



Department of Education State of Hawaii

Financial Statements and Single Audit Reports
(With Independent Auditors' Reports Thereon)

June 30, 2018

Submitted by
THE AUDITOR
STATE OF HAWAII

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Financial Statements and Single Audit Reports

June 30, 2018

Table of Contents

	Page
PART I – INTRODUCTION SECTION	
Audit Objectives	1
Scope of Audit	2
Organization of Report	2
PART II – FINANCIAL SECTION	
Independent Auditors’ Report	3
Management’s Discussion and Analysis	6
Financial Statements:	
Government-wide Financial Statements:	
Statement of Net Position	12
Statement of Activities	13
Fund Financial Statements:	
Balance Sheet – Governmental Funds	14
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position	15
Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds	16
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to Statement of Activities	17
Statement of Revenues and Expenditures – Budget and Actual (Non-GAAP Budgetary Basis) – General Fund	18

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Financial Statements and Single Audit Reports

June 30, 2018

Table of Contents

	Page
Statement of Revenues and Expenditures – Budget and Actual (Non-GAAP Budgetary Basis) – Federal Fund	19
Statement of Fiduciary Net Position – Agency Funds	20
Notes to Financial Statements	21
Supplementary Information:	
Schedule of Expenditures of Federal Awards	44
Notes to the Schedule of Expenditures of Federal Awards	47
 PART III – INTERNAL CONTROL OVER FINANCIAL REPORTING AND COMPLIANCE	
Independent Auditors’ Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	48
 PART IV – COMPLIANCE AND INTERNAL CONTROL OVER FEDERAL AWARDS	
Independent Auditors’ Report on Compliance for Each Major Federal Program and Report on Internal Control over Compliance Required by the Uniform Guidance	50
Schedule of Findings and Questioned Costs	53
 PART V – CORRECTIVE ACTION PLAN	
Response of the Department of Education	60
 PART VI – SUMMARY SCHEDULE OF PRIOR AUDIT FINDING	
Status Report	67

PART I

INTRODUCTION SECTION

March 25, 2019

The Auditor
State of Hawaii

Board of Education
Department of Education
State of Hawaii:

We have completed our audit of the financial statements of the Department of Education, State of Hawaii (the Department), as of and for the fiscal year ended June 30, 2018. We have also audited the Department's compliance with the requirements applicable to its major federal programs for the fiscal year ended June 30, 2018. We transmit herewith our reports pertaining to our audit of the Department's financial statements and its major federal programs.

Audit Objectives

The objectives of the audit were as follows:

1. To provide opinions on the fair presentation of the Department's financial statements and the schedule of expenditures of federal awards in accordance with accounting principles generally accepted in the United States of America.
2. To consider the Department's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements.
3. To perform tests of the Department's compliance with certain provisions of laws, regulations, contracts, and grant agreements, non-compliance with which could have a direct and material effect on the determination of financial statement amounts.
4. To consider the Department's internal control over compliance with requirements that could have a direct and material effect on each of its major federal programs in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, and to test and report on internal control over compliance.
5. To provide an opinion on the Department's compliance with applicable laws, regulations, contracts, and grants that could have a direct and material effect on each of its major federal programs.

Scope of Audit

Our audit of the Department's financial statements, the schedule of expenditures of federal awards, and the Department's compliance with the requirements applicable to each of its major federal programs was performed in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the Uniform Guidance).

Organization of Report

This report has been organized into six parts as follows:

1. The Introduction Section describes briefly the objectives and scope of our audit and the organization and contents of this report.
2. The Financial Section includes management's discussion and analysis, the Department's financial statements and the related notes as of and for the fiscal year ended June 30, 2018, the schedule of expenditures of federal awards for the fiscal year ended June 30, 2018 and related notes, and our independent auditors' report thereon.
3. The Internal Control Over Financial Reporting and Compliance Section contains our independent auditors' report on the Department's internal control over financial reporting and on compliance and other matters based on an audit of financial statements performed in accordance with *Government Auditing Standards*.
4. The Compliance and Internal Control Over Federal Awards Section contains our independent auditors' report on compliance for the Department's major federal programs and on internal control over compliance required by the Uniform Guidance, and a schedule of findings and questioned costs.
5. The Corrective Action Plan Section contains the Department's responses to the audit findings described in the schedule of findings and questioned costs.
6. The Summary Schedule of Prior Audit Finding Section contains the Department's status on the prior audit finding.

* * * * *

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

Very truly yours,

KKDLY LLC

PART II
FINANCIAL SECTION

Independent Auditors' Report

The Auditor
State of Hawaii

Board of Education
Department of Education
State of Hawaii:

Report on the Financial Statements

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

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of certain public charter schools which represent 2% of the total assets and 2% of total fund balances as of June 30, 2018, and 3% of total revenues for the fiscal year ended June 30, 2018, of the Department's governmental funds. Those statements were audited by other auditors, whose reports have been furnished to us, and our opinions, insofar as it relates to the amounts included for the public charter schools, are based solely on the reports of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinions

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Department as of June 30, 2018, and the respective changes in financial position, and, where applicable, the respective budgetary comparison for the General Fund and Federal Fund for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

Change in Accounting Principle

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

Relationship to the State of Hawaii

As discussed in Note 1 to the financial statements, the financial statements of the Department are intended to present the financial position, the changes in financial position, and budgetary comparison of only that portion of the governmental activities, each major fund, and the aggregate remaining fund information of the State of Hawaii that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State of Hawaii as of June 30, 2018, and the changes in its financial position and budgetary comparison for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinions are not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied

certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

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

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 25, 2019, on our consideration of the Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Department's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Department's internal control over financial reporting and compliance.

KKDL Y LLC

Honolulu, Hawaii
March 25, 2019

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Management's Discussion and Analysis

June 30, 2018

As management of the Department of Education, State of Hawaii (the Department) we offer readers this narrative overview and analysis of the financial activities of the Department as of and for the fiscal year ended June 30, 2018. We encourage readers to consider the information presented here in conjunction with the accompanying financial statements and notes to enhance their understanding of the Department's financial performance.

The financial statements represent the combination of Department of Education (the DOE), the Hawaii State Public Library System (the HSPLS), and the Public Charter Schools (the PCS) where the DOE prepares entries, based on information provided by the HSPLS and the PCS, to combine financial data for the three units, in aggregate known as the Department. The fiscal and oversight authority for the DOE, the HSPLS, and the PCS are managed independently. The DOE has determined that the PCS balances are significant, but not material, and relies on certain financial information which have been audited by other auditors and coordinated by the PCS.

FINANCIAL HIGHLIGHTS

Key government-wide financial highlights for fiscal year ended June 30, 2018 (FY 2018) compared to the prior fiscal year ended June 30, 2017 (FY 2017) are as follows:

- Total FY 2018 revenues were \$3.318 billion, an increase of 14% or \$403 million from \$2.915 billion in FY 2017.
- Total FY 2018 expenses were \$3.009 billion, an increase of 7% or \$192 million from \$2.818 billion in FY 2017.
- Of the total FY 2018 expenses of \$3.009 billion, 94% or \$2.815 billion was spent for school-related activities. Of the total FY 2017 expenses of \$2.818 billion, 92% or \$2.596 billion was spent for school-related activities.
- Total assets exceeded liabilities as of June 30, 2018 by \$2.635 billion (net position), compared to \$2.330 billion as of June 30, 2017, an increase of 13%.
- Capital assets, net of accumulated depreciation, comprised of 68% and 70% of the total net position as of June 30, 2018 and 2017, respectively.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Management's Discussion and Analysis

June 30, 2018

OVERVIEW OF THE FINANCIAL STATEMENTS

The Department's financial statements which are comprised of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to financial statements.

- *Government-wide financial statements* – These statements provide a broad overview of the Department's finances, in a manner similar to a private sector business.

The statement of net position present information on all of the Department's assets and liabilities, with the difference between the two 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 Department is improving or deteriorating.

The statement of activities presents information showing how the Department's net position changed during the fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

- *Fund financial statements* – A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Department has two types of funds: governmental funds and fiduciary funds.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, the governmental funds financial statements focus on near-term inflows and outflows of spendable resources, as well as on the balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the Department's near-term financial position. The Department presents four major funds in the fund financial statements: (1) General Fund, (2) Federal Fund, (3) Capital Projects Fund, and (4) Other Fund.

The Department has an annual appropriated budget for its general and federal funds. A budgetary comparison schedule has been provided for these funds to demonstrate compliance with the budget.

Fiduciary funds are used to account for resources held for the benefit of parties outside the Department. The Department reports on agency funds (or student activity funds as the term is used in the schools), which are held in a custodial capacity for students' school activities that take place outside of the formal class period and are not requirements for class work or credit. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the Department's programs.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Management's Discussion and Analysis

June 30, 2018

- *Notes to Financial Statements* – The notes to financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

The following discussion highlights management's understanding of the key aspects of the Department's financial activities.

**Summary Schedule of Net Position
June 30, 2018 and 2017
(Amounts in millions)**

	Governmental Activities		2018-2017	
	2018	2017	Increase (Decrease)	Percentage Change
Assets:				
Current	\$ 1,362.8	\$ 1,175.7	\$ 187.1	16 %
Capital assets, net	1,785.7	1,631.5	154.2	9 %
Total assets	<u>\$ 3,148.5</u>	<u>\$ 2,807.2</u>	<u>\$ 341.3</u>	12 %
Liabilities:				
Current	\$ 348.3	\$ 341.4	\$ 6.9	2 %
Noncurrent	164.9	135.8	29.1	21 %
Total liabilities	<u>513.2</u>	<u>477.2</u>	<u>36.0</u>	8 %
Net position:				
Investment in capital assets	1,785.7	1,631.5	154.2	9 %
Unrestricted	849.6	698.5	151.1	22 %
Total net position	<u>2,635.3</u>	<u>2,330.0</u>	<u>305.3</u>	13 %
Total liabilities and net position	<u>\$ 3,148.5</u>	<u>\$ 2,807.2</u>	<u>\$ 341.3</u>	12 %

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Management's Discussion and Analysis

June 30, 2018

Overall Financial Position - The Department's overall net position has increased as of June 30, 2018 compared to the prior fiscal year-end. The Department's largest portion of net position is investment in capital assets (e.g., land, buildings, equipment), which are unavailable for future spending. The Department's unrestricted portion of net position is available for future spending. The Department's unrestricted portion of net position is available for future use to provide program services. Total government-wide net position increased by \$305 million, or 13%, primarily due to an increase in unrestricted net position.

**Summary Schedule of Changes in Net Position
Fiscal Years 2018 and 2017
(Amounts in millions)**

	Governmental Activities		2018 - 2017	
	2018	2017	Increase (Decrease)	Percentage Change
Revenues:				
Program revenues:				
Charges for services	\$ 66.6	\$ 59.4	\$ 7.2	12 %
Operating grants and contributions	284.4	269.0	15.4	6 %
Capital grants and contributions	1.1	1.7	(0.6)	(35) %
General revenues:				
State allotted appropriations, net of lapses	2,267.5	1,987.6	279.9	14 %
Non-imposed employee wages and fringe benefits	697.4	597.1	100.3	17 %
Unrestricted investment earnings	1.0	0.6	0.4	67 %
Total revenues	<u>3,318.0</u>	<u>2,915.4</u>	<u>402.6</u>	14 %
Transfers, net	<u>(3.3)</u>	<u>(1.0)</u>	<u>(2.3)</u>	230 %
Expenses:				
School-related	2,814.8	2,596.1	218.7	8 %
State and complex area administration	74.3	66.5	7.8	12 %
Public libraries	51.9	50.4	1.5	3 %
Capital outlay	68.4	104.8	(36.4)	(35) %
Total expenses	<u>3,009.4</u>	<u>2,817.8</u>	<u>191.6</u>	7 %
Change in net position	<u>\$ 305.3</u>	<u>\$ 96.6</u>	<u>\$ 208.7</u>	216 %

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Management's Discussion and Analysis

June 30, 2018

Overall Results of Operations - The Department's results of operations for FY 2018 have resulted in an increase in net position of \$305 million. This is higher than the increase in net position of \$97 million for the prior FY 2017. Total FY 2018 expenses were \$3.009 billion, an increase of 7% or \$192 million from \$2.818 billion in FY 2017.

GOVERNMENTAL FUND FINANCIAL ANALYSIS

Within the governmental fund financial statements, the overall net change in fund balance for FY 2018 was \$188 million, and the total overall fund balance for the governmental funds as of June 30, 2018 was \$1.060 billion.

General Fund Budget Results - The Department was appropriated general funds of \$1.732 billion in FY 2018. Increases of "Final" compared to "Original" budgeted amounts as reported on the Statement of Revenues and Expenditures - Budget and Actual (Non-GAAP Budgetary Basis) - General Fund are primarily due to legislative appropriations due to collective bargaining compensation changes.

For the General Fund, the Department is allowed to carry over up to 5% of any appropriation at the end of the fiscal year. Carryover funds enable schools to make long-range fiscal plans, save for major purchases for which single-year funding may not be sufficient, and provide funds to start the next school year. Under the DOE's single-school calendar, schools start their school year in July statewide, within weeks of the beginning of the fiscal year. For the fiscal year ended June 30, 2018, general funds carried over totaled \$48 million, representing 2.79% of general fund appropriations.

Federal Fund Budget Results - The Department expended \$32 million less federal funds than was appropriated during FY 2018; this merely reflects the timing of expenditures versus federal cash that may have been received during the fiscal year.

AGENCY FUNDS

Agency funds, or "student activity funds," are held for students in a custodial capacity and do not require deposit into the State Treasury. The funds contain monies collected and maintained by schools for students. Examples include yearbook, newspaper fund, student government dues, physical education uniform sales, and excursions. The funds are used for school activities that take place outside formal class periods and are not required for class work or credit. Agency funds due to the students and others was \$29 million in FY 2018 representing a 6% increase from the prior fiscal year balance of \$27 million.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Management's Discussion and Analysis

June 30, 2018

CAPITAL ASSETS

The Department's capital improvement program strives to provide and maintain facilities that are well-placed, sufficient in number, flexible, functional, and creatively designed to accommodate population changes, support educational programs, and promote health and safety of students, employees, and the public.

The Department's capital assets as of June 30, 2018 amounted to \$1.786 billion (net of accumulated depreciation of \$1.896 billion), an increase of \$154 million, compared to capital assets as of June 30, 2017 which amounted to \$1.631 billion (net of accumulated depreciation of \$1.778 billion). Depreciation expense for FY 2018 amounted to \$129 million.

The Department is committed under contracts awarded and orders placed for construction, repairs and maintenance, and related expenses. These commitments amounted to approximately \$866 million.

Additional information on the Department's capital assets and construction contract commitments can be found in Note 5 and Note 12 to the financial statements.

DEBT ADMINISTRATION

In July 2017, the Department entered into an interest-free term loan agreement with the State's Hawaii Green Infrastructure Authority (HGIA). The total loan amount allowed to be drawdown was finalized as of June 30, 2018 at \$46 million. The final loan maturity date is June 30, 2037. The loan is unsecured and requires semi-annual payments starting December 31, 2018 and each June 30, and December 31 thereafter to and including the final maturity date. The principal outstanding at June 30, 2018 is \$6 million.

Additional information on the Department's long-term debt can be found in Note 6 to the financial statements.

REQUESTS FOR INFORMATION

Questions concerning any of the information provided in this report or request for additional financial information should be addressed to the Office of the Fiscal Services, Department of Education, P.O. Box 2360, Honolulu, Hawaii 96804. General information about the Department can be found at the Department's website, www.hawaiipublicschools.org.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Statement of Net Position

June 30, 2018

	<u>Governmental Activities</u>
Assets:	
Current assets:	
Cash and cash equivalents	\$ 1,311,965,202
Receivables:	
Due from federal government	34,865,301
Accounts receivable	12,047,870
Due from other agencies	3,886,270
Total current assets	<u>1,362,764,643</u>
Capital assets, net of accumulated depreciation	<u>1,785,730,643</u>
Total assets	<u><u>\$ 3,148,495,286</u></u>
 Liabilities and Net Position:	
Liabilities:	
Current liabilities:	
Vouchers and contracts payable	\$ 149,970,070
Accrued wages and employee benefits	147,736,396
Accrued compensated absences	22,933,431
Workers' compensation claims reserve	20,386,196
Due to State of Hawaii general fund	5,000,000
Note payable	2,294,180
Total current liabilities	<u>348,320,273</u>
Accrued compensated absences, less current portion	45,632,194
Workers' compensation claims reserve, less current portion	115,521,777
Note payable, less current portion	3,724,793
Total liabilities	<u><u>513,199,037</u></u>
 Net Position:	
Investment in capital assets	1,785,730,643
Unrestricted	849,565,606
Total net position	<u>2,635,296,249</u>
Total liabilities and net position	<u><u>\$ 3,148,495,286</u></u>

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Statement of Activities

Fiscal Year Ended June 30, 2018

	Program Revenues			Net Revenue (Expenses) and Change in Net Position	
Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	
Governmental Activities:					
School-related	\$ 2,814,759,834	\$ 64,966,079	\$ 279,835,566	\$ -	\$ (2,469,958,189)
State and complex area administration	74,308,436	-	2,914,121	-	(71,394,315)
Public libraries	51,857,484	1,625,510	1,642,408	-	(48,589,566)
Capital outlay	68,435,522	-	-	1,137,198	(67,298,324)
Total governmental activities	\$ 3,009,361,276	\$ 66,591,589	\$ 284,392,095	\$ 1,137,198	(2,657,240,394)
General Revenues:					
State allotted appropriations, net of lapses					2,267,481,712
Nonimposed employee wages and fringe benefits					697,432,877
Unrestricted investment earnings					1,009,466
Total general revenues					2,965,924,055
Transfers:					
Transfers in					176,582
Transfers out					(3,538,108)
Net transfers					(3,361,526)
Change in Net Position					305,322,135
Net Position at June 30, 2017					2,329,974,114
Net Position at June 30, 2018					\$ 2,635,296,249

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Balance Sheet
Governmental Funds

June 30, 2018

	<u>General</u>	<u>Federal</u>	<u>Capital Projects</u>	<u>Other</u>	<u>Total</u>
Assets:					
Cash and cash equivalents	\$ 188,047,219	\$ 135,442,404	\$ 881,357,584	\$ 107,117,995	\$ 1,311,965,202
Receivables:					
Due from federal government	-	34,567,534	-	297,767	34,865,301
Accounts receivable	-	-	-	12,047,870	12,047,870
Due from other agencies	-	-	-	3,886,270	3,886,270
Total assets	<u>\$ 188,047,219</u>	<u>\$ 170,009,938</u>	<u>\$ 881,357,584</u>	<u>\$ 123,349,902</u>	<u>\$ 1,362,764,643</u>
Liabilities and Fund Balances:					
Liabilities:					
Vouchers and contracts payable	\$ 57,884,673	\$ 21,520,132	\$ 64,191,784	\$ 6,373,481	\$ 149,970,070
Accrued wages and employee benefits payable	138,350,412	7,508,549	293,669	1,583,766	147,736,396
Due to State of Hawaii general fund	<u>5,000,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>5,000,000</u>
Total liabilities	<u>201,235,085</u>	<u>29,028,681</u>	<u>64,485,453</u>	<u>7,957,247</u>	<u>302,706,466</u>
Fund Balances (Deficits):					
Committed	-	-	-	115,392,655	115,392,655
Assigned	-	140,981,257	816,872,131	-	957,853,388
Unassigned	<u>(13,187,866)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(13,187,866)</u>
Total fund balances (deficits)	<u>(13,187,866)</u>	<u>140,981,257</u>	<u>816,872,131</u>	<u>115,392,655</u>	<u>1,060,058,177</u>
Total liabilities and fund balances	<u>\$ 188,047,219</u>	<u>\$ 170,009,938</u>	<u>\$ 881,357,584</u>	<u>\$ 123,349,902</u>	<u>\$ 1,362,764,643</u>

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Reconciliation of the Governmental Funds Balance Sheet
to the Statement of Net Position

June 30, 2018

Total Fund Balances - Governmental Funds \$ 1,060,058,177

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

Capital assets used in governmental activities are not
financial resources and, therefore, are not reported
in the governmental funds.

Governmental capital assets	\$ 3,681,541,834	
Less accumulated depreciation	<u>(1,895,811,191)</u>	1,785,730,643

Some liabilities are not due in the current period and
therefore are not reported in the governmental funds.

Those liabilities include:

Accrued compensated absences	(68,565,625)
Workers' compensation claims reserve	(135,907,973)
Note payable	<u>(6,018,973)</u>

Net Position of Governmental Activities \$ 2,635,296,249

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds

Fiscal Year Ended June 30, 2018

	<u>General</u>	<u>Federal</u>	<u>Capital Projects</u>	<u>Other</u>	<u>Total</u>
Revenues:					
State allotments, net	\$ 1,769,172,574	\$ -	\$ 520,683,058	\$ 4,540,950	\$ 2,294,396,582
Nonimposed employee wages and fringe benefits	697,432,877	-	-	-	697,432,877
Intergovernmental revenues	-	270,364,282	-	2,586,925	272,951,207
Other revenues	-	-	(26,914,870)	80,179,140	53,264,270
	<u>2,466,605,451</u>	<u>270,364,282</u>	<u>493,768,188</u>	<u>87,307,015</u>	<u>3,318,044,936</u>
Expenditures:					
School-related	2,370,063,161	236,125,106	-	66,534,975	2,672,723,242
State and complex area administration	70,467,420	1,790,978	-	351,852	72,610,250
Public libraries	48,917,549	1,153,017	-	984,239	51,054,805
Capital outlay	3,154,466	20,403,115	310,336,624	1,822,746	335,716,951
	<u>2,492,602,596</u>	<u>259,472,216</u>	<u>310,336,624</u>	<u>69,693,812</u>	<u>3,132,105,248</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	<u>(25,997,145)</u>	<u>10,892,066</u>	<u>183,431,564</u>	<u>17,613,203</u>	<u>185,939,688</u>
Other Financing Sources (Uses):					
Proceeds from note payable	-	-	6,018,973	-	6,018,973
Transfers in	-	-	-	71,952	71,952
Transfers out	-	(71,952)	(3,466,156)	-	(3,538,108)
Total other financing sources (uses)	<u>-</u>	<u>(71,952)</u>	<u>2,552,817</u>	<u>71,952</u>	<u>2,552,817</u>
Net Change in Fund Balances	<u>(25,997,145)</u>	<u>10,820,114</u>	<u>185,984,381</u>	<u>17,685,155</u>	<u>188,492,505</u>
Fund Balances at July 1, 2017	<u>12,809,279</u>	<u>130,161,143</u>	<u>630,887,750</u>	<u>97,707,500</u>	<u>871,565,672</u>
Fund Balances (Deficits) at June 30, 2018	<u>\$ (13,187,866)</u>	<u>\$ 140,981,257</u>	<u>\$ 816,872,131</u>	<u>\$ 115,392,655</u>	<u>\$ 1,060,058,177</u>

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances
of Governmental Funds to Statement of Activities

Fiscal Year Ended June 30, 2018

Net Change in Fund Balances - Total Governmental Funds \$ 188,492,505

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

Governmental funds report capital outlays as expenditures.
However, in the statement of activities the cost of those
assets are depreciated over their estimated useful lives
as depreciation expense.

Expenditures for capital assets	\$ 284,407,960	
Less current fiscal year depreciation	(128,875,945)	
Loss on disposal of capital assets	<u>(1,273,215)</u>	154,258,800

Change in compensated absences reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds	718,907
--	---------

Change in workers' compensation liability reported in the statement of activities does not require the use of current financial resources and, therefore, is not reported as expenditures in governmental funds	(32,129,104)
--	--------------

Proceeds from note payable provide current financial resources to governmental funds; however, are reported as an increase in liabilities in the statement of net position	<u>(6,018,973)</u>
--	--------------------

Change in Net Position of Governmental Activities \$ 305,322,135

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Statement of Revenues and Expenditures
Budget and Actual (Non-GAAP Budgetary Basis) - General Fund

Fiscal Year Ended June 30, 2018

	<u>Budgeted Amounts</u>		<u>Actual on Budgetary Basis</u>	<u>Variance Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Revenues:				
State allotments	\$ 1,732,394,174	\$ 1,770,554,468	\$ 1,770,307,816	\$ (246,652)
Expenditures:				
School-related	1,647,229,540	1,682,582,396	1,634,766,860	47,815,536
State and complex area administration	49,838,966	52,010,199	51,030,992	979,207
Public libraries	<u>35,325,668</u>	<u>35,961,873</u>	<u>35,896,761</u>	<u>65,112</u>
	<u>1,732,394,174</u>	<u>1,770,554,468</u>	<u>1,721,694,613</u>	<u>48,859,855</u>
 Excess of revenues over expenditures	 <u>\$ -</u>	 <u>\$ -</u>	 <u>\$ 48,613,203</u>	 <u>\$ 48,613,203</u>

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Statement of Revenues and Expenditures
Budget and Actual (Non-GAAP Budgetary Basis) - Federal Fund

Fiscal Year Ended June 30, 2018

	<u>Budgeted Amounts</u>		<u>Actual on Budgetary Basis</u>	<u>Variance Postive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Revenues:				
Federal grants	\$ 459,286,421	\$ 439,336,001	\$ 254,600,380	\$ (184,735,621)
Expenditures:				
School-related	453,536,662	432,948,381	220,319,626	212,628,755
State and complex area administration	4,201,456	6,085,695	1,826,537	4,259,158
Public libraries	1,548,303	301,925	195,245	106,680
	<u>459,286,421</u>	<u>439,336,001</u>	<u>222,341,408</u>	<u>216,994,593</u>
Excess of revenues over expenditures	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 32,258,972</u>	<u>\$ 32,258,972</u>

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Statement of Fiduciary Net Position
Agency Funds

June 30, 2018

Assets:	
Cash and cash deposits in financial institutions	\$ 28,747,690
Total assets	<u>28,747,690</u>
Liabilities:	
Due to student groups and others	<u>28,747,690</u>
Total liabilities	<u>28,747,690</u>
Net Position	<u><u>\$ -</u></u>

See accompanying notes to financial statements.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

(1) FINANCIAL REPORTING ENTITY

Introduction - The Department of Education, State of Hawaii (the Department) administers the statewide system of public schools and public libraries. Additionally, the Department is responsible for administering state laws regarding regulation of private school operations through a program of inspection and licensing and the professional certification of all teachers for every academic and noncollege type of school. Federal grants received to support public school and public library programs are administered by the Department on a statewide basis.

These financial statements represent the combination of the Department of Education (the DOE), the Hawaii State Public Library System (the HSPLS), and the Public Charter Schools (the PCS) where the DOE prepares entries, based on information provided by the HSPLS and PCS, to combine financial data for the three units, in aggregate known as the Department. The fiscal and oversight authority for the DOE, HSPLS and PCS are managed independently. The DOE has determined that the PCS balances are significant, but not material, and relies on certain financial information which have been audited by other auditors and coordinated by the PCS.

The Department is a part of the executive branch of the State of Hawaii (the State). The financial statements of the Department are intended to present the financial position, the changes in financial position, and the budgetary comparison of only that portion of the governmental activities, each major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2018, and the changes in its financial position and budgetary comparison for the fiscal year then ended, in accordance with accounting principles generally accepted in the United States of America (GAAP). The State Comptroller maintains the central accounts for all state funds and publishes the State's Comprehensive Annual Financial Report (CAFR), which includes the Department's financial activities.

Reporting Entity - The Department has considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the Department are such that exclusion would cause the Department's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board (GASB) has set forth criteria to be considered in determining financial accountability. The Department has determined, based on the GASB criteria, that it has no component units.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

(2) SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements of the Department have been prepared in accordance with GAAP as prescribed by the GASB.

Government-Wide and Fund Financial Statements - The government-wide financial statements report all assets, liabilities, and activities of the Department as a whole.

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

Net position is restricted when constraints placed on it are either externally imposed or imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net position. When both restricted and unrestricted resources are available for use, generally it is the Department's policy to use restricted resources first, then unrestricted resources as they are needed.

Separate financial statements are provided for governmental funds and fiduciary funds. The fiduciary funds, however, are excluded from the government-wide financial statements because the Department cannot use those assets to finance its operations. Major individual governmental funds are reported as separate columns in the fund financial statements. Nonmajor funds are summarized into a single column.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

Government-Wide Financial Statements

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

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Governmental Fund Financial Statements

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Department considers revenues to be available if they are collected within 60 days of the end of the current fiscal year.

Principal revenue sources considered susceptible to accrual include federal grants. Some revenue items that are considered measurable and available to finance operations during the year from an accounting perspective are not available for expenditure due to the State's present appropriation system. These revenues have been accrued in accordance with GAAP since they have been earned and are expected to be collected within 60 days of the end of the period. Other revenues are considered to be measurable and available only when cash is received by the Department.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include employees' vested vacation and workers' compensation claims, which are recorded as expenditures when utilized or paid. The amount of accumulated vacation and workers' compensation claims reserve at June 30, 2018, has been reported only in the government-wide financial statements.

Encumbrances are recorded obligations in the form of purchase or contracts. The State records encumbrances at the time purchase orders or contracts are awarded and executed. Encumbrances outstanding at fiscal year-end do not constitute expenditures or liabilities.

Fiduciary Funds

The financial statement of fiduciary funds is reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above. Agency funds do not have a measurement focus and report only assets and liabilities.

Fund Accounting

The financial transactions of the Department are recorded in individual funds that are reported in the fund financial statements and are described in the following sections. Each fund is considered a separate accounting entity. The operations of each are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund balances, revenues, and expenditures. Fund accounting is designed to demonstrate the legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

The fund financial statements focus on major funds rather than reporting funds by type. Each major fund is reported in separate columns and nonmajor funds are combined in one column. Major funds are funds that have total assets, liabilities, revenues, or expenditures of the fund that are at least 10% of the same element for all funds of its fund type or at least 5% of the same element for all governmental funds combined.

Governmental Funds

General Fund - The general fund is the main operating fund of the Department. The annual operating budget as authorized by the State Legislature provides the basic framework within which the resources and obligations of the general fund are accounted for.

Federal Fund - The federal fund is used to account for federally funded programs for the Department's major activities. This fund is made up entirely by special revenue funds, which account for the proceeds of specific revenue sources that are for specified purposes. In this case, the expenditures are for activities authorized by the federal agency grantor.

Capital Projects Fund - The capital projects fund includes all amounts related to the Department's capital improvement program. It is used to account for financial resources used for the acquisition or construction of major capital facilities.

Other Funds - The other funds is used to account for all financial activities not required to be accounted for in another fund. It includes special revenue and trust funds, which account for the proceeds of specific revenue sources that are legally restricted to expenditures for specified purposes.

Fund Balance

In the fund financial statements, Governmental Funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

The Department classifies fund balances based primarily on the extent to which a government is bound to follow constraints on how resources can be spent in accordance with GASB Statement No. 54 (GASB 54), *Fund Balance Reporting and Governmental Fund Type Definitions*. Classifications include:

Restricted - Balances that are restricted for specific purposes by external parties such as creditors, grantors, or other governments.

Committed - Balances that can only be used for specific purposes pursuant to constraints imposed by formal action of the State Legislature.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Assigned - Balances that are constrained by management to be used for specific purposes, but are neither restricted nor committed.

Unassigned - Residual balances that are not contained in the other classifications.

When both restricted and unrestricted resources are available for use, generally it is the Department's policy to use restricted resources first, then unrestricted resources as they are needed. When committed, assigned and unassigned resources are available for use, generally it is the Department's policy that committed amounts be reduced first, followed by assigned amounts, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of these unrestricted fund balance classifications could be used.

Fiduciary Funds

Agency Fund - The agency funds are used to account for assets held by the Department on behalf of outside parties, or on behalf of individuals. Agency funds are custodial in nature (i.e., assets equal liabilities) and do not involve measurement of results of operations.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash in banks and amounts held in the State Treasury as discussed in Note 4. The State's investments held in the State Treasury are reported at fair value within the fair value hierarchy established by GAAP.

Capital Assets

Capital assets include land, improvements to land, buildings, building improvements, vehicles, machinery, equipment, and all other tangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period.

When capital assets are purchased, they are capitalized and depreciated in the government-wide financial statements. Capital assets are recorded as expenditures of the current period in the governmental fund financial statements.

Capital assets are valued at cost where historical records are available and at estimated historical cost where no records exist. Donated capital assets are valued at their estimated fair value on the date received.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Improvements to capital assets that materially add to the value or extend the life of the assets are capitalized. Other repairs and normal maintenance are not capitalized.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Depreciation expense is recorded in the government-wide financial statements. The Department utilizes the straight-line method over the assets' estimated useful life. No depreciation is recorded for land. The Department has adopted the following capitalization policy:

<u>Asset Type</u>	<u>Minimum Capitalization Amount</u>	<u>Estimated Useful Life</u>
Land	All	Not applicable
Land improvements	\$ 100,000	15 years
Buildings and improvements	100,000	30 years
Furniture and equipment	5,000	7 years
Vehicles	5,000	5 years
Public library materials	All	5 years

Accumulated Vacation

Employees are credited with vacation at the rate of 96 to 168 hours per calendar year. Accumulation of such vacation credits is limited to 720 hours 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.

Program Revenues

Program revenues are derived directly from the programs of the Department or from parties outside of the Department and are categorized as charges for services, operating grants and contributions, or capital grants and contributions.

Charges for services - Charges for services include revenues based on exchange or exchange-like transactions. These revenues arise from charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided. Revenues in this category include fees charged for meals served, educational classes, use of facilities, transportation services, and use of library materials.

Operating and capital grants and contributions - Program-specific operating and capital grants and contributions include revenues arising from mandatory and voluntary nonexchange transactions with other governments, organizations, or individuals that are restricted for use in a particular program. Governmental grants and assistance awards made on the basis of entitlement periods are recorded as intergovernmental receivables and revenues when entitlement occurs. All other federal reimbursement-type grants are recorded as intergovernmental receivables and revenues when the related expenditures or expenses are incurred.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Intrafund and Interfund Transactions

Significant transfers of financial resources between activities included within the same fund are offset within that fund. Transfers of revenues from funds authorized to receive them to funds authorized to expend them have been recorded as operating transfers in the basic financial statements.

Risk Management

The Department is exposed to various risks for losses related to torts; theft of, damage to, or destruction of assets; errors or omissions; workers compensation; and acts of terrorism. A liability for a claim for a risk of loss is established if information indicates that it is probable that a liability has been incurred as of the date of the financial statements and the amount of the loss is reasonably estimable.

Use of Estimates

The preparation of the financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

Change in Accounting Principle

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

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

The adoption of Statement No. 75 had no significant effect on the Department's financial statements as it is the State's policy to allocate a portion of the OPEB liability, OPEB expense, and deferred outflows of resources and deferred inflows of resources related to OPEB only to component units and proprietary funds that are reported separately in stand-alone financial statements or in the State's CAFR.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Recently Issued Accounting Pronouncements

GASB Statement No. 83

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

GASB Statement No. 87

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

(3) BUDGETING AND BUDGETARY CONTROL

Revenue estimates are provided to the State Legislature at the time of budget consideration, and revised and updated periodically during the fiscal year. Amounts reflected as budgeted revenues and budgeted expenditures in the budgetary comparison schedules of the general and federal funds are derived primarily from acts of the State Legislature and from other authorizations contained in other specific appropriation acts in various Session Laws of Hawaii. To the extent not expended or encumbered, general fund appropriations generally lapse at the end of the fiscal year for which the appropriations were made. The State Legislature specifies the lapse date and any other particular conditions relating to terminating the authorization for other appropriations such as those related to the federal funds.

However, Section 37-41.5 of the Hawaii Revised Statutes allows the Department to carryover up to 5% each of any appropriation at the end of the fiscal year except for appropriations to fund certain financing agreements. These carryover funds, to the extent not expended or encumbered, lapse at June 30 of the first fiscal year of the next fiscal biennium. As of June 30, 2018, general funds carried over amounted to approximately \$48,250,000, representing approximately 2.8% of appropriations.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

For purposes of budgeting, the Department’s budgetary fund structure and accounting principles differ from those utilized to present the fund financial statements in accordance with GAAP. The Department’s annual budget is prepared on the modified accrual basis of accounting with several differences, principally related to (1) the encumbrances of purchase orders and contract obligations, (2) recognition of certain receivables, and (3) special revenue funds operating grants accruals and deferrals. These differences represent a departure from GAAP.

The following schedule reconciles the budgetary amounts to the amounts presented in accordance with GAAP for the fiscal year ended June 30, 2018:

	General	Federal
Excess of revenues over expenditures - actual on a budgetary basis	\$ 48,613,203	\$ 32,258,972
Reserved for encumbrances at fiscal year-end	100,474,367	22,334,175
Expenditures for liquidation of prior fiscal year encumbrances	(169,163,341)	(38,904,927)
Net accrued revenues and expenditures	(5,921,374)	(4,796,154)
Excess (deficiency) of revenues over (under) expenditures - GAAP basis	\$ (25,997,145)	\$ 10,892,066

(4) CASH AND CASH EQUIVALENTS

Cash and cash equivalents at June 30, 2018, consisted of cash in banks and amounts held in the State Treasury at June 30, 2018:

Cash in banks	\$ 63,069,496
Amounts held in the State Treasury	1,248,895,706
	\$ 1,311,965,202

Amounts Held in the State Treasury

The Director of Finance is responsible for the safekeeping of all monies paid into the State Treasury. The Director of Finance pools and invests any monies of the State, which in the Director of Finance’s judgment, are in excess of the amounts necessary for meeting the specific requirements of the State. Investment earnings are allocated to the pool participants based upon their equity interest in the pooled monies. Legally authorized investments include obligations of or

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

guaranteed by the U.S. government, obligations of the State, federally-insured savings and checking accounts, time certificates of deposit, and repurchase agreements with federally-insured financial institutions.

At June 30, 2018, amounts held in the State Treasury by the Department totaled \$1,248,895,706. The amounts held in the State Treasury reported in the accompanying financial statements reflects the Department's relative position in the State's investment pool based upon the average monthly investment balance of each participant in the investment pool.

Information relating to the cash and investments in the State Treasury is determined on a statewide basis and not for individual departments or agencies. Information regarding the carrying amount and corresponding bank balances of the investment pool, investment fair values and maturities by type of security, and the collateralization of the investment pool balances is included in the State's CAFR.

Interest Rate Risk

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

Credit Risk

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

Custodial Risk

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

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Concentration of Credit Risk

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

Foreign Currency Risk

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

Cash in Banks

The DOE maintains cash in banks which is held separately from cash in the State Treasury. As of June 30, 2018, the carrying amount of total bank deposits was \$7,007,180 and the corresponding bank balances were approximately \$38,580,000. The PCS also held cash outside of the State Treasury totaling \$56,062,316 at June 30, 2018.

All deposits are collateralized in accordance with State statutes. The balances are insured by the Federal Deposit Insurance Corporation (FDIC) and collateralized with securities held by the Department's agent. All securities pledged as collateral are held either by the State Treasury or by the State's fiscal agents in the name of the State.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

(5) CAPITAL ASSETS

For the fiscal year ended June 30, 2018, capital assets activity for the Department was as follows:

	<u>Balance July 1, 2017</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance June 30, 2018</u>
Governmental activities:				
Capital assets not being depreciated:				
Land	\$ 88,238,609	\$ -	\$ -	\$ 88,238,609
Construction in progress	194,228,450	268,554,645	(171,612,085)	291,171,010
Total capital assets not being depreciated	<u>282,467,059</u>	<u>268,554,645</u>	<u>(171,612,085)</u>	<u>379,409,619</u>
Capital assets being depreciated:				
Land improvements	304,255,996	33,423,058	-	337,679,054
Buildings and improvements	2,420,649,423	73,373,790	(447,424)	2,493,575,789
Furniture and equipment	325,192,884	75,525,885	(7,572,245)	393,146,524
Vehicles	11,861,582	723,322	(238,613)	12,346,291
Public library materials	65,196,168	4,377,238	(4,188,849)	65,384,557
Total capital assets being depreciated	<u>3,127,156,053</u>	<u>187,423,293</u>	<u>(12,447,131)</u>	<u>3,302,132,215</u>
Less accumulated depreciation for:				
Land improvements	(162,092,452)	(16,784,903)	-	(178,877,355)
Buildings and improvements	(1,359,390,752)	(66,324,334)	111,856	(1,425,603,230)
Furniture and equipment	(191,435,368)	(41,102,508)	6,676,705	(225,861,171)
Vehicles	(10,662,566)	(529,330)	238,613	(10,953,283)
Public library materials	(54,570,131)	(4,134,870)	4,188,849	(54,516,152)
Total accumulated depreciation	<u>(1,778,151,269)</u>	<u>(128,875,945)</u>	<u>11,216,023</u>	<u>(1,895,811,191)</u>
Governmental activities, net	<u>\$ 1,631,471,843</u>	<u>\$ 327,101,993</u>	<u>\$ (172,843,193)</u>	<u>\$ 1,785,730,643</u>

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Depreciation expense was charged to functions as follows:

	Governmental Activities
School-related	\$ 119,749,091
State and complex area administration	1,716,417
Public libraries	7,410,437
Total additions to accumulated depreciation	\$ 128,875,945

(6) LONG-TERM LIABILITIES

The change in long-term liabilities during the fiscal year ended June 30, 2018, was as follows:

	Accrued Compensated Absences	Workers' Compensation Claims	Note Payable
Balance at July 1, 2017	\$ 69,284,532	\$ 103,778,869	\$ -
Additions	29,813,863	45,867,544	6,018,973
Reductions	(30,532,770)	(13,738,440)	-
Balance at June 30, 2018	68,565,625	135,907,973	6,018,973
Less current portion	(22,933,431)	(20,386,196)	(2,294,180)
	\$ 45,632,194	\$ 115,521,777	\$ 3,724,793

The compensated absences and workers' compensation liabilities have been paid primarily by the general fund in the past. The carrying amount of liabilities for unpaid workers' compensation claims of approximately \$145.7 million is reported at present value using a discount rate of 2%.

In July 2017, the Department entered into an interest-free term loan agreement with the State's Hawaii Green Infrastructure Authority (HGIA). The total loan amount allowed to be drawdown was finalized as of June 30, 2018 at \$45,883,600. The final loan maturity date is June 30, 2037. The loan is unsecured and requires semi-annual payments of \$1,147,090 starting December 31, 2018 and each June 30, and December 31 thereafter to and including the final maturity date. The principal outstanding at June 30, 2018 is \$6,018,973.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Principal maturities of the note payable are as follows:

Fiscal Year Ending June 30:	
2019	\$ 2,294,180
2020	2,294,180
2021	<u>1,430,613</u>
	<u>\$ 6,018,973</u>

(7) FOOD DISTRIBUTION PROGRAM

The U.S. Department of Agriculture (USDA), Food and Nutrition Service (FNS), has delegated to the Hawaii Child Nutrition Programs office (HCNP) the administrative responsibility of the Food Distribution Program. HCNP is the State Agency that distributes USDA Foods to schools (public, private, and charter), institutions and organizations that participate in the National School Lunch Program (NSLP) and Summer Food Service Program (SFSP). Hawaii's entitlement is determined in part by the number of lunches reimbursed under the NSLP and SFSP of the previous school year. FNS estimates the cost to purchase the USDA Foods. The amount charged to the entitlement is based upon the net dollar values of the purchased USDA Foods. Bonus commodities are USDA Foods that are additional to Hawaii's entitlement. A portion of the entitlement is allocated for the purchase of fresh produce.

The Department received approximately \$5,308,000 of commodities for the fiscal year ended June 30, 2018. No bonus commodities were received for the fiscal year ended June 30, 2018.

(8) NONIMPOSED EMPLOYEE WAGES AND FRINGE BENEFITS

Payroll fringe benefit costs that are funded by state appropriations are assumed by the State and are not charged to the Department's operating funds. These costs, totaling approximately \$697,433,000 for the fiscal year ended June 30, 2018, have been reported as revenues and expenditures in the general fund of the Department.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

(9) LEASE COMMITMENTS

The Department leases equipment from third-party lessors under various operating leases expiring through 2028. Future minimum lease rentals under noncancelable operating leases with terms of one year or more at June 30, 2018 were as follows:

Fiscal Year Ending June 30:	
2019	\$ 4,523,000
2020	3,591,000
2021	2,704,000
2022	1,650,000
2023	586,000
2024-2028	<u>23,000</u>
	<u><u>\$ 13,077,000</u></u>

Total rent expense related to the above leases for the fiscal year ended June 30, 2018 amounted to approximately \$4,442,000.

(10) RETIREMENT BENEFITS

Pension Plan

Plan Description

Generally, all full-time employees of the State and counties, which includes the Department, are required to be members of the Employees' Retirement System of the State of Hawaii (the ERS), a cost-sharing multiple-employer defined benefit pension plan that administers the State's pension benefits program. Benefits, eligibility, and contribution requirements are governed by HRS Chapter 88 and can be amended through legislation.

Benefits Provided

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

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

and the average of the highest salaries during any five years of credited service including any salary paid in lieu of vacation for members hired prior to January 1, 1971. For members hired after June 30, 2012, average final compensation is an average of the highest salaries during any five years of credited service excluding any salary paid in lieu of vacation.

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

The following summarizes the provisions relevant to the largest employee groups of the respective membership class.

Noncontributory Class

Retirement Benefits

General employees' retirement benefits are determined as 1.25% of average final compensation multiplied by the years of credited service. Employees with ten years of credited service are eligible to retire at age 62. Employees with 30 years of credited service are eligible to retire at age 55.

Disability Benefits

Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 35% of their average final compensation. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined in the same manner as retirement benefits but are payable immediately, without an actuarial reduction, and at a minimum of 12.5% of average final compensation.

Death Benefits

For service-connected deaths, the surviving spouse/reciprocal beneficiary receives a monthly benefit of 30% of the average final compensation until remarriage or re-entry into a new reciprocal beneficiary relationship. Additional benefits are payable to surviving dependent children up to age 18. If there is no spouse/reciprocal beneficiary or dependent children, no benefit is payable.

Ordinary death benefits are available to employees who were active at the time of death with at least ten years of credited service. The surviving spouse/reciprocal beneficiary (until remarriage/reentry into a new reciprocal beneficiary relationship) and dependent children (up to age 18) receive a benefit equal to a percentage of member's accrued maximum allowance unreduced for age or, if the member was eligible for retirement at the time of death, the surviving

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

spouse/reciprocal beneficiary receives 100% joint and survivor lifetime pension and the dependent children receive a percentage of the member's accrued maximum allowance unreduced for age.

Contributory Class for Members Hired Prior to July 1, 2012

Retirement Benefits

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

Disability Benefits

Members are eligible for service-related disability benefits regardless of length of service and receive a one-time payment of the member's contributions and accrued interest plus a lifetime pension of 50% of their average final compensation. Ten years of credited service is required for ordinary disability. Ordinary disability benefits are determined as 1.75% of average final compensation multiplied by the years of credited service but are payable immediately, without an actuarial reduction, and at a minimum of 30% of average final compensation.

Death Benefits

For service-connected deaths, the surviving spouse/reciprocal beneficiary receives a lump sum payment of the member's contributions and accrued interest plus a monthly benefit of 50% of the average final compensation until remarriage or re-entry into a new reciprocal beneficiary relationship. If there is no surviving spouse/reciprocal beneficiary, surviving children (up to age 18) or dependent parents are eligible for the monthly benefit. If there is no spouse/reciprocal beneficiary or dependent children/parents, the ordinary death benefit is payable to the designated beneficiary.

Ordinary death benefits are available to employees who were active at time of death with at least one year of service. Ordinary death benefits consist of a lump sum payment of the member's contributions and accrued interest plus a percentage of the salary earned in the 12 months preceding death, or 50% joint and survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% joint and survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Contributory Class for Members Hired After June 30, 2012

Retirement Benefits

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

Disability and Death Benefits

Members are eligible for service-related disability benefits regardless of length of service and receive a lifetime pension of 50% of their average final compensation plus refund of contributions and accrued interest. Ten years of credited service is required for ordinary disability.

Death benefits for contributory members hired after June 30, 2012 are generally the same as those for contributory members hired June 30, 2012 and prior.

Hybrid Class for Members Hired Prior to July 1, 2012

Retirement Benefits

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

Disability Benefits

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

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Death Benefits

For service-connected deaths, the designated surviving spouse/reciprocal beneficiary receives a lump sum payment of the member's contributions and accrued interest plus a monthly benefit of 50% of the average final compensation until remarriage or re-entry into a new reciprocal beneficiary relationship. If there is no surviving spouse/reciprocal beneficiary, surviving dependent children (up to age 18) or dependent parents are eligible for the monthly benefit. If there is no spouse/reciprocal beneficiary or dependent children/parents, the ordinary death benefit is payable to the designated beneficiary.

Ordinary death benefits are available to employees who were active at time of death with at least five years of service. Ordinary death benefits consist of a lump sum payment of the member's contributions and accrued interest plus a percentage multiplied by 150%, or 50% joint and survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% joint and survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary.

Hybrid Class for Members Hired After June 30, 2012

Retirement Benefits

General employees' retirement benefits are determined as 1.75% of average final compensation multiplied by the years of credited service. General employees with ten years of credited service are eligible to retire at age 65. Employees with 30 years of credited service are eligible to retire at age 60. Sewer workers, water safety officers, and emergency medical technicians may retire with 25 years of credited service at age 55.

Disability and Death Benefits

Provisions for disability and death benefits generally remain the same except for ordinary death benefits. Ordinary death benefits are available to employees who were active at time of death with at least ten years of service. Ordinary death benefits consist of a lump sum payment of the member's contributions and accrued interest, or 50% joint and survivor lifetime pension if the member was not eligible for retirement at the time of death but was credited with at least ten years of service and designated one beneficiary, or 100% joint and survivor lifetime pension if the member was eligible for retirement at the time of death and designated one beneficiary.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Contributions

Contributions are established by HRS Chapter 88 and may be amended through legislation. The employer rate is set by statute based on the recommendations of the ERS actuary resulting from an experience study conducted every five years. Since July 1, 2005, the employer contribution rate is a fixed percentage of compensation, including the normal cost plus amounts required to pay for the unfunded actuarial accrued liabilities. The contribution rates for fiscal year 2018 was 18.0% for general employees. Contributions to the pension plan from the Department were approximately \$259,670,000 for the fiscal year ended June 30, 2018.

On May 18, 2017, the Governor signed into law Act 17 SLH 2017. Per Act 17, future employer contributions from the State and counties are expected to increase pursuant to a phased-in contribution rate increase beginning July 1, 2017. The rate for general employees increases to 19.0% on July 1, 2018; 22.0% on July 1, 2019; and 24.0% on July 1, 2020.

The employer is required to make all contributions for noncontributory members. Contributory members hired prior to July 1, 2012 are required to contribute 7.8% of their salary. Contributory members hired after June 30, 2012 are required to contribute 9.8% of their salary. Hybrid members hired prior to July 1, 2012 are required to contribute 6.0% of their salary. Hybrid members hired after June 30, 2012 are required to contribute 8.0% of their salary.

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

Measurement of the actuarial valuation of the pension liability, pension expense, and deferred outflows of resources and deferred inflows of resources related to pension is made for the State as a whole and is not separately computed for the individual state departments and agencies such as the Agency. The State allocates the pension liability, pension expense, and deferred outflows of resources and deferred inflows of resources related to pension only to component units and proprietary funds that are reported separately in stand-alone financial statements or in the State's CAFR. Accordingly, the Department's proportionate share of the State's pension liability, pension expense, and deferred outflows of resources and deferred inflows of resources related to pension is not reported in the accompanying financial statements.

Additional disclosures and required supplementary information pertaining to the State's net pension liability, pension expense, and deferred outflows of resources and deferred inflows of resources related to pension can be found in the State's CAFR. The State's CAFR can be obtained at the Department of Accounting and General Services' website: <http://hawaii.gov/dags/rpts>.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

Postemployment Health Care and Life Insurance Benefits

Plan Description

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

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

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

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

Contributions

Contributions are governed by HRS Chapter 87A and may be amended through legislation. Contributions to the EUTF paid by the Department was approximately \$130,182,000 for the fiscal year ended June 30, 2018.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

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

Measurement of the actuarial valuation of the OPEB liability, OPEB expense, and deferred outflows of resources and deferred inflows of resources related to OPEB is made for the State as a whole and is not separately computed for the individual state departments and agencies such as the Department. The State allocates the OPEB liability, OPEB expense, and deferred outflows of resources and deferred inflows of resources related to OPEB only to component units and proprietary funds that are reported separately in stand-alone financial statements or in the State's CAFR. Accordingly, the Department's proportionate share of the State's OPEB liability, OPEB expense, and deferred outflows of resources and deferred inflows of resources related to OPEB are not reported in the accompanying financial statements.

Additional disclosures and required supplementary information stipulated by Statement No. 75 pertaining to the State's net OPEB liability, OPEB expense, and deferred outflows of resources and deferred inflows of resources related to OPEB can be found in the State's CAFR.

Deferred Compensation Plan

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

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

(11) RISK MANAGEMENT

The State is exposed to various risks of loss related to, among other risks, torts; theft of, damage to, or destruction of assets; errors or omissions; and workers' compensation. The State purchases policies to provide coverage for all state entities, including the Department. The State generally retains the first \$1,000,000 per occurrence of property losses, the first \$4,000,000 with respect to general liability claims, and the first \$500,000 of losses due to crime and cyber liability. Losses in excess of those retention amounts are insured with commercial insurance carriers. The limit per occurrence of property losses is \$200,000,000 except for terrorism, which is \$50,000,000 per occurrence. The annual aggregate limit for general liability losses is \$5,000,000 per occurrence and for crime losses, the limit per occurrence is \$10,000,000 with no aggregate limit. The State also has an insurance policy to cover medical malpractice risk in the amount of \$35,000,000 per occurrence and \$39,000,000 in the aggregate.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to Financial Statements

June 30, 2018

The State is generally self-insured for workers' compensation and automobile claims. The Department administers its workers' compensation losses. A liability for workers' compensation is established if information indicates that a loss has been incurred as of June 30, 2018, and the amount of the loss can be reasonably estimated. The liability also includes an estimate for amounts incurred but not reported and loss adjustment expenses. The amount of the estimated loss is recorded in the accompanying statement of net position, as those losses will be liquidated with future expendable resources.

(12) COMMITMENTS AND CONTINGENCIES

Encumbrances - The Department is committed under contracts awarded and orders placed for construction, repairs and maintenance, expenses, supplies, etc. These commitments as of June 30, 2018 were as follows:

General Fund	\$ 107,945,839
Federal Fund	70,998,094
Capital Projects Fund	676,518,961
Other Fund	<u>10,554,675</u>
	<u>\$ 866,017,569</u>

Litigation - The Department has been named as defendant in a number of lawsuits and claims arising in the normal course of operations. A number of claims may possibly result in adverse judgments against the Department. However, such claim amounts cannot be reasonably estimated at this time. Although the Department and its counsel are unable to express opinions as to the outcome of on-going litigation, it is their opinion that any potential liability arising therefrom will not have a material adverse effect on the financial position of the Department because any judgments against the Department are judgments against the State and would be funded by the legislative appropriation of the State General Fund.

(13) SUBSEQUENT EVENTS

The Department has evaluated subsequent events through March 25, 2019, the date the financial statements were available to be issued, and determined that there are no other matters to disclose.

SUPPLEMENTARY INFORMATION

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Expenditures of Federal Awards

Fiscal Year Ended June 30, 2018

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number ¹	Pass-through Entity Identifying Number	Provided to Subrecipients	Total Federal Expenditures
U.S. Department of Agriculture				
Child Nutrition Cluster:				
School Breakfast Program	10.553		\$ 404,068	\$ 10,783,558
National School Lunch Program:	10.555			
Cash assistance			1,485,074	43,721,240
Cash assistance (commodities)			-	5,307,721
Subtotal - National School Lunch Program			1,485,074	49,028,961
Summer Food Service Program for Children:	10.559			
Cash assistance			642,516	642,516
State administrative expense			-	20,698
Subtotal - Summer Food Service Program for Children			642,516	663,214
Total - Child Nutrition Cluster			2,531,658	60,475,733
Child and Adult Care Food Program	10.558		7,153,342	7,321,409
State Administrative Expense for Child Nutrition	10.560		-	1,378,970
Child Nutrition Discretionary Grants Limited Availability	10.579		94,450	98,242
Fresh Fruit and Vegetable Program	10.582		94,143	1,662,300
Total - U.S. Department of Agriculture			9,873,593	70,936,654
U.S. Department of Commerce				
Office for Coastal Management	11.473		-	32,864
Total - U.S. Department of Commerce			-	32,864
U.S. Department of Defense				
Competitive Grants: Promoting K-12 Student Achievement at Military-Connected Schools:	12.556			
Comprehensive Stem			-	540,591
Readying Radford Complex			-	293,427
Visible Learning			-	193,761
Stem Leilehua Complex			-	183,718
MCASP Kailua Inter FY18			-	17,577
Total - Competitive Grants Promoting K-12 Student Achievement at Military-Connected Schools			-	1,229,074
Invitational Grants for Military-Connected Schools	12.557		-	214,332
Department of Defense Impact Aid	12.558		-	2,799,168
Community Investment	12.600		-	20,403,115
Total - U.S. Department of Defense			-	24,645,689
Institute of Museum and Library Services				
Grants to States	45.310		-	1,153,017
Total - Institute of Museum and Library Services			-	1,153,017

¹ Other identifying number used if no CFDA number available.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Expenditures of Federal Awards (Continued)

Fiscal Year Ended June 30, 2018

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number ¹	Pass-through Entity Identifying Number	Provided to Subrecipients	Total Federal Expenditures
U.S. Department of Education				
Adult Education - Basic Grants to States	84.002		\$ -	\$ 1,970,036
Title I - Grants to Local Educational Agencies	84.010		-	47,865,942
Migrant Education - State Grant Program	84.011		-	912,381
Title I - State Agency Program for Neglected and Delinquent Children and Youth	84.013		-	181,433
Special Education Cluster:				
Grants to States	84.027		-	42,089,443
Preschool Grants	84.173		-	853,452
Total - Special Education Cluster			-	42,942,895
Impact Aid	84.041		-	17,922,264
Migrant Education Coordination Program	84.144		-	124,790
School Safety National Activities	84.184		-	630,543
Education for Homeless Children and Youth	84.196		-	28,701
Twenty-First Century Community Learning Centers	84.287		1,573,160	7,237,368
English Language Acquisition State Grants	84.365		-	4,334,064
Mathematics and Science Partnerships	84.366		-	485,933
Supporting Effective Instruction State Grant	84.367		-	10,874,395
Grants for State Assessments and Related Activities	84.369		-	5,264,457
Statewide Longitudinal Data Systems	84.372		-	1,502,014
School Improvement Grants	84.377		-	2,632,403
Preschool Development Grants	84.419		-	749,207
Student Support and Academic Enrichment Program	84.424		-	1,940,000
Common Core of Data Survey Project	84.ED-08-CO-0029		-	12,001
NAEP State Coordinator	84.ED-08-CO-0029		-	28,155
Passed-through State Department of Human Services:				
Rehabilitation Services - Vocational Rehabilitation Grants to States	84.126	H126A150015-160015	-	82,590
Passed-through Alu Like, Inc.:				
Native Hawaiian Career and Technical Education	84.259	VE-CAS1314-01	-	262,606
Passed-through Office of the State Director for Career and Technical Education:				
Career and Technical Education - Basic Grants to States	84.048	V048A14-V048A17	-	2,650,773
Passed-through University of Hawaii:				
Gaining Early Awareness and Readiness for Undergraduate Programs	84.334	P334S110026	-	424,321
Gaining Early Awareness and Readiness for Undergraduate Programs	84.334A	P334A110247	-	35,637
Native Hawaiian Education	84.362A	S362A14,S362A17	-	240,772
Total - Passed-through University of Hawaii			-	700,730
Total - U.S. Department of Education			1,573,160	151,335,681

¹ Other identifying number used if no CFDA number available.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Expenditures of Federal Awards (Continued)

Fiscal Year Ended June 30, 2018

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number¹	Pass-through Entity Identifying Number	Provided to Subrecipients	Total Federal Expenditures
U.S. Department of Health and Human Services				
Substance Abuse and Mental Health Services-Projects of Regional and National Significance	93.243		\$ -	\$ 1,559,860
Passed-through State Department of Human Services:				
TANF Cluster - Temporary Assistance for Needy Families	93.558	DHS-14-ETPO-1029	-	2,881,181
CCDF Cluster - Child Care and Development Block Grant	93.575	DHS-15-CCPO,17-CCPO	-	131,668
Total - Passed-through State Department of Human Services			-	3,012,849
Head Start	93.600		-	106,368
Cooperative Agreements to Support Comprehensive School Health Programs to Prevent the Spread of HIV and Other Important Health Problems	93.938		-	69,814
Total - U.S. Department of Health and Human Services			-	4,748,891
Total Expenditures of Federal Awards			<u>\$ 11,446,753</u>	<u>\$ 252,852,796</u>

¹ Other identifying number used if no CFDA number available.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Notes to the Schedule of Expenditures of Federal Awards

Fiscal Year Ended June 30, 2018

(1) BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards (the Schedule) for the fiscal year ended June 30, 2018 includes the federal award activity of the Department of Education (the DOE), the Hawaii State Public Library System (the HSPLS), and certain Public Charter Schools (the PCS) where the DOE prepares the Schedule, based on information provided by the HSPLS and the PCS, to combine federal financial data for the three departments, in aggregate known as the Department.

The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the Department, it is not intended to and does not present the financial position, changes in net position, or cash flows of the Department.

The following is a summary of the PCS entities that obtained separate audits performed in accordance with the Uniform Guidance, including separate Uniform Guidance submissions to the Federal Audit Clearinghouse:

- State Public Charter School Commission
- Ka 'Umeke Kā'eo Hawaiian Immersion Public Charter School
- Kamaile Academy
- Ke Kula 'O Nāwahīokalani'ōpu'u Iki LPCS
- Kualapu'u School
- Kua o ka Lā New Century Public Charter School

Awards listed in these separately issued Uniform Guidance submissions, with federal expenditures aggregating to \$7,688,853 for the fiscal year ended June 30, 2018, are not included in the accompanying Schedule.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are reported on the cash basis of accounting. Such expenditures are recognized following as applicable, either the cost principles in the Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribe Governments*, or the cost principles contained in the Uniform Guidance, where in certain types of expenditures are not allowable or are limited as to reimbursement.

(3) INDIRECT COST RATE

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

PART III

**INTERNAL CONTROL OVER FINANCIAL REPORTING
AND COMPLIANCE**

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Auditor
State of Hawaii

Board of Education
Department of Education
State of Hawaii:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund, and aggregate remaining fund information of the Department of Education, State of Hawaii (the Department), as of and for the fiscal year ended June 30, 2018, and the related notes to financial statements, which collectively comprise the Department's basic financial statements, and have issued our report thereon dated March 25, 2019. Our report includes a reference to other auditors who audited the financial statements of certain public charter schools, as described in our report on the Department's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a certain deficiency in material control, described in the accompanying schedule of findings and questioned costs as Finding No. 2018-001, that we consider to be a significant deficiency.

Compliance and Other Matters

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

Department's Response to Finding

The Department's response to the finding identified in our audit is described in Part V, Corrective Action Plan. The Department's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

KKDL Y LLC

Honolulu, Hawaii
March 25, 2019

PART IV

**COMPLIANCE AND INTERNAL CONTROL OVER
FEDERAL AWARDS**

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

The Auditor
State of Hawaii

Board of Education
Department of Education
State of Hawaii:

Report on Compliance for Each Major Federal Program

We have audited the Department of Education, State of Hawaii’s (the Department) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Department’s major federal programs for the fiscal year ended June 30, 2018. The Department’s major federal programs are identified in the summary of auditors’ results section of the accompanying schedule of findings and questioned costs.

The Department’s financial statements include the State Public Charter School Commission, the Ka 'Umeke Kā'eo Hawaiian Immersion Public Charter School, the Kamaile Academy, the Ke Kula 'O Nāwahīokalani'ōpu'u Iki LPCS, the Kualapu'u School, and the Kua o ka Lā New Century Public Charter School. These entities expended \$7,688,853 in federal awards, which are not included in the accompanying schedule of expenditures of federal awards for the fiscal year ended June 30, 2018. Our audit, described below, did not include the operations of the State Public Charter School Commission, the Ka 'Umeke Kā'eo Hawaiian Immersion Public Charter School, the Kamaile Academy, the Ke Kula 'O Nāwahīokalani'ōpu'u Iki LPCS, the Kualapu'u School, and the Kua o ka Lā New Century Public Charter School because these entities separately engaged auditors to perform audits in accordance with Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the Uniform Guidance), including separate Uniform Guidance submissions to the Federal Audit Clearinghouse.

Management’s Responsibility

Management is responsible for compliance with the requirements of federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of the Department's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of the Uniform Guidance.

Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Department's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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

Opinion on Each Major Federal Program

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

Other Matters

The results of our auditing procedures disclosed instances of noncompliance which are required to be reported in accordance with the Uniform Guidance and which are described in the accompanying schedule of findings and questioned costs as Finding Nos. 2018-002 and 2018-003. Our opinion on each major federal program is not modified with respect to these matters.

The Department's responses to the noncompliance findings identified in our audit is described in Part V, Corrective Action Plan. The Department's responses were not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the responses.

Report on Internal Control Over Compliance

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

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a

deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we did identify certain deficiencies in internal control over compliance, described in the accompanying schedule of findings and questioned costs as Finding Nos. 2018-002 and 2018-003, that we consider to be significant deficiencies.

The Department's responses to the internal control over compliance findings identified in our audit is described in Part V, Corrective Action Plan. The Department's responses were not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the responses.

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

KKDL Y LLC

Honolulu, Hawaii
March 25, 2019

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Findings and Questioned Costs

Fiscal Year Ended June 30, 2018

SECTION I – SUMMARY OF AUDITORS’ RESULTS

Financial Statements

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

Unmodified

Internal control over financial reporting:

- Material weakness(es) identified? Yes No
- Significant deficiency(ies) identified? Yes None reported
- Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major federal programs:

- Material weakness(es) identified? Yes No
- Significant deficiency(ies) identified? Yes None reported

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

Unmodified

Any audit findings disclosed that are required to be reported in accordance with 2 CFR Section 200.516(a)?

Yes No

Identification of major federal programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
12.600	U.S. Department of Defense - Community Investment
84.010	U.S. Department of Education - Title I - Grants to Local Educational Agencies
84.377	U.S. Department of Education - School Improvement Grants

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

\$3,000,000

Auditee qualified as low-risk auditee?

Yes No

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Findings and Questioned Costs

Fiscal Year Ended June 30, 2018

SECTION II – FINANCIAL STATEMENT FINDINGS

**Finding No. 2018-001
Accounting for Capital Assets**

Condition

The Office of School Facilities and Support Services (OSFSS) is responsible for planning and directing capital projects, repairs and maintenance, and the related funds released for such projects. The Office of Fiscal Services, Accounting Services Branch (Accounting) relies on information provided by the OSFSS to properly account for capital assets and repairs and maintenance expenses reported in the Department's government-wide financial statements.

During our audit of capital assets, we noted the following conditions:

1. Various jobs consisting of multiple projects using construction management services and a miscellaneous job aggregating to \$8.1 million were incorrectly classified as repairs and maintenance projects instead of capital assets. As a result of these misclassifications, capital assets were understated and repairs and maintenance expenses were overstated by approximately \$8.1 million as of and for the fiscal year ended June 30, 2018. Additionally, related depreciation expense and accumulated depreciation were understated by approximately \$0.1 million.
2. Various adjustments were required to reconcile capital assets and related depreciation expense to the proper balances as of and for the year ended June 30, 2018, including adjustments identified by the Department during its final review process. Capital assets were understated by approximately \$5.6 million and related depreciation expense and accumulated depreciation were understated by approximately \$0.3 million.
3. A number of machinery and equipment purchases were overstated by approximately \$8.2 million due to input errors. As a result of the input errors, accumulated depreciation and depreciation expense were also overstated by approximately \$1.8 million as of and for the fiscal year ended June 30, 2018.

Criteria

Accounting principles generally accepted in the United States of America require that costs incurred to extend the useful life of an asset, to expand the capacity of an asset, or to acquire, including construction of, an asset with a useful life over one year be capitalized. Repairs and maintenance are expensed as incurred and not capitalized.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Findings and Questioned Costs

Fiscal Year Ended June 30, 2018

Cause

The above discrepancies occurred due to the following:

1. The Department classified jobs that comprised multiple contracts or projects at the consolidated job level instead of at the individual contract or project level.
2. Capital assets and related depreciation expense could be reconciled on a more timely basis.
3. Capital asset input errors were not detected in the review process.

Effect

The Department had a net understatement in capital assets and a net overstatement in expenses of approximately \$6.9 million as of and for the fiscal year ended June 30, 2018.

The Department has corrected the discrepancies identified above in the current fiscal year to appropriately present capital assets in the financial statements.

Identification as a Repeat Finding, if applicable

See finding 2017-001 included in the Summary Schedule of Prior Audit Finding.

Recommendation

We recommend that the Department exercise greater care in preparing capital asset reports and schedules for financial reporting purposes. Specifically, the OSFSS should classify jobs with multiple contracts or projects at the individual contract or project level to ensure costs are properly classified as repairs and maintenance or capital assets. In addition, the Department should adjust capital assets and related depreciation to the appropriate balances on a timely basis. Further, additions to capital assets inputted into the Department's capital asset records should be reviewed for accuracy.

Views of Responsible Official(s) and Planned Corrective Action

Management agrees with the findings and recommendations. See Corrective Action Plan on page 61.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Findings and Questioned Costs

Fiscal Year Ended June 30, 2018

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**Finding No. 2018-002
Procurement and Suspension and Debarment**

**Title I Grants to Local Educational Agencies
U.S. Department of Education
CFDA No. 84.010**

Condition

The Department follows the State of Hawaii procurement code and utilizes vendor and price lists approved by the State of Hawaii's Procurement Office (SPO). Department personnel utilizing SPO Vendor List Contract No. 15-05 are responsible for completing Form SPO-010, "Record of Procurement" for purchases that exceed \$5,000 and for obtaining a minimum number of quotes depending on the purchase amount.

In lieu of Form SPO-010, the Department utilizes Form 10-B "Record of Small Purchase" to evidence compliance with the vendor list terms. This form contains the same information as Form SPO-010 and must be attached to the purchase order. Form 10-B contains information supporting the purchase, including (1) the purchase order number; (2) price quotations received, including vendor name, representative, contact information, and the date and amount quoted; (3) the justification for inability to obtain the minimum number of price quotes, if applicable; (4) the justification for awards made other than the lowest price quotation, if applicable; and (5) the signatures and dates of the preparer and the administrator approving the form.

For other small purchases exceeding \$5,000 and not utilizing a vendor or price list, procurement transactions must be supported by a signed and approved Form 10-B and a minimum number of oral and written quotes depending on the purchase amount.

During our testing of procurement, we noted that out of a sample of 40 transactions, 3 transactions were missing the signed and approved Form 10-B and/or did not have documentation evidencing that the required number of quotes were obtained in accordance with the small purchase procurement policies or purchasing thresholds included in SPO Vendor List Contract No. 15-05. Out of the 3 transactions, 2 transactions exceeded \$5,000 and utilized SPO Vendor List Contract No. 15-05. The remaining transaction was a small purchase exceeding \$5,000.

Criteria

In accordance with the 2017 and 2018 Office of Management and Budget (OMB) *Compliance Supplement* and in accordance with 2 CFR § 200.317, "States, and governmental subrecipients of States, will use the same State policies and procedures used for procurements from non-Federal funds."

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Findings and Questioned Costs

Fiscal Year Ended June 30, 2018

In accordance with 2 CFR § 200.303, the non-Federal entity must establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award.

Cause

The Department did not adhere to established policies and procedures for small purchases and the utilization of vendor lists.

Effect

The Department has not complied with applicable small purchase procurement policies and vendor list terms.

Questioned Costs

No questioned or known costs were identified.

Identification as a Repeat Finding, if applicable

Not applicable.

Recommendation

We recommend that the Department strengthen its internal controls and supervisory review over the small purchase procurement process and the utilization of vendor lists such as SPO Vendor List Contract No. 15-05, including the retention of supporting documentation.

Views of Responsible Official(s) and Planned Corrective Action

Management agrees with the findings and recommendations. See Corrective Action Plan on page 63.

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Findings and Questioned Costs

Fiscal Year Ended June 30, 2018

**Finding No. 2018-003
Procurement and Suspension and Debarment**

**School Improvement Grants
U.S. Department of Education
CFDA No. 84.377**

Condition

The Department follows the State of Hawaii procurement code and utilizes vendor and price lists approved by the State of Hawaii's Procurement Office (SPO). Department personnel utilizing SPO Vendor List Contract No. 15-05 are responsible for completing Form SPO-010, "Record of Procurement" for purchases that exceed \$5,000 and for obtaining a minimum number of quotes depending on the purchase amount.

In lieu of Form SPO-010, the Department utilizes Form 10-B "Record of Small Purchase" to evidence compliance with the vendor list terms. This form contains the same information as Form SPO-010 and must be attached to the purchase order. Form 10-B contains information supporting the purchase, including (1) the purchase order number; (2) price quotations received, including vendor name, representative, contact information, and the date and amount quoted; (3) the justification for inability to obtain the minimum number of price quotes, if applicable; (4) the justification for awards made other than the lowest price quotation, if applicable; and (5) the signatures and dates of the preparer and the administrator approving the form.

For other small purchases exceeding \$5,000 and not utilizing a vendor or price list, procurement transactions must be supported by a signed and approved Form 10-B and a minimum number of oral and written quotes depending on the purchase amount.

During our testing of procurement, we noted that out of a sample of 40 transactions, the Department did not have documentation for 5 transactions evidencing that the required number of quotes were obtained in accordance with the small purchase procurement policies or purchasing thresholds included in SPO Vendor List Contract No. 15-05 on the Form 10-B. Out of the 5 transactions, 4 transactions were other small purchases exceeding \$5,000. The remaining transaction exceeded \$5,000 and utilized Vendor List Contract No. 15-05.

Criteria

In accordance with the 2017 and 2018 Office of Management and Budget (OMB) *Compliance Supplement* and in accordance with 2 CFR § 200.317, "States, and governmental subrecipients of States, will use the same State policies and procedures used for procurements from non-Federal funds."

**DEPARTMENT OF EDUCATION
STATE OF HAWAII**

Schedule of Findings and Questioned Costs

Fiscal Year Ended June 30, 2018

In accordance with 2 CFR § 200.303, the non-Federal entity must establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award.

Cause

The Department did not adhere to established policies and procedures for small purchases and the utilization of vendor lists.

Effect

The Department has not complied with applicable small purchase procurement policies and vendor list terms.

Questioned Costs

No questioned or known costs were identified.

Identification as a Repeat Finding, if applicable

Not applicable.

Recommendation

We recommend that the Department strengthen its internal controls and supervisory review over the small purchase procurement process and the utilization of vendor lists, such as SPO Vendor List Contract No. 15-05, including retention of supporting documentation.

Views of Responsible Official(s) and Planned Corrective Action

Management agrees with the findings and recommendations. See Corrective Action Plan on page 65.

PART V

CORRECTIVE ACTION PLAN

(Provided by the Department of Education, State of Hawaii)



STATE OF HAWAII
DEPARTMENT OF EDUCATION
P.O. BOX 2360
HONOLULU, HAWAII 96804

OFFICE OF THE SUPERINTENDENT

March 25, 2019

KKDLY LLC
Topa Financial Center
745 Fort Street, Suite 2100
Honolulu, HI 96813

Ladies and Gentlemen:

The Single Audit of the State of Hawaii Department of Education (HIDOE) for the fiscal year ended June 30, 2018 was completed before the March 31, 2019 Federal deadline. We are pleased that the HIDOE received an unmodified opinion on its financial statements.

We have reviewed your audit findings and recommendations and corrective action plans have been prepared. In accordance with 2 CFR 200.508, the following pages contain the **Corrective Action Plan** for the year ended June 30, 2018 and the **Summary Schedule of Prior Audit Findings** for the year ended June 30, 2017.

Sincerely,

A handwritten signature in blue ink, appearing to be "CK", written over a blue horizontal line.

Dr. Christina M. Kishimoto
Superintendent

CMK:dy
Attachments

c: Internal Audit Office

**STATE OF HAWAII DEPARTMENT OF EDUCATION
CORRECTIVE ACTION PLAN
Fiscal Year Ended June 30, 2018**

FINANCIAL STATEMENT FINDING

2018-001 Accounting for Capital Assets (Page 54)

View of Responsible Officials

Management agrees with the finding and recommendation.

Corrective Action Plan

Conditions 1 and 2: Since the FY 2017 audit, the Office of School Facilities and Support Services (OSFSS) has commenced a reorganization of OSFSS and the accounting duties of the Facilities Development Branch (FDB) have been transferred to the Auxiliary Services Branch (ASB) where a new fiscal section will be responsible for tracking fixed assets.

Although the OSFSS reorganization has not been approved yet, FDB and ASB staff has worked with a Certified Public Accounting firm to help establish fixed asset guidelines to ensure classifications are consistent each year. When the classification guidelines are complete, they will be submitted to the Accounting Services Branch for their comment and review. Once the guidelines are reviewed and approved by all parties, it will become part of the fixed asset classification process where projects will be categorized accurately and consistently.

*Contact Person: Riki Fujitani, Auxiliary Services Director
Auxiliary Services Branch
Office of School Facilities and Support Services*

Anticipated Completion Date: June 30, 2020

Condition 3: The DOE maintains its financial accounting and equipment inventory records on the DOE's computerized Financial Management System (FMS). The processing and management of equipment inventory items is performed by each individual school and office. When schools and offices make changes to the item quantity, the FMS system automatically executes re-calculations of the item cost, causing the item cost to increase, most times incorrectly. This miscalculation results in an overstatement of original cost on DOE's FMS records and financial reports.

2018-001 Accounting for Capital Assets (Continued)

Due to the age of the FMS system, there is a significant risk in making any changes to the system. Therefore, although we could make a change to the FMS system to address this unnecessary re-calculation processing, we do not want to take the risk of “breaking” the system. As a temporary fix, the Accounting Section will review fixed asset equipment additions on the FMS System at a minimum, once a year, to identify input calculation errors that may result in an overstatement of equipment inventory original costs.

*Contact Person: Trisha Kaneshiro, Fiscal Specialist
Accounting Services Branch – Accounting Section
Office of Fiscal Services*

Anticipated Completion Date: June 30, 2019

**STATE OF HAWAII DEPARTMENT OF EDUCATION
CORRECTIVE ACTION PLAN
Fiscal Year Ended June 30, 2018**

FINANCIAL STATEMENT FINDING

2018-002 Procurement and Suspension and Debarment (Page 56)

View of Responsible Officials

Management acknowledges the finding and recommendation.

Corrective Action Plan

The Office of Fiscal Services, Procurement and Contracts Branch (PCB) in collaboration with the Office of Strategy, Innovation and Performance, School Transformation Branch (STB) will obtain a list of the school personnel involved in the procurement and purchasing activities that utilize these grant funds.

Those administrators on this list who have not renewed and strengthened their knowledge in the area of procurement within the past three years will be requested to review the Hawaii Department of Education's (HIDOE) Guidelines for Procurement and Contracting and complete the Procurement and Contracts Training Session registering for the course to obtain a Certificate of Completion via the PDE3 system (PDE3 course number is PD182438 with course content found on the SASA Resources website accessed through the HIDOE Intranet). The individuals will be asked to obtain their Certificate of Completion on or before December 31, 2019.

The STB will share information on the small purchase procurement process with STB staff, Title I Linkers, and Complex Area School Improvement Team members and will include the information in our Title I Fiscal Guidelines and allocation notices to remind all parties of the procurement process. While the focus may be on schools eligible to receive Title I, Part A funds, all schools receiving School Improvement Grant funds are Title I schools. The STB will remind all parties that the small purchase procurement process must be followed whether they are using Title I Grant funds or School Improvement Grant funds.

The PCB will also work with the STB to determine if it is additionally appropriate to conduct procurement training to include topics such as the use of price lists and vendor lists, and policies and procedures related to the small purchase method of procurement. Training could also cover the importance of reviewing for completeness and maintaining in file, documentation related to procurement and contracting actions taken.

2018-002 Procurement and Suspension and Debarment (Continued)

Trainings may be conducted via a combination of in person or web-based sessions depending upon the location of the personnel attending and the schools receiving these grant funds.

*Contact Persons: Lois Mow, Director
Procurement and Contracts Branch
Office of Fiscal Services*

*Wanelle Kaneshiro, Director
School Transformation Branch
Office of Strategy, Innovation, and Performance*

Anticipated Completion Date: December 31, 2019

**STATE OF HAWAII DEPARTMENT OF EDUCATION
CORRECTIVE ACTION PLAN
Fiscal Year Ended June 30, 2018**

FINANCIAL STATEMENT FINDING

2018-003 Procurement and Suspension and Debarment (Page 58)

View of Responsible Officials

Management acknowledges the finding and recommendation.

Corrective Action Plan

The Office of Fiscal Services, Procurement and Contracts Branch (PCB) in collaboration with the Office of Strategy, Innovation and Performance, School Transformation Branch (STB) will obtain a list of the school personnel involved in the procurement and purchasing activities that utilize these grant funds.

Those administrators on this list who have not renewed and strengthened their knowledge in the area of procurement within the past three years will be requested to review the Hawaii Department of Education's (HIDOE) Guidelines for Procurement and Contracting and complete the Procurement and Contracts Training Session registering for the course to obtain a Certificate of Completion via the PDE3 system (PDE3 course number is PD182438 with course content found on the SASA Resources website accessed through the HIDOE Intranet). The individuals will be asked to obtain their Certificate of Completion on or before December 31, 2019.

The STB will share information on the small purchase procurement process with STB staff, Title I Linkers, and Complex Area School Improvement Team members and will include the information in our Title I Fiscal Guidelines and allocation notices to remind all parties of the procurement process. While the focus may be on schools eligible to receive Title I, Part A funds, all schools receiving School Improvement Grant funds are Title I schools. The STB will remind all parties that the small purchase procurement process must be followed whether they are using Title I Grant funds or School Improvement Grant funds.

The PCB will also work with the STB to determine if it is additionally appropriate to conduct procurement training to include topics such as the use of price lists and vendor lists, and policies and procedures related to the small purchase method of procurement. Training could also cover the importance of reviewing for completeness and maintaining in file, documentation related to procurement and contracting actions taken.

2018-003 Procurement and Suspension and Debarment (Continued)

Trainings may be conducted via a combination of in person or web-based sessions depending upon the location of the personnel attending and the schools receiving these grant funds.

*Contact Persons: Lois Mow, Director
Procurement and Contracts Branch
Office of Fiscal Services*

*Wanelle Kaneshiro, Director
School Transformation Branch
Office of Strategy, Innovation, and Performance*

Anticipated Completion Date: December 31, 2019

PART VI

SUMMARY SCHEDULE OF PRIOR AUDIT FINDING
(Provided by the Department of Education, State of Hawaii)

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
Prior Fiscal Year Ended June 30, 2017

SECTION II – FINANCIAL STATEMENT FINDINGS

2017-001 Tracking and Accounting for Capital Assets

(Page 56 to 58 of the Prior Year June 30, 2017 Report)

Status -- *As the shift of fiscal capital improvement project responsibilities from the Facilities Development Branch to the Auxiliary Services Branch occurred during fiscal year 2018 and the Office of Facilities and Support Services (OSFSS) reorganization has not yet been approved corrective action is still in progress.*

OSFSS is working with a certified public accounting firm to help establish fixed asset guidelines to ensure classifications are consistent each year. When the classification guidelines are complete, they will be submitted to the Accounting Services Branch for their comment and review. Once the guidelines are reviewed and approved by all parties, it will become part of the fixed asset classification process where projects will be categorized accurately and consistently. Please refer to the current year response in the Financial Statement Finding No. 2018-001.