with a useful life of more than one year. Capital assets are stated at cost and include contributions by governmental agencies at cost or estimated value. Additions, improvements, and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs related to repairs and maintenance is expensed as incurred.

Assets are depreciated over the individual asset's estimated useful life using the straight-line method. Depreciation on both purchased and contributed assets is charged against operations

Depreciation on all assets is provided for on the straight-line basis over the following estimated useful lives:

	<u>Years</u>
Infrastructure	50-75
Buildings and improvements	30-50
Equipment and machinery	5-25
Rail vehicles	25-35

8. Compensated Absences

HART accrues accumulated vacation when earned by the employee. Vacation benefits accrue at a rate of one and three-quarters working days per month. Each employee is allowed to accumulate a maximum of 90 days of accrued vacation as of the end of the calendar year.

Sick leave accumulates at the rate of one and three-quarters working days for each month. Sick leave is taken only in the event of illness and is not convertible to pay; accordingly, sick leave is not accrued in the accompanying financial statements. Employees who retire or leave government service in good standing with 60 or more unused sick leave days are entitled to an additional service credit in the retirement system. At June 30, 2014 and 2013, accumulated sick leave amounted to \$1,770,935 and \$2,078,026, respectively.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

9. Deferred Compensation Plan

All full-time employees of HART are eligible to participate in the City and County of Honolulu's Public Employees' Deferred Compensation Program (Plan), adopted pursuant to Internal Revenue Code Section 457. The Plan permits eligible employees to defer a portion of their salary until future years by contributing to a fund managed by a plan administrator. The deferred compensation amounts are not available to employees until termination, retirement, death, or unforeseeable emergency.

A trust fund was established to protect Plan assets from claims of general creditors and from diversion to any uses other than paying benefits to participants and beneficiaries. Plan assets of \$3,280,327 and \$2,748,290 are not reported in the accompanying financial statements at June 30, 2014 and 2013, respectively.

10. Net Position

Net position comprises the various net earnings (losses) from operating and non-operating revenues, expenses and contributed capital. Net position is classified in the following two components: net investment in capital assets or unrestricted net position. Net investment in capital assets consists of capital assets, net of accumulated depreciation and reduced by outstanding debt that is attributable to the acquisition, construction, or improvement of those assets. Unrestricted net position consists of all other net position not included in net investment in capital assets.

11. Risk Management

HART is exposed to various risks for losses related to torts; theft of or damage to, or destruction of assets; errors or omissions; natural disasters; and injuries to employees. A liability for a claim for a risk of loss is established if the information indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss is reasonably estimable.

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE B - CASH AND CASH EQUIVALENTS

Cash deposited with the City is maintained by the Department of Budget and Fiscal Services of the City. The City maintains a cash and investment pool that is used by all of the City's funds and HART. Information pertaining to credit risk and interest rate risk is available for only the total cash and investment pool, which is disclosed in the City's Comprehensive Annual Financial Report (CAFR) available at the City's website: <http://www1.honolulu.gov/budget/cafr.htm>.

The respective portion of this pool is displayed in the accompanying financial statements as cash and cash equivalents. The Hawaii Revised Statutes (HRS) provide for the City's Director of Budget and Fiscal Services to deposit the cash with any national or state bank or federally insured financial institution authorized to do business in the State of Hawaii, provided that all deposits are fully insured or collateralized with securities held by the City or its agents in the City's name.

State statutes also authorize the City to invest in obligations of the U.S. Treasury and U.S. agencies, obligations of other states, cities and counties, mutual funds and bank repurchase agreements. Investments in repurchase agreements are primarily U.S. government or federal agency securities. The City does not have a policy relative to interest rate risk. Maturity date for all investments is less than one year.

NOTE C – RECEIVABLES

Receivables as of June 30, 2014 and 2013 were comprised of the following amounts:

	<u>2014</u>	<u>2013</u>
Intergovernmental		
General excise tax	\$ 49,457,334	\$ 50,356,185
Federal grants	<u>78,777,909</u>	<u>83,783,523</u>
	128,235,243	134,139,708
Other	<u>1,756,591</u>	<u>129,388</u>
Total receivables	<u>\$ 129,991,834</u>	<u>\$ 134,269,096</u>

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE D - CAPITAL ASSETS

Capital assets activity during 2014 and 2013 were as follows:

	Balance July 1, 2013	Additions	Deletions	Balance June 30, 2014
Equipment and machinery	\$ 144,569	\$ 26,971	\$ -	\$ 171,540
Less accumulated depreciation	(48,418)	(36,622)	-	(85,040)
	96,151	(9,651)	-	86,500
Land	50,163,534	15,105,025	-	65,268,559
Construction in progress	807,704,824	311,576,713	-	1,119,281,537
Capital assets, net	<u>\$ 857,964,509</u>	<u>\$ 326,672,087</u>	<u>\$ -</u>	<u>\$ 1,184,636,596</u>
	Balance July 1, 2012	Additions	Deletions	Balance June 30, 2013
Equipment and machinery	\$ 171,540	\$ -	\$ (26,971)	\$ 144,569
Less accumulated depreciation	(43,476)	(18,529)	13,587	(48,418)
	128,064	(18,529)	(13,384)	96,151
Land	31,882,014	18,281,520	-	50,163,534
Construction in progress	516,621,600	291,083,224	-	807,704,824
Capital assets, net	<u>\$ 548,631,678</u>	<u>\$ 309,346,215</u>	<u>\$ (13,384)</u>	<u>\$ 857,964,509</u>

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE E - COMMITMENTS

Leases

HART leases office space and equipment under operating leases expiring through fiscal year 2021. The future minimum rental payments for operating leases at June 30, 2014 are as follows:

Fiscal Year	Annual
2015	\$ 1,219,000
2016	1,252,000
2017	1,138,000
2018	751,000
2019	770,000
2020 to 2021	<u>1,137,000</u>
Total Minimum Payments	<u>\$ 6,267,000</u>

Additionally, these leases provide for payment of common area charges. Office and equipment rental expenses were \$2,315,928 and \$2,226,747 for the years ended June 30, 2014 and 2013, respectively.

Other Commitments

HART has contractual commitments at June 30, 2014 of \$2,872,528,541. These include contracts for construction, design, and professional services.

NOTE F – OTHER LONG-TERM LIABILITIES

The following is a summary of changes in other long-term liabilities during the fiscal years ended June 30, 2014 and 2013:

	Balance July 1, 2013	Transfers	Additions	Reductions	Balance June 30, 2014	Current Portion
Accrued vacation	\$ 1,020,250	\$ -	\$ 22,842	\$ -	\$ 1,043,092	\$ 95,014
Other postemployment benefits	1,353,481	-	299,000	-	1,652,481	-
	<u>\$ 2,373,731</u>	<u>\$ -</u>	<u>\$ 321,842</u>	<u>\$ -</u>	<u>\$ 2,695,573</u>	<u>\$ 95,014</u>

	Balance July 1, 2012	Transfers	Additions	Reductions	Balance June 30, 2013	Current Portion
Accrued vacation	\$ 808,538	\$ -	\$ 425,644	\$ 213,932	\$ 1,020,250	\$ 44,990
Other postemployment benefits	1,071,481	-	282,000	-	1,353,481	-
	<u>\$ 1,880,019</u>	<u>\$ -</u>	<u>\$ 707,644</u>	<u>\$ 213,932</u>	<u>\$ 2,373,731</u>	<u>\$ 44,990</u>

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE G - EMPLOYEE BENEFIT PLANS

Defined Benefit Pension Plan

Substantially all employees of HART are members of the Employees' Retirement System of the State of Hawaii (ERS), a cost-sharing multiple-employer defined benefit public employee retirement plan. The ERS provides retirement benefits as well as death and disability benefits and is governed by a Board of Trustees. All contributions, benefits, and eligibility requirements are established by Hawaii Revised Statutes (HRS) Chapter 88 and can be amended by legislative action.

The ERS is composed of a contributory and hybrid contributory retirement plan. Prior to June 30, 1984, the plan consisted of only a contributory option. Effective July 1, 1984, legislation was enacted to create a noncontributory plan for members of the ERS who are also covered under Social Security. Persons employed in positions not covered by Social Security are precluded from the noncontributory plan. The noncontributory plan provides for reduced benefits and covers most eligible employees hired after June 30, 1984. Employees hired before that date were allowed to continue under the contributory plan or to elect the noncontributory plan and receive a refund of employee contributions.

All benefits vest after five and ten years of credited service under the contributory and noncontributory plans, respectively. Both plans provide a monthly retirement allowance based on the employee's age, years of credited service, and average final compensation (AFC). The AFC is the average salary earned during the five highest paid years of service, including the vacation payment, if the employee became a member prior to January 1, 1971. The AFC for members hired on or after that date and prior to January 1, 2003, is based on the three highest years of service, excluding the vacation payment. Effective January 1, 2003, the AFC is the highest three calendar years or highest five calendar years plus lump sum vacation payment, or last 36 credited months or last 60 credited months plus lump sum vacation payment.

Most covered employees under the contributory plan are required to contribute 7.8% of their salary. Prior to July 1, 2005, the funding method used to calculate the total employer contribution requirement was the Entry Age Normal Actuarial Cost Method. Under this method, employer contributions to the ERS were comprised of normal cost plus level annual payments required to liquidate the unfunded actuarial liability over the remaining period of 29 years from July 1, 2000. Effective July 1, 2008, employer contribution rates are a fixed percentage of compensation, generally 16.0% for most covered employees. HART's contribution to the ERS for the years ended June 30, 2014, 2013 and 2012 was \$1,182,861 and \$1,049,223, and \$809,516, respectively.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE G - EMPLOYEE BENEFIT PLANS (continued)

Defined Benefit Pension Plan (continued)

The 2004 State of Hawaii legislative sessions approved a hybrid retirement plan, which took effect on July 1, 2006. Employees who choose to be under this plan are required to contribute 6% of their salary and will receive pensions based on a 2% benefit formula instead of a 1.25% benefit formula under the current noncontributory plan. The hybrid plan does not affect HART's contributions to the ERS.

The ERS issues a CAFR that includes financial statements and required supplementary information, which may be obtained at the following address: Employees' Retirement System of the State of Hawaii, 201 Merchant Street, Suite 1400, Honolulu, Hawaii 96813.

Post-Retirement Health Care and Life Insurance Benefits

In addition to providing pension benefits, the State of Hawaii Employer-Union Health Benefits Trust Fund (EUTF), an agent multiple-employer plan provides certain health care (medical, prescription, vision, and dental) and life insurance benefits for retired City employees. Act 88 established the EUTF during the 2001 legislative session and is codified in HRS 87A. Contributions are based on negotiated collective bargaining agreements and are limited by State statute to the actual cost of benefit coverage.

For employees hired before July 1, 1996, the City pays 100% of the monthly health care premium for employees retiring with 10 or more years of credited service, and 50% of the monthly premium for employees retiring with fewer than 10 years of credited service.

For employees hired after June 30, 1996 and retiring with 25 years or more of service, the City pays the entire health care premium. For employees retiring with at least 15 years of service but fewer than 25 years of service, the City pays 75% of the monthly Medicare or non-Medicare premium. For those retiring with at least 10 years but less than 15 years of service, the City pays 50% of the retired employees' monthly Medicare or non-Medicare premium. For those retiring with less than 10 years of service, the City makes no contributions.

For employees hired after June 30, 2001 and retiring with over 25 years of service, the City will pay 100% of the monthly premium based on the self plan. For those who retire with at least 15 years but fewer than 25 years of service, the City will pay 75% of the retired employees' monthly Medicare or non-Medicare premium based on the self plan. For those retiring with at least 10 years but fewer than 15 years of service, the City pays 50% of the retired employees' monthly Medicare or non-Medicare premium based on the self plan. For those with fewer than 10 years of service, the City makes no contributions.

The City also reimburses 100% of Medicare premium costs for retirees and qualified dependents (through the State), who are at least 65 years of age and have at least 10 years of service.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE G - EMPLOYEE BENEFIT PLANS (continued)

Annual Other Postemployment Benefits (OPEB) Cost and Net OPEB Obligation

HART is required to contribute the annual required contribution (ARC) of the employer, an actuarially determined amount. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years.

The following table displays for the years ended June 30, 2014 and 2013, the components of the annual OPEB cost, the amount contributed to the plan, the changes to the net OPEB obligation, and the percentage of annual OPEB cost contributed:

	<u>2014</u>	<u>2013</u>
Annual required contribution	\$ 292,000	\$ 282,000
Interest on net OPEB obligation	34,000	-
Adjustment to annual required contribution	<u>(27,000)</u>	<u>-</u>
Annual OPEB cost	299,000	282,000
Contribution made	<u>-</u>	<u>-</u>
Increase in net OPEB obligation	299,000	282,000
Net OPEB obligation at beginning of fiscal year	<u>490,000</u>	<u>208,000</u>
Net OPEB obligation at end of fiscal year	<u>\$ 789,000</u>	<u>\$ 490,000</u>
Percentage of annual OPEB cost contributed	0%	0%

Funded Status and Funding Progress

The following is the schedule of the funded status and funding progress of the plan as of the most recent actuarial valuation date, that are, July 1, 2013 and July 1, 2011:

Actuarial accrued liability	\$ 3,413,000	\$ 1,964,000
Actuarial value of plan assets	<u>9,000</u>	<u>-</u>
Unfunded actuarial accrued liability (UAAL)	<u>\$ 3,404,000</u>	<u>\$ 1,964,000</u>
Funded ratio	0.3%	0.0%
Covered payroll (active plan members)	\$ 6,760,000	\$ 5,385,000
UAAL as a percentage of covered payroll	50.4%	36.5%

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE G - EMPLOYEE BENEFIT PLANS (continued)

Annual Other Postemployment Benefits (OPEB) Cost and Net OPEB Obligation (continued)

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the most recent actuarial valuation, dated as of July 1, 2013, the entry age normal actuarial cost method was used. The actuarial assumptions included a discount rate of 7.0%, which was based on EUTF's anticipated asset investment return and the HART's anticipated funding level. Actuarial assumptions also included an annual health cost trend rate for PPO plans of 9.0% for 2014, declining to a rate of 5% after 10 years, and HMO plans of 7.5% for 2014 of 7.5% for 2014, declining to a rate of 5% after 10 years; expected payroll increases of 3.5% to amortize unfunded liabilities, projected salary increases based on the ERS July 1, 2013 assumptions to determine the actuarial accrued liability, and an inflation rate of 3.0%. The unfunded actuarial accrued liability is being amortized over a 30 year closed period as a level percentage of projected payrolls.

The EUTF issues a stand-alone financial report that includes financial statements and required supplementary information, which may be obtained at the following address: State of Hawaii Employer-Union Health Benefits Trust Fund, 201 Merchant Street, Suite 1520, Honolulu, Hawaii 96813.

NOTE H - RELATED PARTY TRANSACTIONS

Intergovernmental Revenues and Federal Grants

During the year ended June 30, 2014, the HART recognized intergovernmental revenues of \$218,390,853 from the GET county surcharge and \$107,116,948 in FTA grant assistance.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE H - RELATED PARTY TRANSACTIONS (continued)

Central Administrative Services Expense Fee

HART has an agreement with the City to pay a Central Administrative Services Expense (CASE) fee for treasury, personnel, purchasing, legal, and other services that the City provides to HART on an on-going basis. CASE fees totaled \$923,621 and \$1,065,418 for the years ended June 30, 2014 and 2013, respectively, and is included as part of administration and general expense in the statements of revenues, expenses and changes in net position.

NOTE I – LITIGATION

HART is party to various legal proceedings arising in the normal course of business. The outcome of individual matters is not predictable. However, management believes that the ultimate resolution of all such matters will not have a material adverse effect on HART's financial position, results of operations, or liquidity.

During the audit period HART was party to various legal proceedings arising in the normal course of business. The ultimate resolution of all such matters did not have a material adverse effect on HART's financial position, results of operations, or liquidity.

HonoluluTraffic.com, et. al. v. Federal Transit Administration, et. al.

In May 2011, a lawsuit was filed in the United States District Court for the District of Hawaii against the Federal Transit Administration (FTA) and the City alleging violations of federal law in approving the City's rail transit project that HART is now responsible for developing, operating, maintaining and expanding. Among other claims, the allegations were that the defendants improperly studied only the first 20 miles of the project and not the full route, that alternatives to the project were not properly considered, that potential native Hawaiian burial sites were not studied prior to the approval of the project and that defendants failed to comply with the federal Department of Transportation Act.

On November 1, 2012, the District Court ruled in favor of the plaintiffs with regard to three matters, and ruled in favor of the defendants in all other respects. The three matters were that the defendants did not adequately analyze above ground traditional cultural properties, they did not adequately support their rejection of an alternative route involving a tunnel underneath Beretania Street and they did not adequately support their determinations regarding the impact of the rail project on Mother Waldron Park. A hearing was held on December 12, 2012 on appropriate remedies, and on December 27, 2012, the court issued a Judgment and Partial Injunction, remanding the matter to the FTA for additional studies and analyses consistent with its findings in the November 2012 order, and enjoining construction and real estate acquisition activities in Section 4 of the project until completion of the additional studies regarding the three matters described above.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE I – LITIGATION (continued)

HonoluluTraffic.com, et. al. v. Federal Transit Administration, et. al.

A study of above-ground traditional cultural properties was completed, and the FTA obtained the concurrence of the State Historic Preservation Officer (SHPO) that there were no previously unidentified eligible traditional cultural properties that would be adversely affected by the project. With respect to the other two matters, on October 8, 2013, the City defendants filed a Notice of Compliance with the District Court, informing the court and all parties that a Final Supplemental Environmental Impact Statement (“FSEIS”) and amended Record of Decision had been completed for the Mother Waldron Park and Beretania Street Tunnel alternative issues, and that the TCP studies (which were incorporated into the FSEIS) had been approved by the SHPO. Plaintiffs challenged the sufficiency of the additional studies. On February 18, 2014, the District Court issued its ruling, affirming that the defendants had fully satisfied the Summary Judgment Order and lifting the partial injunction on construction and real estate acquisition activities in Section 4 of the project.

Separately, the plaintiffs filed an appeal of the District Court’s Judgment and Partial Injunction and other prior rulings in the case to the Ninth Circuit Court of Appeals. The appeal was fully briefed, and oral argument was held in San Francisco on August 15, 2013. On February 18, 2014, the Circuit Court of Appeals issued its decision, affirming the rulings of the District Court in all respects.

Following the issuance of the District Court and the Circuit Court of Appeals decisions, the plaintiffs announced that they were abandoning their legal challenges to the project and would not take any further appeals.

Kaleikini v. Formby et al.

On January 31, 2011, Plaintiff filed a lawsuit in the First Circuit Court of the State of Hawaii, challenging the approval of the Final Environmental Impact Statement (FEIS) as well as other approvals for the City’s rail transit project that HART is now responsible for developing, operating, maintaining and expanding. Plaintiff alleged various State law violations but primarily alleged that an archaeological inventory survey (AIS) had not first been completed for the entire 20-mile project alignment, in violation of State law. Instead, the project was proposed to be built in four sections, with an AIS to be completed for each section prior to any construction taking place in that section. The case involved both City and State of Hawaii defendants.

The Circuit Court granted the City Defendants’ Motion to Dismiss Complaint and/or for Summary Judgment, and denied the Plaintiff’s Motion for Preliminary Injunction and Motion for Reconsideration. In doing so, the Circuit Court determined that the phased approach for AIS completion proposed for the rail project met applicable State law requirements.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE I – LITIGATION (continued)

Kaleikini v. Formby et al. (continued)

Plaintiff then filed an appeal with the ICA, where the matter was fully briefed by all parties. The case was then transferred to the Hawaii Supreme Court. Shortly after the transfer, the Plaintiff-Appellant filed a motion for injunctive relief pending appeal, which the court denied. Oral argument before the Hawaii Supreme Court occurred on May 24, 2012.

On August 24, 2012, the Hawaii Supreme Court vacated the Circuit Court's judgment in favor of the City and State, ruling that the administrative rules implementing HRS §§ 6E-8 and 6E-42 do not permit the State Historic Preservation Division (SHPD) of the Department of Land and Natural Resources to concur in the rail project absent a complete AIS for the entire project. The project had received SHPD approval to conduct separate AISs for each of the four construction phases, with construction proceeding in each phase after completion of the AIS for that phase.

On September 4, 2012, the City Defendants filed a motion to reconsider, modify and/or clarify the Supreme Court's opinion of August 4, 2012. On September 27, 2012, the Supreme Court denied the motion. On October 5, 2012, the Plaintiff filed a request for attorney's fees and costs with the Supreme Court. The State and City Defendants filed oppositions to this request.

Based on the Hawaii Supreme Court's August 2012 decision, ground disturbing construction activities related to the project were halted pending completions of all AIS work or further court rulings. HART continued with property acquisitions (other than those enjoined in the HonoluluTraffic.com case), AIS work and other non-ground disturbing construction activities. HART completed the AIS work and received SHPD's determination letter concurring in the project on August 29, 2013. Construction of the rail project was resumed on September 16, 2013.

While the additional AIS work was being undertaken, the Supreme Court ruled that Plaintiff was entitled to certain fees and costs for the appeal portion of the litigation, and remanded the case to the Circuit Court for further proceedings. The parties entered into a stipulated agreement to resolve remaining issues, and this was approved by the Circuit Court on June 19, 2013. The Circuit Court entered its order of final judgment, officially concluding the case, on February 19, 2014.

HART estimates that the remaining delay claims associated with the above litigation and other delays will cost the Project approximately \$44 - \$90 million.

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE J – ENVIRONMENTAL ISSUES

GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, provided guidance to state and local governments on how to estimate the cost and reporting of pollution remediation. Statement 49 sets forth the following five events and circumstances that would signal that a government should determine if it has to report a remediation liability for potential obligations that they are aware of:

- Pollution poses an imminent danger to the public or environment and a government has little or no discretion to avoid fixing the problem
- A government violates a pollution prevention-related permit or license
- A regulator identifies (or evidence indicates a regulator will identify) a government as responsible (or potentially responsible) for cleaning up pollution, or for paying all or some of the cost of the clean up
- A government is named (or evidence indicates that it will be named) in a lawsuit to compel it to address pollution
- A government begins or legally obligates itself to begin clean up or post-cleanup activities (limited to amounts related to activities the government is legally obligated to complete).

For fiscal year 2014, HART has identified the following sites that meet one of the criteria enumerated above and has estimated the potential remediation liability.

- HART has identified an inactive Air Force / Navy fuel pipeline that is wrapped in asbestos that runs along the Kamehameha Highway guideway alignment. It is estimated that the guideway will cross over the pipeline in 50 locations. The total asbestos remediation cost is estimated to be \$500,000. HART has recorded a liability of \$500,000 related to this remediation action which is included in accrued liabilities in the accompanying statements of net position.
- The property known as the Banana Patch in Waipahu has been found to be contaminated with lead. It is estimated that the remediation cost for the cleanup of the property will be between \$800,000 and \$1,000,000. HART has recorded a liability of \$1,000,000 related to this remediation action which is included in accrued liabilities in the accompanying statements of net position.

Honolulu Authority for Rapid Transportation  
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NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2014 and 2013

NOTE K – SUBSEQUENT EVENTS

On May 20, 2014, HART issued a Request for Sealed Bids, RFB-HRT-708002 for the West Side Station Group with the receipt of bids scheduled for August 13, 2014. HART received three timely bids on August 13, 2014. The bids prices proposed were as follows:

<b>Bidder</b>	<b>Bid Price Proposal</b>
Nan Inc.	\$294,459,000
Nordic PCL	\$312,310,905
Hensel Phelps	\$320,764,000

HART's contract budget for this project was \$151,545,223, and HART's latest independent cost estimate for the project was \$181,610,756. After evaluation of the bid proposals, HART's Chief Procurement Officer (CPO) determined that it was in the public's best interest to cancel the solicitation and resolicit the bid, since the bid proposals significantly exceeded HART's contract budget and the independent cost estimate. The CPO issued the notice of cancellation on September 9, 2014.

On September 15, 2014, Nan Inc. ("Nan") protested HART's cancellation, arguing in summary that: (1) HART's sole justification for cancellation of the RFB focused on assertions that are factually and legally incorrect; (2) HART's stated rationale supporting its decision to cancel this RFB and resolicit the project in a subsequent solicitation or multiple solicitations lacks a reasonable/rational basis; and (3) HART abused its discretion by failing to negotiate with Nan to reduce the scope of the project to come within HART's available funding.

HART's CPO issued his determination on September 30, 2014, denying Nan's protest. In summary, HART's denial provided that: (1) HART was authorized to cancel the RFB because it was in HART's and the public's interest to do so; (2) HART's decision to cancel was reasonable and was not prejudicial; (3) HART was not obligated to negotiate with Nan prior to cancelling the RFB; and (4) Nan failed to demonstrate that it was an "aggrieved" party who has standing to bring a protest of the cancellation as it was not likely to be awarded the contract.

On October 9, 2014, Nan sent its response to HART's denial of Nan's protest, stating that "Nan has decided to withdraw" the protest.

**PART II**  
**SUPPLEMENTARY INFORMATION**

Honolulu Authority for Rapid Transportation  
(a component unit of the City and County of Honolulu)

SCHEDULE OF FUNDING PROGRESS

June 30, 2014

Actuarial valuation date	Actuarial value of assets	Actuarial accrued liability (AAL)	Unfunded AAL (UAAL)	Funded ratio	Covered payroll	UAAL as a percentage of covered payroll
July 1, 2013	9,000	\$ 3,413,000	\$ 3,404,000	0.3%	\$ 6,760,000	50.4%
July 1, 2011	-	\$ 1,964,000	\$ 1,964,000	0.0%	\$ 5,385,000	36.5%

Note: OPEB Actuarial Valuation is issued once every two years. Additionally, the OPEB RSI should disclose three years of valuations. As the HART was formed on July 1, 2011, there is only two years of valuation information available. Accordingly, for 2014, the disclosure of the actuarial valuation will be limited to information for July 1, 2011 and 2013.

**PART III**  
**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**  
**AND ON COMPLIANCE AND OTHER MATTERS**



A Hawaii Limited Liability Partnership

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

**Independent Auditor's Report**

To the Board of Directors  
Honolulu Authority for Rapid Transportation  
City and County of Honolulu

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 Honolulu Authority for Rapid Transportation (HART), as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise HART's basic financial statements, and have issued our report thereon dated December 18, 2014.

**Internal Control over Financial Reporting**

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

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

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

**Compliance and Other Matters**

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

**Purpose of this Report**

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

KMH LLP

KMH LLP

Honolulu, Hawaii  
December 18, 2014