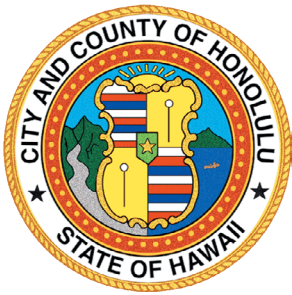




Office of the City Auditor



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

**City and County of Honolulu
Sewer Fund**

**Financial Statements
June 30, 2022**

City and County of Honolulu
Sewer Fund
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Report of Independent Auditors

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

Opinion

We have audited the accompanying financial statements of the City and County of Honolulu, Sewer Fund ("Sewer Fund"), as of and for the year ended June 30, 2022, and the related notes to the financial statements, as listed in the index.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Sewer Fund as of June 30, 2022, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United State of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Sewer Fund, and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Emphasis of Matter

As discussed in Note 2, the financial statements present only the Sewer Fund and do not purport to, and do not present fairly, the financial position of the City and County of Honolulu ("City") as of June 30, 2022, 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. Our opinion is not modified with respect to this matter.

Adoption of New Accounting Principle

As discussed in Note 2, the Sewer Fund adopted Governmental Accounting Standards Board Statement No. 87, *Leases*, in fiscal year 2022. Our opinion is not modified with respect to this matter.

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Responsibilities of Management 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, and for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Sewer Fund's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Sewer Fund's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.



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 and the schedule of the City's proportionate share of the net pension liability, schedule of pension contributions, schedule of changes in net other postemployment benefits ("OPEB") liability and related ratios, and schedule of OPEB contributions on pages 42 through 47 be presented to supplement the basic financial statements. Such information is the responsibility of management and, 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.

Accuity LLP

Honolulu, Hawaii
December 23, 2022

City and County of Honolulu
Sewer Fund
Management's Discussion and Analysis (Unaudited)
June 30, 2022

The following summary discussion and analysis of the financial statements for the year ended June 30, 2022 are provided by the City and County of Honolulu's wastewater enterprise ("Wastewater Enterprise"). The summary is designed to provide an introduction to the Sewer Fund financial statements and the financial condition of the Wastewater Enterprise. We encourage readers to also review the financial statements as a whole.

Financial Highlights

- 98.9 million gallons per day of wastewater were collected and treated in fiscal year 2022, a decrease of 4.6% from fiscal year 2021. As of June 30, 2022, the Wastewater Enterprise had approximately 148,000 customer accounts and served approximately 780,000 residents.
- Total assets and deferred outflows of resources were \$5.7 billion and exceeded total liabilities by \$2.6 billion as of June 30, 2022. As of June 30, 2022, net position (difference between assets, deferred inflows/outflows of resources, and liabilities) increased by \$139.8 million, or 5.8%, from June 30, 2021. The increase in net position in 2022 was primarily due to an increase in capital assets.
- As of June 30, 2022, total assets increased by \$309.4 million to \$5.5 billion, representing a 5.9% increase from the prior fiscal year. The increase in fiscal year 2022 was primarily due to an increase in capital assets.
- Total current and restricted assets increased by 9.5% or \$143.8 million to \$1.7 billion at June 30, 2022. The increase in 2022 was primarily due to revenue bond proceeds.
- Total current liabilities decreased by 3.2% or \$7.4 million to \$223.2 million as of June 30, 2022, primarily due to decreases in accounts payable. As of June 30, 2022, total liabilities increased 4.3% or \$125.0 million to \$3.0 billion due to an increase in revenue bonds payable.
- Due to the implementation of Governmental Accounting Standards Board ("GASB") Statement No. 87, *Leases*, in fiscal year 2022, the lease assets and liabilities have been restated in the amount of approximately \$39,600 at July 1, 2021. It was not practical to determine fiscal 2021 beginning balances, therefore the 2021 financial statements have not been restated for the management's discussion and analysis.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to Wastewater Enterprise's financial statements, which consist of the basic financial statements and notes to the financial statements.

Basic Financial Statements

The basic financial statements are designed to provide readers with a broad overview of the Wastewater Enterprise's finances, in a manner similar to a private-sector business.

City and County of Honolulu
Sewer Fund
Management's Discussion and Analysis (Unaudited)
June 30, 2022

The *statement of net position* presents information on the Wastewater Enterprise's assets, liabilities, and deferred inflows and outflows of resources 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 the Wastewater Enterprise 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 indicates an improved financial position.

The *statement of revenues, expenses, and changes in net position* presents information showing how the Wastewater Enterprise's net position changed during the past fiscal year. All changes in net position are reported as soon as the underlying event occurs, regardless of timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods (e.g., earned but unused vacation leave).

The *statement of cash flows* presents changes in cash and cash equivalents, resulting from operating, financing and investing activities. This statement presents cash receipts and cash disbursements information, without consideration of the earnings event, when an obligation arises, or depreciation of capital assets.

Notes to Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

City and County of Honolulu
Sewer Fund
Management’s Discussion and Analysis (Unaudited)
June 30, 2022

Financial Analysis

The following are the highlights of the condensed statements of net position for the Wastewater Enterprise (in thousands of dollars):

Condensed Statements of Net Position

	2022	2021
Assets		
Current assets	\$ 1,456,300	\$ 1,414,515
Restricted assets, noncurrent	200,573	98,560
Capital assets, net	3,888,158	3,722,560
Deferred outflows of resources	120,008	136,546
Total assets and deferred outflows	<u>\$ 5,665,039</u>	<u>\$ 5,372,181</u>
Liabilities		
Current liabilities	\$ 223,231	\$ 230,591
Noncurrent liabilities	2,824,268	2,691,870
Deferred inflows of resources	51,742	23,714
Total liabilities and deferred inflows	<u>3,099,241</u>	<u>2,946,175</u>
Net investment in capital assets	1,426,191	1,344,655
Restricted for debt service	115,746	115,164
Unrestricted	1,023,861	966,187
Total net position	<u>2,565,798</u>	<u>2,426,006</u>
Total liabilities, deferred inflows, and net position	<u>\$ 5,665,039</u>	<u>\$ 5,372,181</u>

Net Position

Net position (the difference between assets, liabilities, and deferred inflows/outflows of resources) may serve, over time, as a useful indicator of a government’s financial position. In the case of the Wastewater Enterprise, assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by \$2.6 billion at the end of fiscal year 2022. Additions of capital assets resulted in a 5.8% increase in net position from fiscal year 2021 to 2022. The largest portion of the Wastewater Enterprise’s net position represented its investment in capital assets (e.g., land, buildings, transmission and distribution system, etc.). The Wastewater Enterprise uses these capital assets to provide wastewater services on the Island of Oahu and consequently, capital assets are not available to liquidate liabilities or other spending.

City and County of Honolulu
Sewer Fund
Management's Discussion and Analysis (Unaudited)
June 30, 2022

The following are the highlights of the condensed statements of revenues, expenses, and changes in net position (in thousands of dollars):

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

	2022	2021
Operating revenues	\$ 469,136	\$ 459,482
Operating expenses	(222,364)	(222,681)
Operating income	<u>246,772</u>	<u>236,801</u>
Nonoperating revenues (expenses)		
Interest income	7,337	5,774
Interest expense	(72,169)	(64,393)
Other	(22,714)	(2,721)
Income before transfers and capital contributions	<u>159,226</u>	<u>175,461</u>
Transfers out	(21,297)	(21,646)
Capital contributions	<u>1,863</u>	<u>587</u>
Change in net position	139,792	154,402
Net position		
Beginning of year	<u>2,426,006</u>	<u>2,271,604</u>
End of year	<u>\$ 2,565,798</u>	<u>\$ 2,426,006</u>

The changes in net position were primarily due to:

- Operating revenues, comprised mainly of sewer service charges, increased 2.1% to \$469.1 million for fiscal year 2022 compared to the prior fiscal year. Sewer service charge rates remained the same in fiscal year 2022.
- Operating expenses decreased \$317,000 or 0.1% to \$222.4 million for fiscal year 2022 compared \$222.7 million for fiscal year 2021.
- Interest expense increased by \$7.8 million or 12.1% to \$72.2 million for fiscal year 2022 compared to fiscal year 2021. The increase in 2022 was due primarily to increased interest expense on wastewater revenue bonds.
- Contributed capital increased to \$1.9 million in fiscal year 2022, up from \$587,000 in fiscal year 2021. Contributed capital represents assets (primarily capital assets) transferred from other city governmental funds and other entities. Approximately \$21.3 million was transferred out during fiscal year 2022 for the Wastewater Enterprise's share of central administrative expenses incurred by the City.

City and County of Honolulu
Sewer Fund
Management’s Discussion and Analysis (Unaudited)
June 30, 2022

Capital Assets and Debt Administration

Capital Assets

The Wastewater Enterprise’s investment in capital assets amounted to \$3.9 billion and \$3.7 billion, net of accumulated depreciation, as of June 30, 2022 and 2021, respectively, an increase of \$165.6 million or 4.4% in 2022. Capital assets include land, buildings, infrastructure, land improvements, equipment, machinery, and leased equipment for the 9 treatment plants, 71 pumping stations, and over 2,100 miles of sewer line that makes up the Wastewater Enterprise. Capital assets are added, rehabilitated or replaced according to the infrastructure and facilities twenty-year capital plan.

Long-term Debt

Wastewater revenue bonds and State revolving fund loans are the primary long-term financing instruments used to fund the acquisition of capital assets. Revenue bonds outstanding as of June 30, 2022 and 2021 totaled \$2.4 billion and \$2.2 billion, respectively. State revolving fund notes payable outstanding at June 30, 2022 and 2021 totaled \$321.2 million and \$298.6 million, respectively.

Debt service coverage was 254% on Senior Revenue Bonds, 203% on all revenue bonds, and 173% on all debt at June 30, 2022. Debt service coverage exceeded the requirements of bond covenants and policies of the City Council in 2022.

Additional information on the Wastewater Enterprise’s capital assets and long-term debt can be found in the notes to the financial statements.

Currently Known Facts, Decisions or Conditions

The Department of Environmental Service (the “Department”) and its Wastewater System has not experienced any material adverse impact on its operations or finances from Coronavirus Disease 2019 (“COVID-19”). The Department does not anticipate significant decreases in Wastewater System service charge revenues as a result of the COVID-19 pandemic, as approximately 67% of the total revenue from sewer service charges comes from residential accounts and the Department’s rates and charges include fixed monthly charges. The Department is allowing payment plans but is not waiving fees. During fiscal year 2022 the City and County of Honolulu’s Rental and Utility Relief Program provided financial assistance with utility bills, including wastewater bills, to eligible renters financially impacted by COVID-19.

Requests for Information

Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City and County of Honolulu, Department of Environmental Services, 1000 Uluohia Street, Suite 308, Kapolei, HI 96707.

City and County of Honolulu
Sewer Fund
Statement of Net Position
June 30, 2022
(Amounts in thousands)

Assets and Deferred Outflows of Resources

Current assets	
Cash and cash equivalents	\$ 210,843
Receivables	
Accounts, net of allowance for uncollectible accounts of \$6,007	73,909
Interest	1,607
Investments	1,158,614
Employee advances	485
Inventories of materials and supplies	10,444
Other assets	<u>398</u>
Total current assets	1,456,300
Restricted assets – investments	200,573
Capital assets and intangible right-of-use leases, net	<u>3,888,158</u>
Total assets	<u>5,545,031</u>
Deferred outflows of resources	
Deferred refunding costs, net	82,369
Deferred pension costs	21,033
Deferred other postemployment benefit costs	11,478
Deferred asset retirement obligations costs	<u>5,128</u>
Total deferred outflows of resources	<u>120,008</u>
Total assets and deferred outflows of resources	<u>\$ 5,665,039</u>

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

City and County of Honolulu
Sewer Fund
Statement of Net Position
June 30, 2022
(Amounts in thousands)

Liabilities, Deferred Inflows of Resources, and Net Position

Current liabilities	
Accounts payable	\$ 63,726
Interest payable	39,589
Bonds payable	87,288
Notes payable	29,067
Accrued payroll	2,161
Other liabilities	1,400
Total current liabilities	<u>223,231</u>
Notes payable	292,086
General obligation bonds payable, net	384
Asset retirement obligations	13,594
Revenue bonds payable, net	2,319,485
Net pension liability	108,121
Net other postemployment benefit liability	83,921
Other liabilities	6,677
Total liabilities	<u>3,047,499</u>
Deferred inflows of resources	
Deferred pension costs	28,858
Deferred other postemployment benefit costs	22,500
Deferred leases	384
Total deferred inflows of resources	<u>51,742</u>
Net position	
Net investment in capital assets	1,426,191
Restricted for debt service	115,746
Unrestricted	1,023,861
Total net position	<u>2,565,798</u>
Total liabilities, deferred inflows of resources, and net position	<u>\$ 5,665,039</u>

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

City and County of Honolulu
Sewer Fund
Statement of Revenues, Expenses, and Changes in Net Position
Year Ended June 30, 2022
(Amounts in thousands)

Operating revenues	
Sewer service charges	\$ 458,012
Other revenue	11,124
Total operating revenues	<u>469,136</u>
Operating expenses	
Depreciation and amortization	90,353
Administrative and general	52,386
Utilities	24,675
Fringe benefits	22,995
Contractual services	21,571
Materials and supplies	8,341
Maintenance	921
Fuel and lubricants	1,122
Total operating expenses	<u>222,364</u>
Operating income	<u>246,772</u>
Nonoperating revenues (expenses)	
Interest income	7,337
Interest expense	(72,169)
Loss from disposal of property	(9)
Net decrease in fair value of investments	(21,394)
Other	(1,311)
Total nonoperating expenses, net	<u>(87,546)</u>
Income before transfers and capital contributions	159,226
Transfers out	(21,297)
Capital contributions	1,863
Change in net position	<u>139,792</u>
Net position	
Beginning of year	<u>2,426,006</u>
End of year	<u>\$ 2,565,798</u>

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

City and County of Honolulu
Sewer Fund
Statement of Cash Flows
Year Ended June 30, 2022
(Amounts in thousands)

Cash flows from operating activities	
Cash received from customers	\$ 459,714
Cash payments to suppliers	(64,517)
Cash payments to employees	(66,858)
Other receipts	1,260
Net cash provided by operating activities	<u>329,599</u>
Cash flows from noncapital financing activities	
Transfers out	<u>(21,297)</u>
Net cash used in noncapital financing activities	<u>(21,297)</u>
Cash flows from capital and related financing activities	
Acquisition and construction of capital assets	(280,112)
Proceeds from issuance of notes	48,168
Repayments on notes	(25,656)
Interest paid on notes	(3,107)
Proceeds from issuance of bonds, net	260,001
Repayments on bonds	(81,968)
Interest paid on bonds	(76,654)
Principal paid on leases	(12)
Interest paid on leases	(2)
Net cash used in capital and related financing activities	<u>(159,342)</u>
Cash flows from investing activities	
Purchase of investments	(1,584,420)
Proceeds from maturity of investments	1,475,052
Interest on investments	6,398
Net cash used in investing activities	<u>(102,970)</u>
Net increase in cash and cash equivalents	45,990
Cash and cash equivalents	
Beginning of year	<u>164,853</u>
End of year	<u>\$ 210,843</u>

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

City and County of Honolulu
Sewer Fund
Statement of Cash Flows
Year Ended June 30, 2022
(Amounts in thousands)

Reconciliation of operating income to net cash provided by operating activities

Operating income	\$ 246,772
Adjustments to reconcile operating income to net cash provided by operating activities	
Depreciation and amortization	90,353
Write-off of capital assets	7,621
Change in	
Accounts receivable	(8,659)
Other assets	(398)
Inventories of materials and supplies	78
Deferred outflows from pension	5,415
Deferred outflows from other postemployment benefits	4,754
Deferred outflows from asset retirement obligations	(202)
Accounts payable	632
Other liabilities	(496)
Net pension liability	(26,465)
Asset retirement obligations	866
Net other postemployment benefits liability	(17,766)
Due to other City funds	(934)
Deferred inflows from pension	18,969
Deferred inflows from other postemployment benefits	8,675
Deferred inflows from leases	384
Net cash provided by operating activities	<u>\$ 329,599</u>

Supplemental disclosure of noncash capital and related financing activities

The Sewer Fund received \$1.9 million in contributions of capital assets from government agencies and developers, which are recorded as capital contributions at their cost or estimated cost for the year ended June 30, 2022.

Amortization of net bond premiums, (discounts), and (deferred loss on refunding) amounted to \$16.6 million, (\$125,000), and (\$6.6) million, respectively, in fiscal 2022.

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

City and County of Honolulu
Sewer Fund
Notes to Financial Statements
June 30, 2022

1. Financial Reporting Entity

The Sewer Fund was established as an enterprise fund effective July 1, 1999 in conjunction with the November 1998 City Resolution 98-193, CD1, authorizing the issuance of the Wastewater System Revenue Bonds for the City and County of Honolulu's ("City") wastewater system. The fund accounts for the operations of the City's wastewater system.

The Sewer Fund is one of the various enterprise funds of the City. The Sewer Fund's financial statements reflect only its portion of the proprietary fund type. The City's Director of Budget and Fiscal Services maintains the central accounts for all City funds and publishes financial statements for the City annually, which include the Sewer Fund's financial activities.

2. Summary of Significant Accounting Policies

Financial Statement Presentation

The Sewer Fund is included in the City's Enterprise Funds. The Sewer Fund's financial statements are intended to present the financial position, change in financial position, and cash flows of only that portion of the funds of the City's Enterprise Funds that is attributable to the transactions of the Sewer Fund.

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

Basis of Accounting

The accompanying 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.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions included revenue recognized related to unbilled accounts, allowance for uncollectible accounts, net pension liability, net other postemployment benefits ("OPEB"), asset retirement obligations ("ARO"), and measurement of leases. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash includes amounts in demand and time deposits primarily with various financial institutions in the State of Hawaii. Cash on deposit with financial institutions is collateralized in accordance with state statutes. Investments with original maturity of three months or less when purchased are considered cash equivalents.

City and County of Honolulu
Sewer Fund
Notes to Financial Statements
June 30, 2022

Investments

Investments consist of U.S. Treasury and government securities and nonparticipating guaranteed investment contracts. All nonparticipating investment contracts are recorded at amortized cost. Participating investment contracts with maturities of one year or more are stated at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Participating investment contracts with maturities of less than one year are recorded at amortized cost.

Inventories of Materials and Supplies

Inventories of materials and supplies are stated at weighted average cost. The costs of inventories are recorded as expenditures when consumed rather than when purchased.

Receivables

Sewer service charge revenues are accrued by the City based on estimated billings for services provided through the end of the fiscal year. Receivables included estimated unbilled sewer charges amounting to approximately \$36.0 million at June 30, 2022. The allowance for doubtful accounts is based on the aging of accounts receivable. Approximately 90% of balances over 120 days are regarded as uncollectible.

Restricted Assets

Revenue bond indentures allow the City to invest in U.S. government securities. At June 30, 2022, restricted assets consisted of unspent debt proceeds of \$184.0 million, revenue bond collateral reserves of approximately \$15.9 million, and investments held in clearance accounts of \$749,000, totaling \$200.6 million.

Capital Assets

Capital assets include property, plant and equipment, including infrastructure (sewer system, network of pipes, and sewer mains). Assets with an initial individual cost of \$5,000 or more for equipment and \$100,000 for buildings, structures and infrastructure, and an estimated useful life of more than one year are capitalized. Such assets are recorded at cost or estimated cost.

Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	Years
Buildings and land improvements	10 – 50
Transmission and distribution system	13 – 100
Equipment and machinery	5 – 25

Sales and retirements of depreciable property are recorded by removing the related cost and accumulated depreciation from the accounts. Gains or losses on sales and retirements of property are reflected in results of operations.

City and County of Honolulu
Sewer Fund
Notes to Financial Statements
June 30, 2022

Normal maintenance and repairs that do not add to the value of the assets or materially extend asset lives are not capitalized. Betterments are capitalized and depreciated over the remaining useful lives of the related assets, as applicable.

Leases – Lessee

The Sewer Fund recognizes a lease liability and a right-of-use lease asset (“lease asset”) in the statement of net position. The Sewer Fund has a policy to recognize lease liabilities and lease assets for all land leases and leases with an initial individual present value of expected payments of \$5,000 or more for equipment and \$100,000 for buildings, structures and infrastructure, and a lease term of more than one year.

At the commencement of a lease, the Sewer Fund initially measures the lease liability at the present value of payments expected to be made during the lease term. Variable payments based on future performance or usage of the lease asset are not included in the measurement of the lease liability. Subsequently, the lease liability is reduced by the principal portion of lease payments made.

Lease assets are recorded at the amount of the initial measurement of the lease liabilities and modified by any lease payments made to the lessor at or before the commencement of the lease term, less any lease incentives received from the lessor at or before the commencement of the lease term along with any initial direct costs that are ancillary charges necessary to place the lease asset into service. Lease assets are amortized using the straight-line method over the shorter of the lease term or the useful life of the underlying asset, unless the lease contains a purchase option that management determined is reasonably certain of being exercised. In this case, the lease asset is amortized over the useful life of the underlying asset.

Key estimates and judgments related to leases include how the Sewer Fund determines (1) the discount rate it uses to discount the expected lease payments to present value, (2) the lease term, and (3) lease payments.

- The Sewer Fund uses its estimated incremental borrowing rate as the discount rate for leases.
- The lease term includes the noncancellable period of the lease as well as any periods covered by the Sewer Fund’s option to extend the lease if it is reasonably certain, based on all relevant factors, that management will exercise that option. Lease payments included in the measurement of the lease liability are composed of fixed payments and purchase option price that the Sewer Fund is reasonably certain to exercise.

The Sewer Fund monitors changes in circumstances that would require a remeasurement of its lease and will remeasure any lease asset and liability if certain changes occur that are expected to significantly affect the amount of the lease liability. The Sewer Fund’s lease assets and lease liabilities are recorded in capital assets and intangible right-of-use leases, net and other current and noncurrent liabilities, respectively, in the statement of net position.

City and County of Honolulu
Sewer Fund
Notes to Financial Statements
June 30, 2022

Leases – Lessor

The Sewer Fund recognizes lease receivables and deferred inflows of resources in the statement of net position. The Sewer Fund has a policy to recognize lease receivables and deferred inflows of resources for all land leases and leases with an initial individual present value of expected receipts of \$5,000 or more for equipment and \$100,000 for buildings, structures and infrastructure, and a lease term of more than one year. Variable payments based on future performance of the lessee or usage of the underlying asset are not included in the measurement of the lease receivable.

At the commencement of a lease, the Sewer Fund initially measures the lease receivable at the present value of payments expected to be received during the lease term. Subsequently, the lease receivable is reduced by the principal portion of the lease payments received. The deferred inflows of resources are initially measured as the initial amount of the lease receivable, adjusted for lease payments received at or before the lease commencement date. Subsequently, the deferred inflows of resources are recognized as revenue over the life of the lease term in a systematic and rational method.

Key estimates and judgments related to leases include how the Sewer Fund determines (1) the discount rate it uses to discount the expected lease receipts to present value, (2) the lease term, and (3) lease payments.

- The Sewer Fund uses its estimated incremental borrowing rate as the discount rate for leases.
- The lease term includes the noncancellable period of the lease as well as any periods covered by the lessee's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessee will exercise that option. Lease receipts included in the measurement of the lease receivable are composed of fixed payments from the lease.

The Sewer Fund monitors changes in circumstances that would require a remeasurement of its lease and will remeasure any lease receivable and deferred inflows of resources if certain changes occur that are expected to significantly affect the amount of the lease receivable. The lease receivable is recorded in other assets in the statement of net position.

Asset Retirement Obligations

AROs represent the liabilities where both an external obligating event and internal obligating event have occurred, and the liability is reasonably estimable and recorded based on the City's best estimates of the current value of outlays expected to be incurred. The AROs are reevaluated annually for the effects of general inflation or deflation and any events that would cause a significant change in the estimated outlays. Refer to Note 7 for more information.

Original Issue Discounts or Premiums

Original issue discounts or premiums on bonds are amortized ratably over the terms of the respective issues and are offset against the bonds payable in the statement of net position.

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Accrued Vacation

Employees are credited with vacation at the rate of one and three-quarters working days per month. Accumulation of such vacation credits is limited to 90 days at calendar year-end and is convertible to pay upon termination of employment. Such accumulated vacation has been accrued and reflected in the statement of net position.

Deferred Outflows and Inflows of Resources

Deferred outflows of resources represent consumptions of net position that apply to future periods and will not be recognized as an outflow of resources (expenditures) until then. The balances consist of:

- 1) Deferred charges on refunding bonds resulting from the difference between the carrying value of debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt on a basis that approximates the effective-interest method.
- 2) Differences between projected and actual experience and changes in assumptions are recognized in pension/OPEB expense using a systematic and rational method over a closed period equal to the average of the expected remaining service lives of all employees that are provided with pensions/OPEB through the pension/OPEB plans (active and inactive employees) determined as of the beginning of the measurement period. The average of expected remaining service lives for the purposes of recognizing the applicable deferred outflows and inflows of resources established in fiscal year 2021 for pension and OPEB are 5.1542 years and 5.8823 years, respectively.
- 3) A corresponding deferred outflow of resources equal to the ARO is also recognized. The deferred outflow of resources is amortized over the remaining useful life of the related capital assets.
- 4) Deferred inflow of resources resulting from leases where the Sewer fund is the lessor equal to the present value of payments expected to be received during the lease. The deferred inflows of resources are recognized over the life of the lease in a systematic and rational method.

Additionally, differences between projected and actual earnings on pension/OPEB plan investments are recognized in pension/OPEB expense using a systematic and rational method over a closed five-year period.

Contributions to the pension/OPEB plans from the employer subsequent to the measurement date of the net pension/OPEB liability and before the end of the reporting period are reported as deferred outflows of resources.

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Pension

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions and pension expense, information about the fiduciary net position of the Employees' Retirement System of the State of Hawaii ("ERS"), and additions to/deductions from ERS's fiduciary net position have been determined on the same basis as they are reported by ERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Other Postemployment Benefits

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

Net Position

Net position is comprised of the accumulated income from operating and nonoperating revenues, expenses, transfers, and capital contributions. Net position is classified in the following three components: net investment in capital assets, restricted for debt service, and unrestricted net position. Net investment in capital assets consists of capital assets, net of accumulated depreciation, and is reduced by outstanding debt that is attributable to the acquisition, construction or improvement of those assets. Debt related to unspent proceeds or other restricted cash and investments at fiscal year-end are not included in the calculation of the amount of net investment in capital assets. Restricted for debt service consists of net position for which constraints are placed thereon by external parties, such as lenders, grantors, contributors, laws, regulations, and enabling legislation, including self-imposed legal mandates. Unrestricted net position consists of all other net position not included in the above categories. When an expense is incurred for purposes for which both restricted and unrestricted net position is available, restricted resources are applied first, then unrestricted resources as they are needed.

Operating Revenues and Expenses

The City distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services in connection with the Sewer Fund's principal wastewater operations. The principal operating revenues are from charges for wastewater system usage, 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.

Capital Contributions

Capital contributions represent assets transferred from or constructed utilizing contributions from governmental agencies and developers and recorded at cost on the date placed in service.

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Transfers

Transfers include authorized transfers of resources from the fund legally required to receive them to the fund through which such resources are to be expended. Transfers also include reimbursement of funds to the City's General Fund for expenditures of the General Fund on behalf of the Sewer Fund. During the year ended June 30, 2022, approximately \$21.3 million was transferred out for the Sewer Fund's share of central administrative expenses incurred by the City.

Risk Management

The City 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 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.

Coronavirus Disease 2019 ("COVID-19")

The outbreak of COVID-19 has been declared a pandemic by the World Health Organization. The state of emergency declared by the Governor of Hawaii and the Mayor of the City at the outset of the pandemic is no longer effective as of March 26, 2022.

The COVID-19 pandemic and related economic disruptions resulting from the emergency measures to contain it ended in fiscal year 2022 and as a result the City's revenues are expected to return to pre-pandemic levels.

New Accounting Pronouncements

GASB Statement No. 87

In June 2017, GASB issued Statement No. 87, *Leases*. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. The Sewer fund adopted this Statement effective July 1, 2021.

The adoption of Statement No. 87 resulted in the recording of lease assets, lease liabilities, lease receivables, and deferred inflows of resources related to leases at July 1, 2021, in accordance with the provisions of this Statement. Lease liabilities and lease assets of approximately \$40,000 were reported at July 1, 2021. Refer to Note 6 for additional details on the Sewer Fund's leases.

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GASB Statement No. 94

In March 2020, GASB issued Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*. The primary objective of this Statement is to improve financial reporting by addressing issues related to public-private and public-public partnership arrangements. The requirements for this Statement are effective for reporting periods beginning after June 15, 2022. Management has not yet determined the effect this Statement will have on its financial statements.

GASB Statement No. 96

In May 2020, GASB issued Statement No. 96, *Subscription-Based Information Technology Arrangements*. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements for government end users. This Statement is effective for periods beginning after June 15, 2022. Management has not yet determined the effect this Statement will have on its financial statements.

GASB Statement No. 99

In April 2022, GASB issued Statement No. 99, *Omnibus 2022*. This Statement enhances comparability in accounting and financial reporting and improves the consistency of authoritative literature by addressing (1) practice issues that have been identified during implementation and application of certain GASB Statements and (2) accounting and financial reporting for financial guarantees. Certain requirements of this Statement are effective upon issuance, while other requirements are effective for periods beginning after June 15, 2022 and periods beginning after June 15, 2023. Management has not yet determined the effect this Statement will have on its financial statements.

GASB Statement No. 100

In June 2022, GASB issued Statement No. 100, *Accounting Changes and Error Corrections – an amendment of GASB Statement No. 62*. This Statement enhances accounting and financial reporting requirements for accounting changes and error corrections to provide more understandable, reliable, relevant, consistent and comparable information for making decisions or assessing accountability. This Statement is effective for fiscal years beginning after June 15, 2023. Management has not yet determined the effect this Statement will have on its financial statements.

GASB Statement No. 101

In June 2022, GASB issued Statement No. 101, *Compensated Absences*. This Statement aims to better meet the information needs of financial statement users by updating the recognition and measurement guidance for compensated absences. That objective is achieved by aligning the recognition and measurement guidance under a unified model and by amending certain previously required disclosures. This Statement is effective for fiscal years beginning after December 15, 2023. Management has not yet determined the effect this Statement will have on its financial statements.

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3. Cash and Investments

The cash and investment balances reported in the accompanying statement of net position are included in the City's investment pool that is substantially used by all of the City's funds. Information pertaining to credit risk, interest rate risk, and fair value measurements is available for only the investment pool, which is disclosed in the City's Annual Comprehensive Financial Report ("ACFR") available at City's website: <https://www.honolulu.gov/budget/budget-acfr.html>.

State statutes 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. Section 46-50, Hawaii Revised Statutes, the City's investment policy, and Resolution 18-115, CD1 govern acceptable types of investments. The City's Resolution 07-51, CD1 governs the deposit and short-term investment of general excise and use tax revenues.

Interest Rate Risk

The City structures the 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 the fluctuation in interest rates. The City may invest operating funds primarily in shorter-term securities, money market mutual funds, or similar investment pools. As of June 30, 2022, the City had no investments in money market mutual funds or external investment pools.

4. Credit Risk

Financial instruments, which potentially expose the City to concentrations of credit risk, consist primarily of cash, investments in debt securities, and accounts receivable from customers. Cash and cash equivalents are maintained in various financial institutions in the State. Credit risk related to investments in debt securities has been mitigated by limiting such investments to debt obligations of the U.S. government. All the City's investments at June 30, 2022 were invested in the City's pooled investment fund.

The customer base is concentrated among commercial, industrial, residential and governmental customers located within Honolulu, Hawaii. Although the City is directly affected by Honolulu's economy, management does not believe significant credit risk exists at June 30, 2022, except as provided in the allowance for uncollectible accounts. The City manages its credit exposure through procedures designed to identify and monitor credit risk.

5. Due to Other City Funds

Due to other City funds consists primarily of payroll-related expenses for the Sewer Fund temporarily advanced by the General Fund.

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6. Capital Assets and Leases

The capital assets and leased assets activity for the year ended June 30, 2022 was as follows (in thousands of dollars):

	Balance at July 1, 2021 (As Restated)	Additions	Retirements/ Transfers	Balance at June 30, 2022
Depreciable assets				
Buildings and improvements	\$ 1,432,793	\$ 1,326	\$ (19)	\$ 1,434,100
Transmission and distribution system	2,423,704	224,193	(2,623)	2,645,274
Equipment and machinery	162,763	10,686	(258)	173,191
Land improvements	7,999	-	-	7,999
Total depreciable assets	<u>4,027,259</u>	<u>236,205</u>	<u>(2,900)</u>	<u>4,260,564</u>
Less: Accumulated depreciation				
Buildings and improvements	(401,929)	(30,999)	-	(432,928)
Transmission and distribution system	(572,130)	(48,617)	369	(620,378)
Equipment and machinery	(79,560)	(10,498)	249	(89,809)
Land improvements	(3,076)	(227)	-	(3,303)
Total accumulated depreciation	<u>(1,056,695)</u>	<u>(90,341)</u>	<u>618</u>	<u>(1,146,418)</u>
Net depreciable assets	2,970,564	145,864	(2,282)	3,114,146
Amortizable leased assets				
Equipment and machinery	40	-	-	40
Less: Accumulated amortization	-	(12)	-	(12)
Net amortizable leased assets	40	(12)	-	28
Land	48,629	1,863	-	50,492
Construction in progress	703,367	259,270	(239,145)	723,492
Total capital assets, net	<u>\$ 3,722,600</u>	<u>\$ 406,985</u>	<u>\$ (241,427)</u>	<u>\$ 3,888,158</u>

Depreciation and amortization expense was \$90.4 million for the year ended June 30, 2022.

Leases

The Sewer Fund entered into an agreement to lease a property to a telecommunications company in August 2021, which expires in August 2041. At June 30, 2022, lease receivables of \$397,000 were reported in other assets in the statement of net position. For the year ended June 30, 2022, lease revenue and interest revenue were approximately \$17,000 and \$18,000, respectively.

The Sewer Fund leases various information technology equipment under contracts ranging from one to four years through November 2025.

City and County of Honolulu
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7. Long-Term Liabilities

General Obligation Bonds

The City issues general obligation bonds for the construction of major capital facilities. The Sewer Fund's general obligation bonds are collateralized by or expected to be paid from sewer user charges. These instruments are a direct obligation of the City for which its full faith and credit is pledged. The general obligation bonds for the Sewer Fund were issued in 2020 in the original amount totaling approximately \$456,000 and mature serially through fiscal year 2028. The general obligation bonds bear interest at rates ranging from 1.71% to 2.17% at June 30, 2022. No new general obligation bonds have been issued to finance construction of Sewer Fund capital facilities since fiscal year 1998. General obligation bonds issued after 1998 were used for refunding. Subsequently, Sewer Fund capital facilities were funded by wastewater system revenue bonds.

Wastewater System Revenue Bonds

Wastewater system revenue bonds in the City's business-type activities with outstanding balances as of June 30, 2022 were issued during fiscal years 2013 through 2022, in the original amount totaling \$2.9 billion, less discounts of \$3.8 million and adjusted for premiums of \$300.8 million, which are being amortized over the related term of the bonds. The bonds bear interest at 0.30% to 5.25% at June 30, 2022 and mature at various dates through fiscal year 2052. The wastewater system revenues collateralize the revenue bonds.

The wastewater system revenue bonds issued are limited special obligations of the City. The net revenues and all funds and accounts established other than the rebate account, the subordinate obligation account, and the reimbursable obligation account, and, in certain instances, the common reserve account or separate series reserve accounts have been pledged as security for the payment of debt service on the bonds. In an event of default, the bonds contain a provision that the holders of not less than 25% in principal amount of the bonds then outstanding may declare that all the principal and accrued interest is due and payable immediately. An event of default includes but is not limited to the following situations: failure to pay principal, redemption price, and interest due; failure to punctually perform or observe any of the covenants, agreements or conditions; and filing a petition in bankruptcy. The City has covenanted and agreed to maintain the wastewater system in good repair, to fix rates and charges sufficient to meet the net revenue requirement, to not dispose of the properties comprising the wastewater system, to maintain and keep proper books, and other actions consistent with conducting the business of the wastewater system in an efficient and economical manner.

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On May 25, 2022, the City issued taxable Senior Series A wastewater system revenue bonds for \$241.4 million. The bonds mature annually on July 1, 2026 through 2051 and bear interest rates of 4.00% to 5.25%. For the bonds maturing July 1, 2033 through July 1, 2038, and bonds maturing from July 1, 2041 through July 1, 2051, the City may exercise its option of redemption on or after July 1, 2032 in whole or in part, at any time in any order of maturity selected by the City, and by lot within maturity selected by the City, and by lot within maturity at the principal amount thereof, plus interest accrued to the date fixed for redemption thereof, without premium except for 2047 Term Bonds. The proceeds of the bonds will be used to fund the cost of certain additions and improvements to the wastewater system.

Defeased Bonds

The Sewer Fund defeased certain general obligation and revenue bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on the old bonds. Accordingly, the assets of the irrevocable trusts and the liability for the defeased bonds are not included in the Sewer Fund's financial statements. At June 30, 2022, approximately \$430.8 million of the Sewer Fund's bonds outstanding were considered defeased.

Notes Payable

The notes payable to the State are for the construction of necessary treatment works and for other projects intended for wastewater reclamation or waste management. During fiscal year 2022, the City issued notes payable amounting to \$48.2 million. The notes amounted to \$321.2 million at June 30, 2022, bearing interest ranging from 0.00% to 0.50%, and require annual principal and interest payments through fiscal year 2042.

The notes payable are collateralized by the City's wastewater net revenue. The outstanding loans contain a provision that, in the event of default, the Director of the State of Hawaii Department of Health ("DOH") shall be entitled to collect a rate of 12% simple interest per year commencing on the repayment due date and ending on the date of the check or warrant issued by the City. A default is deemed to exist if repayment of loan fees or current loans are not paid when due, if the City fails to fulfill its obligation, or if the City becomes financially insolvent. The City covenanted that it shall exercise its revenue bonds, revenue, assessment, and other authority as needed to the extent allowed by law to pay the semiannual repayments and loan fees.

Total interest costs incurred in 2022 were \$72.2 million.

City and County of Honolulu
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Scheduled maturities of long-term debt are as follows (in thousands of dollars):

Years ending June 30,	General Obligation Bonds	Revenue Bonds – Direct Placements	Revenue Bonds	Notes Payable – Direct Borrowings	Total Principal	Total Interest
2023	\$ 73	\$ 13,445	\$ 73,770	\$ 29,067	\$ 116,355	\$ 81,108
2024	74	14,015	75,900	29,236	119,225	82,513
2025	75	14,095	76,445	29,406	120,021	79,419
2026	77	14,440	79,005	29,578	123,100	75,967
2027	78	17,965	93,475	27,217	138,735	71,922
2028–2032	80	96,420	440,875	91,790	629,165	299,569
2033–2037	-	57,415	417,160	50,149	524,724	207,109
2038–2042	-	-	382,340	34,710	417,050	118,638
2043–2047	-	-	278,875	-	278,875	55,479
2048–2052	-	-	121,125	-	121,125	12,298
	<u>457</u>	<u>227,795</u>	<u>2,038,970</u>	<u>321,153</u>	<u>2,588,375</u>	<u>\$ 1,084,022</u>
Less: Current portion	(73)	(13,445)	(73,770)	(29,067)	(116,355)	
	<u>\$ 384</u>	<u>\$ 214,350</u>	<u>\$ 1,965,200</u>	<u>\$ 292,086</u>	<u>\$ 2,472,020</u>	

Asset Retirement Obligations

The Sewer Fund accounts for certain costs associated with the future dismantling and removal of underground storage tanks in accordance with GAAP. Under GAAP, the act of placing the tanks into operation requires the Sewer Fund to recognize a liability and corresponding deferred outflow of resources equal to the estimated current cost of activities that state law requires the City to perform upon retirement of the tanks in the future. The tanks currently have estimated lives ranging from 8–22 years.

The amounts reported as a liability and deferred outflow of resources at June 30, 2022 were determined based on probability-weighted engineering estimates of what it would cost to perform all dismantling and removal tasks. Actual costs may be higher due to inflation, changes in technology, or changes in regulations.

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Changes in Long-Term Liabilities

Activity for long-term liabilities, other than net pension and OPEB, for the years ended June 30, 2022 was as follows (in thousands of dollars):

	Balance at July 1, 2021 (As Restated)	Additions	Reductions	Balance at June 30, 2022	Amount Due Within One Year
General obligation bonds	\$ 525	\$ -	\$ (68)	\$ 457	\$ 73
Revenue bonds – direct placements	234,915	-	(7,120)	227,795	13,445
Revenue bonds	1,872,395	241,355	(74,780)	2,038,970	73,770
Notes payable – direct borrowings	298,641	48,168	(25,656)	321,153	29,067
	<u>2,406,476</u>	<u>289,523</u>	<u>(107,624)</u>	<u>2,588,375</u>	<u>116,355</u>
Add: Unamortized net premium	136,394	19,969	(16,428)	139,935	-
Total long-term debt	<u>2,542,870</u>	<u>309,492</u>	<u>(124,052)</u>	<u>2,728,310</u>	<u>116,355</u>
Compensated absences	8,094	2,097	(2,900)	7,291	628
Asset retirement obligations	12,728	866	-	13,594	-
Lease liability	40	-	(12)	28	13
Total long-term liabilities	<u>\$ 2,563,732</u>	<u>\$ 312,455</u>	<u>\$ (126,964)</u>	<u>\$ 2,749,223</u>	<u>\$ 116,996</u>

8. Net Position

At June 30, 2022, net position consisted of the following (in thousands of dollars):

Net investment in capital assets	
Net property, plant and equipment	\$ 3,888,158
Deferred outflows of resources – deferred refunding costs, net	82,369
Less:	
Wastewater general obligation bonds payable, net of unamortized premiums and discounts	(457)
Wastewater system revenue bonds payable, net of unamortized premium, discount, and issue cost	(2,406,700)
Notes payable	(321,153)
Lease liability	(28)
Amount of debt related to unspent debt proceeds	<u>184,002</u>
	1,426,191
Restricted for debt service	115,746
Unrestricted	<u>1,023,861</u>
	<u>\$ 2,565,798</u>

9. Employee Benefit Plans

Defined Benefit Pension Plan

Plan Description

Substantially all eligible employees of the City are members of the ERS, a cost-sharing multiple-employer defined benefit pension 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 HRS Chapter 88 and can be amended by legislative action. The ERS is composed of three classes: contributory, noncontributory and hybrid retirement classes. Prior to July 1, 1984, the plan consisted of only a contributory class. In 1984, legislation was enacted to create a new noncontributory class for members of the ERS who are also covered under social security. Persons employed in positions not covered by social security were precluded from the noncontributory class. The noncontributory class provides for reduced benefits and covers most eligible employees hired starting July 1, 1984. Employees hired before that date were allowed to continue under the contributory class or to elect the new noncontributory class and receive a refund of employee contributions. In 2004, legislation was enacted to create a hybrid retirement class, which took effect July 1, 2006. Employees in the contributory and noncontributory classes were given the option to join the hybrid class or to remain in their existing class effective July 1, 2006. Starting July 1, 2006, all new employees covered by social security are required to join the hybrid class.

All benefits vest after five or ten years of credited service. Vesting is determined by the employee's class and date of hire. The monthly retirement allowance benefit formula is calculated based on the employee's age, years of credited service, average final compensation ("AFC"), and multiplier.

For employees who became members prior to January 1, 1971, the AFC is the average salary earned during the five highest paid years of service, including the vacation payment or the average salary earned during the three highest paid years of service excluding any lump sum vacation payment. For employees who became members on January 1, 1971 through June 30, 2012, the AFC is based on the three highest paid years of service excluding the vacation payment. For employees who became members after June 30, 2012, the AFC is the highest five years excluding any lump sum vacation payment.

The ERS issues an Annual Comprehensive Financial Report that may be obtained by writing to the Employees' Retirement System of the State of Hawaii, 201 Merchant Street, Suite 1400, Honolulu, Hawaii 96813 or found on the ERS website at <http://ers.hawaii.gov/resources/financials>.

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Contributions

General employees covered under the contributory class and hired prior to July 1, 2012 are required to contribute 7.80% of their salary and will receive pensions based on a 2.00% multiplier. General employees hired after June 30, 2012 are required to contribute 9.80% of their salary with pensions based on a 1.75% multiplier. General employees covered under the hybrid class prior to July 1, 2012 are required to contribute 6.00% of their salary and will receive pensions based on a 2.00% multiplier. General employees hired after June 30, 2012 are required to contribute 8.00% of their salary with pensions based on a 1.75% multiplier. Employees covered under the noncontributory class will receive pensions based on a 1.25% multiplier.

Contributions are established by HRS Chapter 88 and may be amended through legislation. The employer rate is set by statute based on the recommendations of the ERS actuary resulting from an experience study conducted every five years. Since July 1, 2005, the employer contribution rate is a fixed percentage of compensation, including the normal cost plus amounts required to pay for the unfunded actuarial accrued liabilities. The Sewer Fund's contribution requirements for the year ended June 30, 2022 was approximately \$9.5 million.

The City is required to contribute the remaining amounts necessary to pay contributory class benefits and all amounts necessary to pay noncontributory class benefits. The funding method used to calculate the total employer contribution requirement is the Entry Age Normal Actuarial Cost Method.

On May 18, 2017, the Governor signed into law Act 17 (Session Laws of Hawaii ("SLH") 2017), which increased future employer contributions to a phased-in contribution rate increase over four years beginning July 1, 2017. The rate for all employees, other than police and firefighters, increased to 19.00% on July 1, 2018; 22.00% on July 1, 2019; and 24.00% on July 1, 2020 and thereafter.

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

At June 30, 2022, the Sewer Fund reported a liability of \$108.1 million, for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2021 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Sewer Fund's proportion of the net pension liability was based on a projection of the Sewer Fund's long-term share of contributions to the pension plan relative to the projected contributions of all participating members of ERS, actuarially determined. At June 30, 2021, the City's proportion was 18.60%. The Sewer Fund's proportionate share of the City's proportionate share as of June 30, 2021 was 4.76%.

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For the year ended June 30, 2022, the Sewer Fund recognized pension expense of \$6.4 million. At June 30, 2022, the Sewer Fund reported deferred outflows and inflows of resources related to pensions from the following sources (in thousands of dollars):

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between actual and expected experience	\$ 4,536	\$ (824)
Net difference between projected and actual earnings on pension plan investments	-	(22,092)
Changes of assumptions	128	(55)
Changes in proportion and differences between employer contributions and proportionate share of contributions	6,861	(5,887)
Sewer Fund contributions subsequent to the measurement date	9,508	-
	<u>\$ 21,033</u>	<u>\$ (28,858)</u>

The \$9.5 million reported as deferred outflows of resources related to pension at June 30, 2022, resulting from Sewer Fund contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2022. Other amounts reported as deferred outflows and inflows of resources related to pension will be recognized in pension expense as follows (in thousands of dollars):

Years ending June 30,	
2023	\$ (3,856)
2024	(3,558)
2025	(4,411)
2026	(5,714)
2027	206
	<u>\$ (17,333)</u>

Actuarial Assumptions

The total pension liability in the June 30, 2021 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.50 %
Projected salary increases, including inflation	3.50 % – 7.00 %
Investment rate of return, including inflation	7.00 %

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

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There were no other changes in assumptions between the measurement date, June 30, 2021, and the reporting date, June 30, 2022, that are expected to have a significant effect on the proportionate share of the net pension liability.

The post-retirement mortality rates are based on the 2019 Public Retirees of Hawaii mortality table with adjustments based on generational projections of the BB projection table for 2019 and full generational projection in future years. Pre-retirement mortality rates are based on multiples of the Pub-2010 mortality table based on the occupation of the member.

The long-term expected rate of return on pension plan investments was determined using a “top down approach” of the Client-Constrained Simulation-based Optimization Model (a statistical technique known as “resampling with a replacement” that directly keys in on specific plan-level risk factors as stipulated by the ERS’s Board of Trustees) in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future nominal rates of return (real returns and inflation) by the target asset allocation percentage.

The target allocation and best estimate of long-term geometric average strategic range for each major asset class as of June 30, 2021 are summarized in the following table:

Strategic Allocation	Long-Term Target Allocation	Expected Long-Term Geometric Average Strategic Range*
Broad growth	63.00 %	8.00 %
Diversifying strategies	37.00 %	5.10 %
	<u>100.00 %</u>	

* Uses an expected inflation of 2.1%.

Discount Rate

The discount rate used to measure the total pension liability was 7.00%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that employer contributions will be made at rates equal to the difference between actuarially determined contribution rates and the member rate. Based on these assumptions, the pension plan’s fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

City and County of Honolulu
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Sensitivity of the Sewer Fund’s Proportionate Share of the Net Pension Liability to Changes in the Discount Rate

The following presents the Sewer Fund’s proportionate share of the net pension liability calculated using the single discount rate of 7.00%, as well as what the Sewer Fund’s proportionate share of the net pension liability would be if it were calculated using a single discount rate that is one percentage point lower or one percentage-point higher than the current rates (in thousands of dollars):

	1% Decrease (6.00%)	Current Discount Rate (7.00%)	1% Increase (8.00%)
Sewer Fund’s proportionate share of the net pension liability	<u>\$ 152,508</u>	<u>\$ 108,121</u>	<u>\$ 71,527</u>

Pension Plan Fiduciary Net Position

The pension plan’s fiduciary net position is determined on the same basis used by the pension plan. The ERS financial statements are prepared using the accrual basis of accounting under which expenses are recorded when the liability is incurred, and revenues are recorded in the accounting period in which they are earned and become measurable. Employer and member contributions are recognized in the period in which the contributions are due. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. Investment purchases and sales are recorded as of their trade date. Administrative expenses are financed exclusively with investment income. There were no significant changes after the June 30, 2021 measurement date.

Payables to the Pension Plan

At June 30, 2022, the Sewer Fund had no payable to ERS.

Postemployment Healthcare and Life Insurance Benefits

Plan Description

Pursuant to Act 88 (SLH 2001), the employers provide certain health care (medical, prescription, vision and dental) and life insurance benefits to all qualified employees. The EUTF, established on July 1, 2003, is an agent, multiple-employer defined benefit plan.

The EUTF issues a stand-alone financial report that is publicly available at <https://eutf.hawaii.gov>. Questions concerning any of the information contained therein or requests for any additional financial information related to that report should be addressed to EUTF, P.O. Box 2121, Honolulu, Hawaii 96805-2121.

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City Policy

The actuarial valuation of the EUTF does not provide OPEB information by department or agency. Accordingly, the City’s policy on the accounting and reporting for OPEB is to allocate a portion of the City’s net OPEB liability, deferred inflows and outflows, and OPEB expense to proprietary funds that are reported separately in stand-alone financial statements or in the City’s ACFR. The basis for the allocation is the proportionate share of contributions made by each proprietary fund for retiree health benefits.

Benefits Provided

For employees hired before July 1, 1996, the employers pay 100% of the base monthly contribution for employees retiring with ten or more years of credited service, and 50% of the base monthly contribution for employees retiring with fewer than ten years of credited service. The employers’ contributions are based on the plan (single, two-party or family) selected by the retiree.

For employees hired after June 30, 1996 and retiring with 25 years or more of service, the employers pay the entire base monthly contribution. For employees retiring with at least 15 years but fewer than 25 years of service, the employers pay 75% of the base monthly contribution. For those retiring with at least ten years but fewer than 15 years of service, the employers pay 50% of the base monthly contribution. For those retiring with fewer than ten years of service, the employers make no contributions. If the retiree was hired before July 1, 2001, the employers’ contributions are based on the plan (single, two-party or family) selected by the retiree. If the retiree was hired on or after July 1, 2001, the employers are responsible for the single plan base monthly contribution while the retiree must pay the difference if family coverage is elected.

Employees Covered by Benefit Terms

At July 1, 2021, the City had the following number of plan members covered:

Inactive plan members or beneficiaries currently receiving benefits	7,730
Inactive plan members entitled to but not yet receiving benefits	788
Active plan members	<u>8,674</u>
Total plan members	<u><u>17,192</u></u>

Contributions

Act 268 (SLH 2013) required EUTF to establish and administer separate trust accounts for each public employer for the purpose of receiving irrevocable employer contributions to prefund OPEB for retirees and their beneficiaries. It established the Hawaii EUTF Trust Fund Task Force to examine further steps to address the unfunded liability and requires all public employers to make their annual required contributions (now known as actuarially determined contributions) effective with fiscal year 2014.

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The employers' OPEB contributions (comprised of pay-as-you-go retiree costs and prefunding amounts paid to EUTF) are established by Hawaii State statutes. The retiree is responsible to pay the difference if the single plan base monthly contribution is less than the cost of the monthly premium for those employees hired on or after July 1, 2001. For fiscal years 2019 through 2021, the employers' prefunding contribution shall be equal to 100% of the valuation amount determined by an actuary retained by the EUTF board. Commencing with fiscal year 2019, the annual contribution shall be equal to the actuarially determined amount. In any fiscal year, should an employer's contribution be less than the actuarially determined amount, the difference shall be transferred to the OPEB trust account from the employer's portion of the transient accommodations tax revenues and all other of its revenues held by the State.

The Governor's Fourteenth Supplementary Proclamation, issued on October 13, 2020, suspended specific provisions of law. Included were Sections 87A-42(b) – (f), HRS, *other postemployment benefits trust*, 87A-43, HRS, *payment of public employer contributions to the other postemployment benefits trust*, and 237-31(3), HRS, *remittances*, related to the requirement for public employers to pay the annual required contribution to the EUTF in fiscal year 2021. This relief provision was extended to fiscal year 2022 and 2023 by Act 229, SLH 2021. The City did not utilize this relief provision for fiscal year 2022.

OPEB contributions for the year ended June 30, 2022 amounted to approximately \$10.4 million. The employer is required to make all contributions for members.

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

At June 30, 2022, the Sewer Fund reported a liability of \$83.9 million, respectively, for its proportionate share of net OPEB liability. The net OPEB liability was measured as of July 1, 2021 and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of that date. The City's proportion of the net OPEB liability was based on a projection of the City's long-term share of contributions to the EUTF relative to projected contributions of all participants, actuarially determined. The City's proportion of the net OPEB liability was based on an allocation of the City's net OPEB liability based on the proportionate share of qualified payroll. At June 30, 2021, the Sewer Fund's share of the City's net OPEB liability was 5.70%.

There were no changes in assumptions between the measurement date, July 1, 2021, and the reporting date, June 30, 2022, that are expected to have a significant effect on the proportionate share of the net OPEB liability.

City and County of Honolulu
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Notes to Financial Statements
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For the year ended June 30, 2022, the Sewer Fund recognized OPEB expense of approximately \$7.8 million. At June 30, 2022, the Sewer Fund reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources (in thousands of dollars):

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ -	\$ (10,776)
Changes of assumptions	1,029	(519)
Net difference between projected and actual earnings on OPEB plan investments	-	(4,986)
Change in proportionate share between City funds	-	(6,219)
Sewer Fund contributions subsequent to the measurement date	10,449	-
	<u>\$ 11,478</u>	<u>\$ (22,500)</u>

The \$10.4 million reported as deferred outflows of resources related to OPEB at June 30, 2022 resulting from Sewer Fund's contribution subsequent to measurement date will be recognized as a reduction of the net OPEB liability in the year ending June 30, 2022. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows:

Years ending June 30,	
2023	\$ (5,019)
2024	(4,985)
2025	(5,112)
2026	(5,094)
2027	(1,261)
	<u>\$ (21,471)</u>

City and County of Honolulu
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June 30, 2022

Actuarial Assumptions

The total OPEB liability reflected in the actuarial valuation report as of July 1, 2021 was determined using the following actuarial assumptions and methods, applied to all periods including in the measurement, unless otherwise specified:

Valuation date	July 1, 2021
Actuarial cost method	Entry age normal
Discount rate	7.00%
Inflation	2.50%
Salary increases	3.50% to 7.00% including inflation
Demographic assumptions	Based on the experience study covering the five-year period ended June 30, 2018 as conducted for the ERS
Mortality	System-specific mortality tables utilizing scale BB to project generational mortality improvement
Participation rates	98% healthcare participation assumption for retirees that receive 100% of the Base Monthly Contribution ("BMC"). Healthcare participation rates of 25%, 65% and 90% for retirees that receive 0%, 50% or 75% of the BMC, respectively. 100% for life insurance and 98% for Medicare Part B
Healthcare cost trend rates	
PPO*	Initial rate of 7.25% declining to a rate of 4.70% after 12 years
HMO*	Initial rate of 7.25% declining to a rate of 4.70% after 12 years
Part B & BMC	Initial rates of 5.00% declining to a rate of 4.70% after 9 years
Dental	4.00%
Vision	2.50%
Life insurance	0.00%

* Blended rates for medical and prescription drugs.

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The long-term expected rate of return on EUTF’s investments was determined using a building-block method in which best-estimate ranges of expected future real rate of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Long-Term Target Allocation	Long-Term Expected Real Rate of Return
Private equity	12.5 %	10.19 %
U.S. microcap	6.0 %	7.62 %
U.S. equity	16.0 %	6.09 %
Non-U.S. equity	11.5 %	7.12 %
Global options	5.0 %	4.33 %
Real Assets	10.0 %	6.16 %
Private Credit	8.0 %	5.83 %
TIPS	5.0 %	(0.07%)
Long Treasuries	6.0 %	1.06 %
Alternative Risk Premia	5.0 %	1.46 %
Trend Following	10.0 %	2.01 %
Reinsurance	5.0 %	4.44 %
	100.0 %	

Single Discount Rate

The discount rate used to measure the net OPEB liability was 7.00%, based on the expected rate of return on OPEB plan investments of 7.00%. Beginning with the fiscal year 2019 contribution, the Sewer Fund’s funding policy is to pay the recommended actuarially determined contribution, which is based on layered, closed amortization periods. Based on those assumptions, the OPEB plan’s fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive plan members. In July 2020, the Governor’s office issued the Tenth Proclamation related to the COVID-19 Emergency, allowing employers of the EUTF to suspend ACT 268 contributions for year ended June 30, 2021 and instead limit their contribution amounts to the OPEB benefits due. This temporary ACT 268 suspension would not derail the plan’s long-term funding progress. Even if ACT 268 is suspended through the year ending June 30, 2025, the OPEB plan’s fiduciary net position is expected to be available to make all projected future benefit payments of current plan members. Act 229, SLH 2021 suspends the contribution requirement for fiscal years 2022 and 2023. The City made its full Annual Required Contributions in fiscal year 2022 and intends to make contributions for fiscal year 2023. Therefore, the long-term expected rate of return on OPEB plan investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

City and County of Honolulu
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June 30, 2022

Changes in Net OPEB Liability

The following table represents a schedule of changes in the net OPEB liability (amounts in thousands). The ending balances are as of the measurement date, July 1, 2021.

	Total OPEB Liability	Plan Fiduciary Net Position	Net OPEB Liability
Balance at June 30, 2021	\$ 144,879	\$ 43,192	\$ 101,687
Service cost	2,655	-	2,655
Interest on the total OPEB liability	9,724	-	9,724
Difference between expected and actual experience	(4,746)	-	(4,746)
Employer contributions	-	12,806	(12,806)
Net investment income	-	11,131	(11,131)
Benefit payments	(4,756)	(4,756)	-
Administrative expense	-	(6)	6
Other	(4,912)	(3,444)	(1,468)
Net changes	<u>(2,035)</u>	<u>15,731</u>	<u>(17,766)</u>
Balance at June 30, 2022	<u>\$ 142,844</u>	<u>\$ 58,923</u>	<u>\$ 83,921</u>

***Sensitivity of the Net OPEB Liability to Changes in the Discount Rate
and Healthcare Cost Trend Rates***

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

	1% Decrease (6.00%)	Current Discount Rate (7.00%)	1% Increase (8.00%)
Sewer Fund's proportionate share of the net OPEB liability	<u>\$ 106,059</u>	<u>\$ 83,921</u>	<u>\$ 66,525</u>

The following table presents the Sewer Fund's net OPEB liability calculated using the assumed healthcare cost trend rate, as well as what the Sewer Fund's net OPEB liability would be if it were calculated using the trend rate that is one percentage point lower or one percentage point higher than the current healthcare cost trend rate (amounts in thousands):

	1% Decrease	Healthcare Cost Trend	1% Increase
Sewer Fund's proportionate share of the net OPEB liability	<u>\$ 65,816</u>	<u>\$ 83,921</u>	<u>\$ 107,264</u>

Payables to the OPEB Plan

At June 30, 2022, the Sewer Fund had no payables to EUTF.

City and County of Honolulu
Sewer Fund
Notes to Financial Statements
June 30, 2022

10. Management Agreement

The Board of Water Supply (“BWS”) has an agreement with the City’s Department of Environmental Services to provide certain services through June 30, 2024, for the billing and collection of sewer service charges. These fees are included in contractual services expense in the Sewer Fund. Service fees, in addition to credit card fees incurred, amounted to approximately \$3.5 million for the year ended June 30, 2022.

11. Commitments

Construction Contracts

The City has contractual commitments for the Sewer Fund of approximately \$1.1 billion at June 30, 2022, primarily for construction contracts.

Accumulated Sick Leave Pay

Sick leave accumulates at the rate of one and three-quarters working days for each month, without limit. Sick leave is taken only in the event of illness and is not convertible to pay; accordingly, sick leave is not accrued. Employees who retire or leave government service in good standing with sixty or more unused sick leave days are entitled to an additional service credit in the retirement system. At June 30, 2022, accumulated sick leave, including vested and nonvested accumulated rights to receive sick leave benefits, amounted to approximately \$16.2 million.

Deferred Compensation Plan

All full-time employees of the Sewer Fund are eligible to participate in the City’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. Deferred compensation plan assets are not reported in the financial statements.

Environmental Protection Agency Consent Decree

The Wastewater Treatment Plants (“WWTP”) and other facilities operated by the Department are governed either by National Pollutant Discharge Elimination System (“NPDES”) permits or by the DOH Underground Injection Control or Wastewater Management Permits or Clean Air Branch Covered Source and Non-Covered Source Permits.

The City is contesting certain conditions for the Waianae WWTP NPDES permit. The matter is currently pending before the Intermediate Court of Appeals on a procedural issue.

City and County of Honolulu
Sewer Fund
Notes to Financial Statements
June 30, 2022

In addition, during the course of operating the wastewater system, occasional events of non-compliance with other permits, laws and regulations occur, including:

- Wastewater spills, which are subject to reporting pursuant to the NPDES permits, the 2010 Consent Decree described below, and DOH regulations.
- Exceedance of interim effluent limits set forth in the 2010 Consent Decree for the Sand Island and Honouliuli WWTPs, which are reported monthly with the discharge monitoring reports for the plants.
- On August 11, 2020, DOH issued a Notice of Apparent Violation and Request for Information regarding the City's Honouliuli WWTP. The City responded on September 10, 2020.
- On July 1, 2021, the Environmental Protection Agency ("EPA") transmitted a Notice of Opportunity to Resolve Clean Water Act Violations regarding the City's Kailua Regional WWTP. Settlement negotiations are ongoing.
- On February 25, 2022, DOH transmitted a Request for Information regarding sanitary sewer overflows within the Sand Island WWTP collection system. The City provided an initial response on March 30, 2022, with a supplementary response provided on April 14, 2022.
- On May 11, 2022, DOH issued a Notice of Apparent Violation and Request for Information regarding the City's Honouliuli WWTP. The City responded on June 6, 2022.
- No other incident of noncompliance is subject to existing or threatened enforcement.

The City is complying with the terms of a consent decree (the "2010 Consent Decree") entered by the United States District Court in Hawaii to settle certain previous environmental lawsuits relating to the Wastewater System. The Court retains continuing jurisdiction to enforce the 2010 Consent Decree. The following is a brief discussion of the 2010 Consent Decree and the City's obligations thereunder.

The 2010 Consent Decree, approved by the EPA, DOH, the Sierra Club, Hawaii Chapter, Our Children's Earth Foundation, and Hawaii's Thousand Friends, was entered by the United States District Court in Hawaii. Three previous environmental lawsuits were dismissed. The City's appeal of the EPA's January 2009 final decisions denying the City's applications to renew its permit variances from secondary treatment for the Honouliuli and Sand Island WWTP was dismissed on February 2, 2011. The 2010 Consent Decree allows 10 years for completion of work on the collection system, 14 years for the upgrade of the Honouliuli WWTP to secondary treatment, and up to 25 years, with the possibility of a three-year extension, for the upgrade of the Sand Island WWTP to secondary treatment. The City provided \$2.84 billion in capital funding for mandated projects from fiscal year 2009 through fiscal year 2021 (which includes the 10-year collection system portion of the consent decree). Of this amount, \$1.39 billion was

City and County of Honolulu
Sewer Fund
Notes to Financial Statements
June 30, 2022

provided for the collection system, much of this going toward work that was already required or planned. The amount for treatment plan included \$500 million for upgrades at Honouliuli, and \$750 million for the first phases of the upgrades at Sand Island. The second phase of the Sand Island upgrade is expected to incur approximately \$2.0 billion in capital costs from fiscal year 2022 through fiscal year 2034. As part of the settlement, the City paid a civil penalty in the amount of \$800,000 to the United States, and \$800,000 to the State. In addition, the City paid \$800,000 to the Sierra Club, Hawaii Chapter, Our Children's Earth Foundation, and Hawaii's Thousand Friends, to fund four supplemental environmental projects. The Honouliuli WWTP and Sand Island WWTP upgrades are expected to be completed by 2024 and 2035, respectively.

The 2010 Consent Decree became effective upon its entry by the Court on December 17, 2010. The City also settled the nonprofit organizations' claim for their attorneys' fees and costs for an additional payment of \$1.1 million.

Certification of the City's fulfillment of the collection system portion of the Consent Decree was approved via letter from the EPA and DOH dated January 28, 2021. The City had additionally obtained an extension to complete a single remaining collection system project, SI-CS-10, which was timely completed on April 20, 2022.

Pending Wastewater System Litigation

The City and the Department generally are self-insured with respect to general liability claims. During the year ended June 30, 2022, the Department reached settlements of lawsuits and claims related to the Wastewater System and paid judgment, settlements and losses with general funds approximating \$385,000.

The City's Corporation Counsel is of the opinion that the expected liability arising out of any pending litigation would not constitute a material impairment of the Department's financial position.

**Required Supplementary Information
(Unaudited)**

City and County of Honolulu
Sewer Fund
Schedule of the City's Proportionate Share of the Net Pension Liability
Last Ten Fiscal Years*
(Amounts in thousands)

Defined Benefit Plan

The following presents the Schedule of the City's Proportionate Share of the Net Pension Liability for the City as a whole, of which the Sewer Fund is one of its various enterprise funds.

Measurement Period	Proportion of Net Pension Liability	Proportionate Share of Net Pension Liability	Covered Payroll	Proportionate Share of Net Pension Liability as a Percentage of Covered Payroll	Plan Fiduciary Net Position as a Percentage of Total Pension Liability
Years ending June 30,					
2021	18.60 %	\$ 2,270,106	\$ 700,332	324.15 %	64.25 %
2020	19.08 %	2,919,908	689,084	423.74 %	53.18 %
2019	18.81 %	2,665,560	666,311	400.05 %	54.87 %
2018	18.20 %	2,424,496	640,203	378.71 %	55.48 %
2017	17.82 %	2,307,225	626,639	368.19 %	54.80 %
2016	18.17 %	2,428,894	599,494	405.16 %	51.28 %
2015	17.41 %	1,520,529	578,043	263.05 %	62.42 %
2014	16.31 %	1,307,396	536,304	243.78 %	63.92 %
2013	16.76 %	1,496,794	509,130	293.99 %	57.96 %

* Prior fiscal years are not available. Table will be built prospectively.

See accompanying independent auditors' report.

City and County of Honolulu

Sewer Fund

Notes to Schedule of the City's Proportionate Share of the Net Pension Liability

Last Ten Fiscal Years

(Amounts in thousands)

There were no significant changes in actuarial assumptions for the measurement period June 30, 2021.

Contribution rates are a percentage of pensionable payroll and are set by statute based on the recommendation of the ERS actuary. Act 256 (SLH 2007) established contribution rates beginning July 1, 2008 through June 30, 2012. Act 163 (SLH 2011) established contribution rates beginning July 1, 2012 through July 1, 2015. Act 17 (SLH 2017) established new contribution rates beginning July 1, 2017 until statutory changes are implemented. Contribution rates by year are as follows:

Effective Starting	Police and Fire	General Employees
July 1, 2020 and thereafter	41.0 %	24.0 %
July 1, 2019	36.0 %	22.0 %
July 1, 2018	31.0 %	19.0 %
July 1, 2017	28.0 %	18.0 %
July 1, 2015	25.0 %	17.0 %
July 1, 2014	24.0 %	16.5 %
July 1, 2013	23.0 %	16.0 %

Act 152 (SLH 2012) amended the definition of compensation for new employees hired after June 30, 2012 for the purpose of pension benefit calculations. Compensation is defined as normal periodic payments and does not include overtime, supplemental payments, bonuses, lump sum salary differentials, and other types of differentials. For employees hired prior to July 1, 2012, compensation includes overtime, supplemental payments, bonuses, and other types of differentials for the purpose of pension benefit calculations.

Act 153 (SLH 2012) requires employers to pay additional contributions for those employees who retire on or after July 1, 2012 with significant "non-base pay" increases in the three or five years used to calculate their average final compensation and maximum retirement allowances. The amount is determined by comparing the maximum retirement allowance that would have been received without the significant non-base pay increase to the actual maximum allowance. These amounts are assessed, on a fiscal year basis, for all retirees meeting the criteria during the previous fiscal year.

See accompanying independent auditors' report.

City and County of Honolulu
Sewer Fund
Schedule of Pension Contributions
Last Ten Fiscal Years
(Amounts in thousands)

Defined Benefit Plan

The following presents the Schedule of Pension Contributions for the City as a whole, of which the Sewer Fund is one of its various enterprise funds.

Years ending June 30,	Statutorily Required Contributions	Contributions in Relation to Statutorily Required Contributions	Contribution Excess (Deficiency)	Covered Payroll	Contributions as a Percentage of Covered Payroll
2022	\$ 253,897	\$ 253,756	\$ (141)	\$ 673,922	37.65 %
2021	245,875	245,628	(247)	700,332	35.07 %
2020	212,405	212,694	289	689,084	30.87 %
2019	176,114	176,416	302	666,311	26.48 %
2018	152,657	157,686	5,029	640,203	24.63 %
2017	140,342	139,569	(773)	626,639	22.27 %
2016	135,217	129,245	(5,972)	599,494	21.56 %
2015	121,465	132,308	10,843	578,043	22.89 %
2014	102,885	87,979	(14,906)	536,304	16.40 %
2013	93,503	87,840	(5,663)	509,130	17.25 %

See accompanying independent auditors' report.

City and County of Honolulu
Sewer Fund
Schedule of Changes in Net OPEB Liability and Related Ratios
Last Ten Fiscal Years*
(Amounts in thousands)

Postemployment Healthcare and Life Insurance Benefits

The following presents the Schedule of Changes in Net OPEB Liability and Related Ratios, for the City as a whole, of which the Sewer Fund is one of its various enterprise funds.

	2021	2020	2019	2018	2017
Total other postemployment benefits ("OPEB") liability					
Service cost	\$ 46,591	\$ 48,212	\$ 45,917	\$ 44,698	\$ 43,835
Interest on the total OPEB liability	170,600	173,113	163,723	155,684	147,732
Difference between expected and actual experience in the measurement of total OPEB liability	(83,264)	(158,493)	(9,002)	(36,127)	-
Changes of assumptions	-	(13,867) **	16,227	31,781	-
Benefit payments	(83,430)	(84,672)	(83,074)	(80,555)	(76,220)
Net change in total OPEB liability	50,497	(35,707) **	133,791	115,481	115,347
Total OPEB liability – beginning	2,455,565	2,491,272	2,357,481	2,242,000	2,126,653
Total OPEB liability – ending	<u>\$ 2,506,062</u>	<u>\$ 2,455,565 **</u>	<u>\$ 2,491,272</u>	<u>\$ 2,357,481</u>	<u>\$ 2,242,000</u>
Plan fiduciary net position					
Employer contributions	\$ 190,106	\$ 183,677	\$ 177,331	\$ 143,665	\$ 125,017
Net investment income	195,285	13,620	22,566	30,844	30,907
Benefit payments	(83,430)	(84,672)	(83,074)	(80,555)	(76,220)
OPEB plan administrative expense	(100)	(102)	(169)	(95)	(72)
Other	(156)	(153)	36,505	-	1,147
Net change in plan fiduciary net position	301,705	112,370	153,159	93,859	80,779
Plan fiduciary net position – beginning	732,059	619,689	466,530	372,671	291,892
Plan fiduciary net position – ending	<u>1,033,764</u>	<u>732,059</u>	<u>619,689</u>	<u>466,530</u>	<u>372,671</u>
Net OPEB liability – ending	<u>\$ 1,472,298</u>	<u>\$ 1,723,506 **</u>	<u>\$ 1,871,583</u>	<u>\$ 1,890,951</u>	<u>\$ 1,869,329</u>
Plan fiduciary net position as a percentage of total OPEB liability	41.25 %	29.81 %	24.87 %	19.79 %	16.62 %
Covered-employee payroll	\$ 712,833	\$ 689,783	\$ 667,656	\$ 648,001	\$ 626,639
Net OPEB liability as a percentage of covered-employee payroll	206.54 %	249.86 %	280.32 %	291.81 %	298.31 %

* Data for prior fiscal years is not available. Table will be built prospectively.

** Revised from previous financial statements.

See accompanying independent auditors' report.

City and County of Honolulu
Sewer Fund
Schedule of OPEB Contributions
Last Ten Fiscal Years*
(Amounts in thousands)

Postemployment Healthcare and Life Insurance Benefits

The following presents the Schedule of OPEB Contributions for the City as a whole, of which the Sewer Fund is one of its various enterprise funds.

	Actuarially Determined Contribution	Actual Contribution	Contribution Excess (Deficiency)	Covered Employee Payroll	Contributions as a Percentage of Covered Employee Payroll
Years ending June 30,					
2022	\$ 197,569	\$ 197,569	\$ -	\$ 673,922	29.32 %
2021	190,106	190,106	-	712,833 **	26.67 % **
2020	183,677	183,677	-	689,783	26.63 %
2019	177,331	177,331	-	667,656	26.56 %
2018	166,876	143,665	(23,211)	648,001	22.17 %

* Information prior to the year ended June 30, 2018 is not available. As information becomes available in future years, up to ten years will be displayed prospectively.

** Revised from previous financial statements.

See accompanying independent auditors' report.

City and County of Honolulu
Sewer Fund
Notes to Schedule of OPEB Contributions
Year Ended June 30, 2022

Valuation date	The actuarially determined contribution for fiscal year ended June 30, 2022 was developed in the July 1, 2019 valuation.
Actuarial cost method	Entry age normal
Discount rate	7.00%
Inflation	2.50%
Amortization method*	Level percent, closed
Equivalent single amortization period	17.2% as of fiscal year ended June 30, 2022
Payroll growth	3.50%
Asset method	4-year smoothed
Salary increases	3.50% to 7.00%; including inflation
Demographic assumptions	Based on the experience study covering the five-year period ended June 30, 2018 as conducted for the ERS
Mortality	System-specific mortality tables utilizing scale BB to project generational mortality improvement
Participation rates	98.00% healthcare participation assumptions for retirees that receive 100% of the Base Monthly Contribution (“BMC”). Healthcare participation rates of 25%, 65% and 90% for retirees that receive 0%, 50% or 75% of the BMC, respectively. 100% for life insurance and 98% for Medicare Part B
Healthcare cost trend rates	
PPO**	Initial rate of 8.00% declining to a rate of 4.86% after 12 years
HMO**	Initial rate of 8.00% declining to a rate of 4.86% after 12 years
Part B & Base Monthly Contribution (“BMC”)	Initial rate of 5.00%, declining to a rate of 4.70% after 11 years
Dental	5.00% for the first two years, then 4.00% for all future years
Vision	0.00% for the first two years, then 2.50% for all future years
Life insurance	0.00%

* Closed bases are established at each valuation for new unfunded liabilities.

** Blended rates for medical and prescription drugs.

See accompanying independent auditors’ report.