



Office of the City Auditor



**City and County of
Honolulu
State of Hawai`i**

**City and County of Honolulu
Public Transportation System
Bus and Paratransit Operations**

**Financial Statements and Supplemental Schedules
June 30, 2017 and 2016**

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A Hawaii Limited Liability Partnership

Independent Auditor's Report

To the Chair and Members of the City Council
City and County of Honolulu

Report on the Financial Statements

We have audited the accompanying financial statements of the City and County of Honolulu, Public Transportation System – Bus and Paratransit Operations (Bus and Paratransit Operations) as of and for the years ended June 30, 2017 and 2016, and the related notes to the 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 Bus and Paratransit Operations as of June 30, 2017 and 2016, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Bus and Paratransit Operations and do not purport to, and do not, present fairly the financial position of the City and County of Honolulu as of June 30, 2017 and 2016, and the changes in its financial position or, where applicable, its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements of the Bus and Paratransit Operations. The supplementary schedules consisting of 1) detailed schedules of net position as of June 30, 2017 and 2016 and 2) detailed schedules of revenues, expenses and changes in net position for the years ended June 30, 2017 and 2016, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The supplementary schedules 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. The information as of and for the years ended June 30, 2017 and 2016 have been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary schedules as of and for the years ended June 30, 2017 and 2016 are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

KMH LLP

KMH LLP

Honolulu, Hawaii
December 8, 2017

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Management’s Discussion and Analysis
June 30, 2017 and 2016

This section of the City and County of Honolulu, Public Transportation System – Bus and Paratransit Operations (Bus and Paratransit Operations) financial report presents the reader with an introduction and overview of the Bus and Paratransit Operations’ financial performance during the fiscal year ended June 30, 2017. Please read it in conjunction with the Bus and Paratransit Operations’ financial statements, which follows this section.

The City and County of Honolulu public transportation system plays a vital role in Hawaii’s economy as the primary means of public transportation on the island of Oahu. The Bus Operations unit (TheBus) provides regular bus services to the public, and the Paratransit Operations unit (Handi-Van) provides van transportation services for those people who cannot readily use the bus services.

Financial Highlights

- The Bus and Paratransit Operations’ net position increased by \$2.1 million or 1% in fiscal year 2017. The term “net position” refers to the difference between assets and liabilities.
- Operating revenues decreased by \$1.4 million or 3% from the prior fiscal year.
- Transfers and contributions decreased by \$12.9 million or 7% from the prior fiscal year.
- Total expenses for the fiscal year 2017 increased by approximately \$5.4 million or 2% compared to the prior fiscal year.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to TheBus and Handi-Van financial statements, which is comprised of the basic financial statements, notes to the financial statements and supplemental schedules. The basic financial statements are designed to provide readers with a broad overview of TheBus and Handi-Van’s finances, in a manner similar to a private-sector business.

The statements of net position present information of TheBus’ and Handi-Van’s assets and liabilities, with the difference reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of TheBus and Handi-Van is improving or deteriorating. Net position increases when revenues and subsidies exceed expenses. Increases to assets, without a corresponding increase to liabilities, results in increased net position, which indicate an improved financial position.

The statements of revenues, expenses and changes in net position present information showing how TheBus’ and Handi-Van’s net position changed during the past two fiscal years. All changes in net position are reported as soon as the underlying event occurs, regardless of timing of related cash flows.

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Management’s Discussion and Analysis
June 30, 2017 and 2016

Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods.

The statements of cash flows report cash receipts, cash payments, and net changes in cash resulting from operations, investing, noncapital financing and capital financing activities. The notes to financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

In addition to the basic financial statements and accompanying notes to financial statements, this report also presents the detailed statements of net position and operations for the separate balances and transactions for TheBus and Handi-Van as of and for the years ended June 30, 2017 and 2016.

Financial Analysis

A condensed summary of the Bus and Paratransit Operations’ net position at June 30, 2017, 2016 and 2015 is shown below:

Table 1
Condensed Statements of Net Position
(in thousands of dollars)

	2017	2016	2015
Current and other assets	\$ 32,370	\$ 30,383	\$ 29,401
Restricted assets	552	716	319
Capital assets, net	<u>216,610</u>	<u>217,053</u>	<u>194,331</u>
Total assets	<u>249,532</u>	<u>248,152</u>	<u>224,051</u>
Current liabilities	9,669	10,412	9,264
Noncurrent liabilities	<u>18,141</u>	<u>18,142</u>	<u>16,919</u>
Total liabilities	<u>27,810</u>	<u>28,554</u>	<u>26,183</u>
Net position			
Invested in capital assets	216,610	217,053	194,331
Unrestricted	<u>5,112</u>	<u>2,545</u>	<u>3,537</u>
Total net position	<u>\$ 221,722</u>	<u>\$ 219,598</u>	<u>\$ 197,868</u>

City and County of Honolulu Public Transportation System – Bus and Paratransit Operations

Management’s Discussion and Analysis
June 30, 2017 and 2016

The total assets exceed liabilities by approximately \$221.7 million, \$219.6 million, and \$197.9 million at June 30, 2017, 2016, and 2015, respectively. Net position increased by approximately \$2.1 million or 1% from June 30, 2016, and increased by approximately \$21.7 million or 10.9% from June 30, 2015. The largest portion of the Bus and Paratransit Operations’ net position represents its investment in capital assets (e.g., buses, paratransit vans, buildings, maintenance equipment, etc.). The Bus and Paratransit Operations use these capital assets to provide services to the users of the public transportation system; consequently, these assets are not available to liquidate liabilities or for future spending.

A summary of operations and changes in net position for the fiscal years ended June 30, 2017, 2016 and 2015 follows:

Table 2
Condensed Statements of Revenues, Expenses and Changes in Net Position
(in thousands of dollars)

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Operating revenues	\$ 53,833	\$ 55,253	\$ 57,022
Total revenues	<u>53,833</u>	<u>55,253</u>	<u>57,022</u>
Depreciation	18,870	17,668	14,870
Other operating expenses	235,833	231,618	230,309
Nonoperating expenses	<u>229</u>	<u>346</u>	<u>71</u>
Total expenses	<u>254,932</u>	<u>249,632</u>	<u>245,250</u>
Loss before transfers and contributions	(201,099)	(194,379)	(188,228)
Transfers and contributions	<u>203,225</u>	<u>216,109</u>	<u>195,152</u>
Change in net position	<u>\$ 2,126</u>	<u>\$ 21,730</u>	<u>\$ 6,924</u>

The changes in net position are an indicator of whether the overall fiscal condition of the Bus and Paratransit Operations improved or declined during the fiscal year. The total net position may serve over time as a useful indicator of the Bus and Paratransit Operations’ financial position.

City and County of Honolulu Public Transportation System – Bus and Paratransit Operations

Management’s Discussion and Analysis
June 30, 2017 and 2016

Capital Asset and Debt Administration

As of June 30, 2017, the Bus and Paratransit Operations had approximately \$217 million invested in capital assets as shown in Table 3. There was a net decrease (additions, deductions and depreciation) of approximately \$0.4 million or 0.2% and net increase of approximately \$22.7 million or 11.7% for the fiscal years ended June 30, 2017 and 2016, respectively.

Table 3
Capital Assets
(in thousands of dollars)

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Buses	\$ 262,811	\$ 257,409	\$ 229,542
Buildings and improvements	85,576	85,466	84,916
Shop and office equipment	28,941	28,230	28,645
Paratransit vans	19,663	19,698	19,748
Automobiles and trucks	<u>3,295</u>	<u>3,117</u>	<u>3,033</u>
	400,286	393,920	365,884
Less: Accumulated depreciation	<u>238,416</u>	<u>231,369</u>	<u>225,723</u>
	161,870	162,551	140,161
Land	53,985	53,985	53,985
Construction in progress	<u>755</u>	<u>517</u>	<u>185</u>
Total	<u>\$ 216,610</u>	<u>\$ 217,053</u>	<u>\$ 194,331</u>

Major capital asset additions and disposals to the public transportation system for the fiscal year ended June 30, 2017, included the following:

- Acquisition of 18 diesel buses for \$9.9 million.
- Acquisition of 8 hybrid buses for \$5.7 million.
- Disposal of older buses, Paratransit vans, automobiles and trucks, and equipment with an original cost of \$11.9 million resulting in related losses of \$71,000.

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Management's Discussion and Analysis
June 30, 2017 and 2016

Currently Known Facts, Decisions, or Conditions

Oahu Transit Services, Inc. (OTS) manages, operates and maintains the Bus and Paratransit Operations on behalf of the City and County of Honolulu. The management agreement between the City and County of Honolulu and OTS provides for the payment of \$117,130 per quarter beginning with the quarter ended September 30, 2010 until a new management and operations agreement is executed.

The collective bargaining agreement between OTS, for its bus operations, and the Hawaii Teamsters and Allied Workers Union, Local 996, is effective from July 1, 2013 through June 30, 2018. The collective bargaining agreement between OTS, for its paratransit operations, and the Hawaii Teamsters and Allied Workers Union, Local 996, is effective from April 1, 2015 through March 31, 2020.

Request for Information

The financial report is designed to provide a general overview of the Bus and Paratransit Operations' finances for all interested parties. Questions concerning any of the information provided in this report or requests for additional information should be addressed in writing to the City and County of Honolulu, Department of Transportation Services.

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Statements of Net Position
June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ 20,493,608	\$ 18,910,949
Accounts receivable	1,678,483	1,792,590
Advance to Oahu Transit Services, Inc.	487,980	788,182
Parts, supplies and fuel inventories	9,364,953	8,829,619
Other assets	<u>345,252</u>	<u>61,889</u>
Total current assets	32,370,276	30,383,229
Restricted Assets Held by Oahu Transit Services, Inc.	552,217	716,170
Capital Assets, net	<u>216,610,162</u>	<u>217,053,103</u>
Total assets	<u>\$ 249,532,655</u>	<u>\$ 248,152,502</u>
Liabilities and Net Position		
Current Liabilities		
Unearned revenue	\$ 952,728	\$ 1,010,954
Reserve for insurance claims payable	<u>9,707,790</u>	<u>9,402,020</u>
Total current liabilities	10,660,518	10,412,974
Reserve for Insurance Claims Payable, noncurrent	<u>17,149,486</u>	<u>18,141,392</u>
Total liabilities	<u>27,810,004</u>	<u>28,554,366</u>
Commitments and Contingencies		
Net Position		
Invested in capital assets	216,610,162	217,053,103
Unrestricted	<u>5,112,489</u>	<u>2,545,033</u>
Total net position	<u>221,722,651</u>	<u>219,598,136</u>
Total liabilities and net position	<u>\$ 249,532,655</u>	<u>\$ 248,152,502</u>

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

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Statements of Revenues, Expenses and Changes in Net Position
Years Ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Operating Revenues		
Passenger fares for transit services	\$ 53,510,671	\$ 54,914,493
Nontransportation revenue	<u>322,070</u>	<u>338,190</u>
Total operating revenues	<u>53,832,741</u>	<u>55,252,683</u>
Operating Expenses		
Contract services	178,267,255	172,851,207
Insurance	12,516,375	17,272,149
Fuel and lubricants	13,178,252	12,409,931
Depreciation	18,870,089	17,668,269
Materials and supplies	15,593,366	13,863,864
Outside services	11,487,420	11,005,669
State fuel taxes	2,912,283	2,963,808
Utilities, rentals and others	<u>1,878,131</u>	<u>1,250,945</u>
Total operating expenses	<u>254,703,171</u>	<u>249,285,842</u>
Loss from operations	<u>(200,870,430)</u>	<u>(194,033,159)</u>
Nonoperating Income (Expense)		
Noncapital contributions	21,000,000	21,000,000
Loss on disposal of parts and supplies	(158,293)	(289,903)
Loss on disposal of capital assets	<u>(71,431)</u>	<u>(55,810)</u>
Total nonoperating income	<u>20,770,276</u>	<u>20,654,287</u>
Loss before transfers and capital contributions	(180,100,154)	(173,378,872)
Transfers	166,067,887	156,214,210
Capital Contributions	<u>16,156,782</u>	<u>38,894,345</u>
Changes in net position	2,124,515	21,729,683
Net Position		
Beginning of year	<u>219,598,136</u>	<u>197,868,453</u>
End of year	<u>\$ 221,722,651</u>	<u>\$ 219,598,136</u>

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

City and County of Honolulu Public Transportation System – Bus and Paratransit Operations

Statements of Cash Flows
Years Ended June 30, 2017 and 2016

	2017	2016
Cash Flows From Operating Activities		
Cash received from passengers	\$ 53,566,552	\$ 54,788,670
Cash paid to suppliers and others	(138,124,488)	(130,943,140)
Cash paid to reimburse Oahu Transit Services, Inc. for its employees	(98,749,448)	(97,501,027)
Net cash used in operating activities	(183,307,384)	(173,655,497)
Cash Flows From Noncapital Financing Activity --		
Transfers and noncapital contributions	187,067,887	177,214,210
Cash Flows From Capital and Related Financing Activity --		
Purchases of capital assets	(2,341,797)	(1,551,437)
Net increase in cash and cash equivalents	1,418,706	2,007,276
Cash and Cash Equivalents		
Beginning of year	19,627,119	17,619,843
End of year (including \$552,217 and \$716,170 in restricted assets in 2017 and 2016, respectively)	\$ 21,045,825	\$ 19,627,119
Reconciliation of Loss from Operations to Net Cash Used In Operating Activities		
Loss from operations	\$ (200,870,430)	\$ (194,033,159)
Adjustments to reconcile loss from operations to net cash used in operating activities:		
Depreciation	18,870,089	17,668,269
Loss on disposal of parts and supplies	(158,293)	(289,903)
Changes in assets and liabilities		
Accounts receivable and advance to Oahu Transit Services	414,309	1,153,768
Parts, supplies, fuel inventories and other current assets	(818,697)	(525,534)
Reserve for insurance claims payable	(686,136)	2,597,993
Unearned revenue	(58,226)	(226,931)
Net cash used in operating activities	\$ (183,307,384)	\$ (173,655,497)
Supplemental Disclosure of Noncash Activities		
Contribution of Capital Assets from the Federal Transit Administration and City	\$ 16,156,782	\$ 38,894,345
Loss on Disposal of Capital Assets	\$ 71,431	\$ 55,810

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

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

1. Financial Reporting Entity

The Department of Transportation Services (DTS) of the City and County of Honolulu (City) oversees the operations of the City bus and paratransit systems. As discussed in Note 3, the City selected Oahu Transit Services, Inc. (OTS), a nonprofit organization, to manage, operate and maintain the City bus and paratransit systems as an instrumentality of the City, except for labor. The accompanying financial statements present only the accounts maintained by OTS in managing the City's Public Transportation System – Bus and Paratransit Operations (Bus and Paratransit Operations) and do not include other organizations, departments, activities, and/or functions of the City. The accompanying financial statements are not intended to present fairly the financial position of the City, and the changes in its financial position and cash flows of its proprietary funds in accordance with accounting principles generally accepted in the United States of America.

Chapter 13 of the Revised Ordinance of the City effectuated the formation of OTS to serve as the transit management services contractor. OTS' Board of Directors (Board) selects new members to fill vacancies on the Board, subject to City approval. The City may remove any director when the City determines that the removal is required to fulfill the best interest of the city bus and paratransit system. As a result, OTS is reported as a discretely-presented component unit of the City.

The collective bargaining agreements between OTS, for its bus operations, and the Hawaii Teamsters and Allied Workers Union, Local 996, are effective from July 1, 2013 through June 30, 2018. The collective bargaining agreements between OTS, for its paratransit operations, and the Hawaii Teamsters and Allied Workers Union, Local 996, are effective from April 1, 2015 through March 31, 2020 and April 1, 2016 through March 31, 2019.

2. Summary of Significant Accounting Policies

a. Basis of Accounting

The accounting policies of the Bus and Paratransit Operations conform to generally accepted accounting principles as applicable to enterprise activities of governmental units as promulgated by the Governmental Accounting Standards Board (GASB). In accordance with GASB standards, the City has elected not to apply the Financial Accounting Standards Board (FASB) pronouncements on accounting and financial reporting that were issued after November 30, 1989.

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

2. Summary of Significant Accounting Policies (continued)

a. Basis of Accounting (continued)

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

Operating revenues and expenses are distinguished from nonoperating items. Operating revenues and expenses generally result from providing services in connection with the City's bus and paratransit systems.

The principal operating revenues are from charges for passenger fares, while operating expenses include cost of services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

b. Use of Estimates

The preparation of financial statements in accordance 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 disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions includes management's estimates of uncollectible accounts and reserve for insurance claims payable. Actual results could differ from those estimates.

c. Cash and Cash Equivalents

The Bus and Paratransit Operations consider all cash on hand, demand deposits and short-term investments (including restricted assets) with original maturities of three months or less from the date of acquisition to be cash and cash equivalents.

d. Accounts Receivables

Accounts receivable consists primarily of amounts due from third parties who purchase transportation services. Accounts are written off when it is determined, after considering economic conditions, business conditions and collection efforts, that the accounts are uncollectible. Management considers all accounts receivable as of June 30, 2017 and 2016 to be fully collectible. Accordingly, no allowance for doubtful accounts has been established.

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

2. Summary of Significant Accounting Policies (continued)

e. Parts, Supplies and Fuel Inventories

Inventories of parts, supplies and fuel are stated at weighted average cost. Inventories are written off when management determines that such items are obsolete or unusable.

f. Capital Assets

Capital assets with an initial, individual cost of \$5,000 or more for equipment and \$100,000 for buildings, structures and infrastructure, and an estimated life of more than one year are capitalized. All acquired property and equipment are recorded at cost. Those assets transferred to the Bus and Paratransit Operations from the various departments or agencies of the City are recorded at the net book value at date of transfer. Upon retirement or disposal of capital assets, the remaining net book value is charged to nonoperating expense.

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

	<u>Years</u>
Buildings and improvements	30 – 40
Buses	7 – 12
Paratransit vans	5
All other assets	5 – 15

g. Unearned Revenue

Revenues from bus vouchers are recognized upon redemption. Revenues from annual and two-year bus passes are deferred until the applicable period has passed.

h. Net Position

Net position comprises the various net earnings (loss) from operating and nonoperating revenues, expenses, transfers and contributions. Net position is classified in the following components: invested in capital assets and unrestricted net position. Invested in capital assets consists of capital assets, net of accumulated depreciation. Unrestricted net position consists of all other net position not categorized as invested in capital assets. When both restricted and unrestricted resources are available for use, generally, it is management's policy to use restricted resources first, then unrestricted resources as they are needed.

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

2. Summary of Significant Accounting Policies (continued)

i. Revenue and Expenses

Revenue collected by OTS, except for management fees, is the property of the City and is remitted to a depository controlled by the City. Generally, OTS is reimbursed by the City for all expenses paid by OTS in managing and operating the bus and paratransit systems.

j. Risk Management

The Bus and Paratransit Operations is exposed to various risks for losses related to torts; theft of, 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 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. For the prior and current fiscal years, the City maintained risk property insurance covering all real and personal property of the City, including the structures, equipment, inventory and vehicles owned by the City and provided to OTS to operate and manage the transit system for the City. This master policy provided \$300 million in blanket limits, subject to a general deductible of \$75,000 and various deductibles for the perils of earthquake, flood and hurricane. In addition, this policy provided \$50 million in sublimits for Garaged Licensed Vehicles, subject to a \$1 million limit for any one vehicle.

k. Transfers

The City provides assistance to fund the Bus and Paratransit Operations and OTS through transfers. The source of such funding is subject to the availability of appropriations from the City Council, City and County of Honolulu.

l. Contributions

Contributions from the City for capital assets (primarily buses and vans) that were funded by federal and local grants are recognized when the assets or resources are received.

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

2. Summary of Significant Accounting Policies (continued)

m. Adopted Accounting Pronouncements

In November 2016, GASB issued Statement No. 83 (GASB 83), *Certain Asset Retirement Obligations (ARO)*. GASB 83 establishes standards of accounting and financial reporting for certain AROs. The requirements of this Statement apply to financial statements of all state and local governments. The provisions of GASB 83 are effective for periods beginning after June 15, 2018. Earlier adoption is encouraged. Management has not yet determined the effect this Statement will have on the financial statements.

3. Management and Operations Agreement

OTS has an agreement with the City to manage the City bus system and the City special transit service (Paratransit). OTS provides the employees to operate and manage the bus and paratransit systems. Under the agreement, the City reimburses OTS for operating expenses incurred for salaries and wages, employee benefits (including vacation, sick leave and employee benefit plan costs), professional and consulting fees, materials, supplies and services, and all other operating expenses attributable to the bus and paratransit systems included in the annual budgeting process. Contract services reported on the statements of revenues, expenses and change in net position include reimbursements paid to OTS for labor and fringe benefits. The agreement provided for the City to pay OTS an annual management fee of approximately \$469,000 and \$487,000 for the fiscal years ended June 30, 2017 and 2016, respectively.

The current agreement with the City provides for the City to pay OTS approximately \$117,000 per quarter beginning with the quarter ended September 30, 2010 until a new management and operations agreement is executed. For the year ended June 30, 2016, a one-time additional \$18,740 was added to the management agreement. The agreement provides that the City furnish and retain title to the transit buses, paratransit vans, properties, facilities and equipment used in the transit system.

In accordance with the aforementioned agreement with OTS and governing ordinances, management believes that the City and Bus and Paratransit Operations are liable only for reimbursable employee benefit costs approved by the City's annual budgeting process. Accordingly, the City's and Bus and Paratransit Operations' 2017 and 2016 financial statements only include costs related to employee benefits which are currently reimbursable. Any long term liabilities related to OTS' employee benefits have not been recorded in the accompanying financial statements. If the agreement with OTS is cancelled, the City may have a contingent liability, related to OTS' long term employee benefits. However, the City has no plans to do so; therefore, the City and Bus and Paratransit Operations has not recorded a contingent liability.

City and County of Honolulu

Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

4. Cash and Cash Equivalents

The cash balances reported in the accompanying statements of net position are included in the City's cash and investment pool. Specific information pertaining to bank and invested balances, classification of credit risk, and interest rate risk is available for only the total cash and investment pool.

State statutes authorize the City to invest in obligations of the U.S. Treasury and U.S. agencies, obligations and other states, cities, and counties, mutual funds and bank repurchase agreements. Investments in repurchase agreements are primarily U.S. government and federal agency securities. The City structures its investment portfolio so that securities mature to meet cash requirements for ongoing operations avoiding the need to sell securities on the open market prior to maturity. This practice decreases the City's exposure to risk caused by fluctuation of interest rates.

5. Restricted Assets Held by OTS

OTS, the trustor, maintains trust funds for the purpose of maintaining adequate funds for expenses incurred through the City's workers' compensation, general and automotive liability self-insurance programs. Pursuant to the trust agreement, the trustee is required to invest the funds in either interest-bearing bonds, notes or obligations of the United States. All income realized from the investments reverts to the trust fund. Upon termination of the trust fund, all assets of the trust fund will be distributed to the City subject to certain limitations as described in the trust agreement. Payments for self-insured workers' compensation, general and automotive liability claims are made from the trust fund subject to certain limitations as described in the trust agreement.

Restricted assets as of June 30, 2017 and 2016 consisted of the following and were uninsured and uncollateralized:

	<u>2017</u>	<u>2016</u>
Cash	\$ 395,558	\$ 671,725
Money market mutual fund	<u>156,659</u>	<u>44,445</u>
	<u>\$ 552,217</u>	<u>\$ 716,170</u>

City and County of Honolulu Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

6. Capital Assets

The changes in capital assets were as follows:

	Balance July 1, 2016	Additions	Retirements/ Transfers	Balance June 30, 2017
Buses	\$ 257,409,461	\$ 15,557,285	\$ (10,114,087)	\$ 262,852,659
Buildings and improvements	85,466,148	110,214	-	85,576,362
Shop and office equipment	28,229,738	858,080	(167,264)	28,920,554
Paratransit vans	19,697,612	1,303,376	(1,338,337)	19,662,651
Automobiles and trucks	3,116,662	431,483	(274,895)	3,273,250
	393,919,621	18,260,438	(11,894,583)	400,285,476
Less: Accumulated depreciation	<u>(231,368,645)</u>	<u>(18,870,089)</u>	<u>11,823,152</u>	<u>(238,415,582)</u>
	162,550,976	(609,651)	(71,431)	161,869,894
Land	53,985,443	-	-	53,985,443
Capital assets to be placed in service	<u>516,684</u>	<u>754,825</u>	<u>(516,684)</u>	<u>754,825</u>
Capital assets, net	<u>\$ 217,053,103</u>	<u>\$ 145,174</u>	<u>\$ (588,115)</u>	<u>\$ 216,610,162</u>

	Balance July 1, 2015	Additions	Retirements/ Transfers	Balance June 30, 2016
Buses	\$ 229,541,461	\$ 38,433,089	\$ (10,565,089)	\$ 257,409,461
Buildings and improvements	84,916,042	550,106	-	85,466,148
Shop and office equipment	28,645,175	916,860	(1,332,297)	28,229,738
Paratransit vans	19,747,876	-	(50,264)	19,697,612
Automobiles and trucks	3,033,149	214,250	(130,737)	3,116,662
	365,883,703	40,114,305	(12,078,387)	393,919,621
Less: Accumulated depreciation	<u>(225,722,953)</u>	<u>(17,668,269)</u>	<u>12,022,577</u>	<u>(231,368,645)</u>
	140,160,750	22,446,036	(55,810)	162,550,976
Land	53,985,443	-	-	53,985,443
Capital assets to be placed in service	<u>185,207</u>	<u>1,194,107</u>	<u>(862,630)</u>	<u>516,684</u>
Capital assets, net	<u>\$ 194,331,400</u>	<u>\$ 23,640,143</u>	<u>\$ (918,440)</u>	<u>\$ 217,053,103</u>

Depreciation expense was \$18,870,089 and \$17,668,269 for the fiscal years ended June 30, 2017 and 2016, respectively.

City and County of Honolulu Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

7. Reserve for Insurance Claims Payable

The City sponsors an automotive and general liability self-insurance program for OTS. This self-insurance program is for claims up to \$2 million effective July 1, 2006. The City also has a workers' compensation self-insurance program, which covers OTS claims up to \$1 million per occurrence effective July 1, 2002. OTS has obtained excess insurance coverage for general liability and automotive claims and workers' compensation through various insurance companies for amounts in excess of claims covered under the two self-insurance programs. The amounts payable for claims incurred and claims incurred but not reported for the fiscal years ended June 30, 2017 and 2016, were as follows:

	Balance			Balance	Amounts
	July 1, 2016	Incurred	Payments	June 30, 2017	Due Within
					One Year
Automotive and general liability	\$ 8,072,356	\$ 4,063,376	\$ (3,520,040)	\$ 8,615,692	\$ 2,614,737
Workers' compensation	19,471,056	8,547,371	(9,776,843)	18,241,584	7,093,053
Reserve for insurance claims payable	<u>\$ 27,543,412</u>	<u>\$ 12,610,747</u>	<u>\$ (13,296,883)</u>	<u>\$ 26,857,276</u>	<u>\$ 9,707,790</u>

	Balance			Balance	Amounts
	July 1, 2015	Incurred	Payments	June 30, 2016	Due Within
					One Year
Automotive and general liability	\$ 8,966,931	\$ 5,523,071	\$ (6,417,646)	\$ 8,072,356	\$ 6,670,721
Workers' compensation	15,978,488	11,935,804	(8,443,236)	19,471,056	2,731,299
Reserve for insurance claims payable	<u>\$ 24,945,419</u>	<u>\$ 17,458,875</u>	<u>\$ (14,860,882)</u>	<u>\$ 27,543,412</u>	<u>\$ 9,402,020</u>

The OTS workers' compensation loss and allocated loss adjustment expense (ALAE) reserve as of June 30, 2017 for accidents occurring from March 1, 1998 to June 30, 2017 is estimated to be \$18.2 million on an undiscounted basis and \$16.0 million on a discounted basis (discounted at 4.5%). The OTS automotive and general liability loss and ALAE reserve as of June 30, 2017 for accidents occurring from January 1, 2000 through June 30, 2017 is estimated to be \$8.6 million on an undiscounted basis and \$7.8 million on a discounted basis (discounted at 4.5%). The actuarially determined reserve estimates are based on data net of subrogation and salvage and net of excess insurance. They include the third party administrator fee for workers' compensation. Determination of a reserve amount for workers' compensation and automotive and general liability claims is a significant estimate. It is reasonably possible that one or more future events could result in material change in the estimated claim losses in the near term.

City and County of Honolulu Public Transportation System – Bus and Paratransit Operations

Notes to Financial Statements
June 30, 2017 and 2016

8. Transfers and Contributions

The Bus and Paratransit Operations receive significant support for operations from the City and the Federal Transit Administration. Transfers from the City totaled approximately \$166.0 million and \$156.2 million for the fiscal years ended June 30, 2017 and 2016, respectively. In addition, capital and noncapital contributions for the fiscal years ended June 30, 2017 and 2016 were as follows:

	2017	2016
Federal capital contributions	\$ 12,931,400	\$ 29,993,353
City capital contributions	3,225,382	8,900,992
Total capital contributions	\$ 16,156,782	\$ 38,894,345
 Total noncapital contributions -		
FTA preventative maintenance funds	\$ 21,000,000	\$ 21,000,000

9. Litigation

OTS and the City are involved in various lawsuits arising from the normal operations of the Bus and Paratransit Operations. Claims for punitive damages related to certain lawsuits may not be covered by insurance. As provided in the management agreement with the City, the City indemnifies OTS from any and all claims made against OTS and the City for legal liability, damages and injuries where such claims are reasonably related to the providing of mass transportation services.

Supplemental Schedules

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Supplemental Schedule – Detailed Statement of Net Position
June 30, 2017

	<u>Bus Operations</u>	<u>Paratransit Operations</u>	<u>Eliminations</u>	<u>Total</u>
Assets				
Current assets				
Cash and cash equivalents	\$ 20,493,008	\$ 600	\$ -	\$ 20,493,608
Accounts receivable	1,660,702	17,781	-	1,678,483
Advance to Oahu Transit Services, Inc. for accrued expenses	487,980	-	-	487,980
Parts, supplies and fuel inventories	8,994,987	369,966	-	9,364,953
Other current assets	79,265	265,987	-	345,252
Inter-unit receivables	45,943,434	-	(45,943,434)	-
Total current assets	77,659,376	654,334	(45,943,434)	32,370,276
Restricted assets held by Oahu Transit Services, Inc.	552,217	-	-	552,217
Capital assets, net	195,230,451	21,379,711	-	216,610,162
Total assets	<u>\$ 273,442,044</u>	<u>\$ 22,034,045</u>	<u>\$ (45,943,434)</u>	<u>\$ 249,532,655</u>

See independent auditor's report.

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Supplemental Schedule – Detailed Statement of Net Position (continued)
 June 30, 2017

	<u>Bus Operations</u>	<u>Paratransit Operations</u>	<u>Eliminations</u>	<u>Total</u>
Liabilities and Net Position				
Current liabilities				
Accounts payable	\$ -	\$ -	\$ -	\$ -
Inter-unit payables	-	45,943,434	(45,943,434)	-
Unearned revenue	952,728	-	-	952,728
Reserve for insurance claims payable	<u>9,707,790</u>	<u>-</u>	<u>-</u>	<u>9,707,790</u>
Total current liabilities	10,660,518	45,943,434	(45,943,434)	10,660,518
Reserve for insurance claims payable, noncurrent	<u>17,149,486</u>	<u>-</u>	<u>-</u>	<u>17,149,486</u>
Total liabilities	<u>27,810,004</u>	<u>45,943,434</u>	<u>(45,943,434)</u>	<u>27,810,004</u>
Net position				
Invested in capital assets	195,230,451	21,379,711	-	216,610,162
Unrestricted	<u>50,401,589</u>	<u>(45,289,100)</u>	<u>-</u>	<u>5,112,489</u>
Total net position	<u>245,632,040</u>	<u>(23,909,389)</u>	<u>-</u>	<u>221,722,651</u>
Total liabilities and net position	<u>\$ 273,442,044</u>	<u>\$ 22,034,045</u>	<u>\$ (45,943,434)</u>	<u>\$ 249,532,655</u>

See independent auditor's report.

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Supplemental Schedule – Detailed Statement of Net Position
June 30, 2016

	<u>Bus Operations</u>	<u>Paratransit Operations</u>	<u>Eliminations</u>	<u>Total</u>
Assets				
Current assets				
Cash and cash equivalents	\$ 18,910,349	\$ 600	\$ -	\$ 18,910,949
Accounts receivable	1,776,924	15,666	-	1,792,590
Advance to Oahu Transit Services, Inc. for accrued expenses	788,182	-	-	788,182
Parts, supplies and fuel inventories	8,433,240	396,379	-	8,829,619
Other assets	61,889	-	-	61,889
Intercompany receivables	43,649,005	-	(43,649,005)	-
Total current assets	73,619,589	412,645	(43,649,005)	30,383,229
Restricted assets held by Oahu Transit Services, Inc.	716,170	-	-	716,170
Capital assets, net	194,332,031	22,721,072	-	217,053,103
Total assets	<u>\$ 268,667,790</u>	<u>\$ 23,133,717</u>	<u>\$ (43,649,005)</u>	<u>\$ 248,152,502</u>

See independent auditor's report.

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Supplemental Schedule – Detailed Statement of Net Position (continued)
 June 30, 2016

	Bus Operations	Paratransit Operations	Eliminations	Total
Liabilities and Net Position				
Current liabilities				
Intercompany payables	\$ -	\$ 43,649,005	\$ (43,649,005)	\$ -
Unearned revenue	1,010,954	-	-	1,010,954
Reserve for insurance claims payable	9,402,020	-	-	9,402,020
Total current liabilities	10,412,974	43,649,005	(43,649,005)	10,412,974
Reserve for insurance claims payable, noncurrent	18,141,392	-	-	18,141,392
Total liabilities	28,554,366	43,649,005	(43,649,005)	28,554,366
Net position				
Invested in capital assets	194,332,031	22,721,072	-	217,053,103
Unrestricted	45,781,393	(43,236,360)	-	2,545,033
Total net position	240,113,424	(20,515,288)	-	219,598,136
Total liabilities and net position	\$ 268,667,790	\$ 23,133,717	\$ (43,649,005)	\$ 248,152,502

See independent auditor's report.

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Supplemental Schedule – Detailed Statement of Revenues, Expenses and Changes in Net Position
Year Ended June 30, 2017

	Bus Operations	Paratransit Operations	Eliminations	Total
Operating Revenues				
Passenger fares for transit services	\$ 51,441,589	\$ 2,069,082	\$ -	\$ 53,510,671
Nontransportation revenue	288,676	33,394	-	322,070
Total operating revenues	<u>51,730,265</u>	<u>2,102,476</u>	<u>-</u>	<u>53,832,741</u>
Operating Expenses				
Contract services	144,965,979	33,301,276	-	178,267,255
Insurance	10,185,729	2,330,646	-	12,516,375
Fuel and lubricants	11,143,909	2,034,343	-	13,178,252
Depreciation	15,832,655	3,037,434	-	18,870,089
Materials and supplies	14,083,731	1,509,635	-	15,593,366
Outside services	5,308,097	6,179,323	-	11,487,420
State fuel taxes	2,392,228	520,055	-	2,912,283
Utilities, rentals and others	1,645,261	232,870	-	1,878,131
Total operating expenses	<u>205,557,589</u>	<u>49,145,582</u>	<u>-</u>	<u>254,703,171</u>
Loss from operations	<u>(153,827,324)</u>	<u>(47,043,106)</u>	<u>-</u>	<u>(200,870,430)</u>

See independent auditor's report.

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Supplemental Schedule – Detailed Statement of Revenues, Expenses and Changes in Net Position (continued)
Year Ended June 30, 2017

	Bus Operations	Paratransit Operations	Eliminations	Total
Loss from operations	\$ (153,827,324)	\$ (47,043,106)	\$ -	\$ (200,870,430)
Nonoperating Income (Expense)				
Noncapital contributions	21,000,000	-	-	21,000,000
Loss on disposal of parts and supplies	(158,293)	-	-	(158,293)
Loss on disposal of capital assets	(71,431)	-	-	(71,431)
	<u>20,770,276</u>	<u>-</u>	<u>-</u>	<u>20,770,276</u>
Loss before transfers and capital contributions	<u>(133,057,048)</u>	<u>(47,043,106)</u>	<u>-</u>	<u>(180,100,154)</u>
Interfund Transfers	(43,649,005)	43,649,005	-	-
Transfers	166,067,887	-	-	166,067,887
Capital Contributions	<u>16,156,782</u>	<u>-</u>	<u>-</u>	<u>16,156,782</u>
Changes in net position	5,518,616	(3,394,101)	-	2,124,515
Net Position				
Beginning of year	<u>240,113,424</u>	<u>(20,515,288)</u>	<u>-</u>	<u>219,598,136</u>
End of year	<u>\$ 245,632,040</u>	<u>\$ (23,909,389)</u>	<u>\$ -</u>	<u>\$ 221,722,651</u>

See independent auditor's report.

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Supplemental Schedule – Detailed Statement of Revenues, Expenses and Changes in Net Position
Year Ended June 30, 2016

	<u>Bus Operations</u>	<u>Paratransit Operations</u>	<u>Eliminations</u>	<u>Total</u>
Operating Revenues				
Passenger fares for transit services	\$ 53,197,736	\$ 1,716,757	\$ -	\$ 54,914,493
Nontransportation revenue	309,761	28,429	-	338,190
Total operating revenues	<u>53,507,497</u>	<u>1,745,186</u>	<u>-</u>	<u>55,252,683</u>
Operating Expenses				
Contract services	140,086,779	32,764,428	-	172,851,207
Insurance	13,743,069	3,529,080	-	17,272,149
Fuel and lubricants	10,399,076	2,010,855	-	12,409,931
Depreciation	13,793,125	3,875,144	-	17,668,269
Materials and Supplies	12,555,835	1,308,029	-	13,863,864
Outside services	5,758,153	5,247,516	-	11,005,669
State fuel taxes	2,450,660	513,148	-	2,963,808
Utilities, rentals and others	1,273,335	(22,390)	-	1,250,945
Total operating expenses	<u>200,060,032</u>	<u>49,225,810</u>	<u>-</u>	<u>249,285,842</u>
Loss from operations	<u>(146,552,535)</u>	<u>(47,480,624)</u>	<u>-</u>	<u>(194,033,159)</u>

See independent auditor's report.

City and County of Honolulu
Public Transportation System – Bus and Paratransit Operations

Supplemental Schedule – Detailed Statement of Revenues, Expenses and Change in Net Position (continued)
Year Ended June 30, 2016

	Bus Operations	Paratransit Operations	Eliminations	Total
Loss from operations	\$ (146,552,535)	\$ (47,480,624)	\$ -	\$ (194,033,159)
Nonoperating Income (Expense)				
Noncapital contributions	21,000,000	-	-	21,000,000
Loss on disposal of capital assets	(55,810)	-	-	(55,810)
Loss on disposal of parts and supplies	(111,221)	(178,682)	-	(289,903)
Total nonoperating income	<u>20,832,969</u>	<u>(178,682)</u>	<u>-</u>	<u>20,654,287</u>
Loss before transfers and capital contributions	<u>(125,719,566)</u>	<u>(47,659,306)</u>	<u>-</u>	<u>(173,378,872)</u>
Interfund transfer	(39,577,066)	39,577,066	-	-
Transfers	156,214,210	-	-	156,214,210
Capital contributions	<u>38,894,345</u>	<u>-</u>	<u>-</u>	<u>38,894,345</u>
Changes in net position	29,811,923	(8,082,240)	-	21,729,683
Net Position				
Beginning of year	<u>210,301,501</u>	<u>(12,433,048)</u>	<u>-</u>	<u>197,868,453</u>
End of year	<u>\$ 240,113,424</u>	<u>\$ (20,515,288)</u>	<u>\$ -</u>	<u>\$ 219,598,136</u>

See independent auditor's report.