Hawaii Health Systems Corporation

Financial Report
with Supplemental Information
June 30, 2016

Hawaii Health Systems Corporation

Contents

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Independent Auditor's Report

To the Board of Directors
Hawaii Health Systems Corporation

Report on the Financial Statements

We have audited the accompanying financial statements of Hawaii Health Systems Corporation (HHSC), a component unit of the State of Hawaii, as of and for the year ended June 30, 2016 and the related notes to the financial statements, which collectively comprise HHSC's financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of HHSC as of June 30, 2016 and the respective changes in its financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of Directors
Hawaii Health Systems Corporation

Emphasis of Matter

As discussed in Note 1, the financial statements present only HHSC (a component unit of the State of Hawaii) and do not purport to, and do not, present fairly the financial position of the State of Hawaii as of June 30, 2016 or the changes in its financial position or its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified in respect to this matter.

Other Matters

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise Hawaii Health Systems Corporation's financial statements. The accompanying other supplemental information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Required Supplemental Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, schedule of the proportionate share of the net pension liability, and schedule of contributions, as identified in the table of contents, 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, which 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 supplemental information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

To the Board of Directors
Hawaii Health Systems Corporation

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated December 28, 2016 on our consideration of HHSC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the 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 HHSC's internal control over financial reporting and compliance.

Plante & Moran, PLLC

December 28, 2016

This discussion and analysis of Hawaii Health Systems Corporation’s (HHSC or the “Corporation”) financial performance provides an overview of the Corporation's financial activities for the fiscal years ended June 30, 2016 and 2015. Please read it in conjunction with the Corporation's financial statements, which begin on page 13.

Using this Annual Report

The Corporation's financial statements consist of three statements: (a) a statement of net position, (b) a statement of revenue, expenses, and changes in net position, and (c) a statement of cash flows. These financial statements and related notes provide information about the activities of the Corporation, including resources held by the Corporation but restricted for specific purposes. It is important to note that as of July 1, 2014, the Corporation implemented a new accounting standard, GASB 68, which is reflected in the amounts shown below for 2016 and 2015.

The Statement of Net Position and Statement of Revenue, Expenses, and Changes in Net Position

The analysis of the Corporation's finances begins on page 5. One of the most important questions asked about the Corporation's finances is, "Is the Corporation as a whole better or worse off as a result of the year's activities?" The statement of net position and the statement of revenue, expenses, and changes in net position report information about the Corporation's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenue and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Corporation's net position and changes thereof. You can think of the Corporation's net position - the difference between assets and deferred outflows compared to liabilities and deferred inflows - as one way to measure the Corporation's financial health or financial position. Over time, increases or decreases in the Corporation's net position are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the Corporation's patient base and measures of the quality of service it provides to the community, as well as local economic factors, to assess the overall health of the Corporation.

The Statement of Cash Flows

The final required statement is the statement of cash flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operating, investing, and financing activities. It provides answers to such questions as, "Where did cash come from?”, "What was cash used for?", and "What was the change in cash balance during the reporting period?"

The Corporation's Net Position

The Corporation's net position is the difference between its assets plus deferred outflows and liabilities plus deferred inflows reported in the statement of net position. The Corporation's net position increased by $9,297,597 (2 percent) in 2016 and increased by $22,109,899 after restatement in 2015, as you can see from the following table.

Assets and Deferred Outflows, Liabilities and Deferred Inflows, and Net Position

Summarized financial information of HHSC's statement of net position as of June 30, 2016 and 2015 is as follows:

	2016	2015
Assets		
Current assets	$ 305,966,031	$ 292,659,374
Capital assets - Net	358,553,697	363,310,339
Other assets	4,851,311	7,150,602
Deferred Outflows	81,615,629	68,293,235
Total assets and deferred outflows	**$ 750,986,668**	**$ 731,413,550**
Liabilities		
Current liabilities	$ 115,648,733	$ 128,278,636
Other postemployment liability	369,314,030	338,248,725
Due to the State of Hawaii	20,122,507	34,122,507
Accrued postretirement benefit obligations	623,325,235	583,997,239
Other liabilities	79,744,740	88,630,726
Deferred Inflows	42,551,713	67,153,604
Total liabilities and deferred inflows	1,250,706,958	1,240,431,437
Net Position		
Invested in capital assets - Net of related debt	310,465,416	304,552,720
Restricted	1,512,025	4,132,930
Unrestricted	(811,697,731)	(817,703,537)
Total net position	(499,720,290)	(509,017,887)
Total liabilities and net position	**$ 750,986,668**	**$ 731,413,550**

At June 30, 2016 and 2015, HHSC's current assets approximated 46 and 44 percent, respectively, of total assets. Current assets increased approximately $13.3 million in 2016 due to an increase in cash of $16.3 million and a decrease in due from the State of Hawaii CIP funds of $6 million. These changes are offset by an increase in third-party payor settlements of approximately $12.2 million. Current assets increased approximately $36.8 million in 2015 due to increases in cash of $30.8 million and due from State of Hawaii CIP funds of $16.1 million. These increases are offset by a decrease in third-party payor settlements of $13.4 million. The increases in cash for both 2016 and 2015 are primarily due to various factors, as reflected in the statement of cash flows. The decrease in due from the State of Hawaii CIP funds for 2016 is due to the timing of when payments were made from the state to HHSC. The increase in due from State of Hawaii CIP funds for 2015 is due to additional unexpended appropriations from the State of Hawaii for capital improvements. The increase in estimated third-party payor settlements in 2016 and the 2015 decrease is primarily attributable to the timely payment of uncompensated care revenue and significant settlements of prior year cost report filings, primarily for the three acute facilities in HHSC. The reasons for this change are discussed in the operating results and changes in net position section below.

At June 30, 2016 and 2015, HHSC's current liabilities were approximately 9 and 10 percent of total liabilities, respectively. The primary reason for the decrease in current liabilities in 2016 is due to the timing of payments coupled with the completion of significant capital projects during 2016. The primary reason for the decrease in current liabilities in 2015 of $29.2 million is due to a $16.7 million decrease in accounts payable and accrued expenses and a decrease in the current portion of long-term debt of $12.6 million. The decrease in accounts payable and accrued expenses is primarily due to the savings realized from HHSC's contingency plans, increases in cash collections, and cost reporting and other settlements from third-party payors, which allowed HHSC to pay down previously extended accounts payable. The decrease in current portion of long-term debt is due to the refinancing in January 2015 of Maui Memorial Medical Center's (MMMC) series 2013 bond issuance through the issuance of Revenue Bond Number 3, which extended the payment term of the series 2013 bond issuance.

At June 30, 2016 and 2015, HHSC's net position is reflected as its investment in capital assets, net of related debt, of approximately $310 million and $305 million, respectively. Total net position was approximately $(500 million) in 2016 and $(509 million) in 2015.

Capital Assets

At June 30, 2016 and 2015, HHSC's capital assets, net of accumulated depreciation, comprised approximately 54 and 55 percent of its total assets, respectively. These assets consist mainly of land, hospital buildings, and equipment that are used in HHSC's operations. The decrease of approximately $4.8 million in 2016 is due to depreciation taken on previously placed-in-service assets and the completion of significant portions of the EMR project and the increase of approximately $8.9 million in 2015 is due primarily to ongoing construction projects, particularly the EMR project.

A summary of HHSC's capital assets as of June 30, 2016 and 2015 is as follows:

	2016	2015
Land and land improvements	$ 7,814,855	$ 7,770,788
Building and improvements	479,469,411	458,859,742
Equipment	256,948,507	238,381,691
Construction in progress	28,612,313	32,120,301
Total capital assets	772,845,086	737,132,522
Less accumulated depreciation and amortization	(414,291,389)	(373,822,183)
Capital assets - Net	**$ 358,553,697**	**$ 363,310,339**

Long-term Debt and Capital Lease Obligations

At June 30, 2016 and 2015, HHSC had long-term debt and capital lease obligations totaling approximately $55.8 million and $66.6 million, respectively. The decrease of $10.8 million in 2016 and $10.4 million in 2015 was due to continuing payments on existing obligations with very little new issuances of capital lease obligations. More detailed information about HHSC's long-term debt and capital lease obligations is presented in the notes to the financial statements.

Operating Results and Changes in Net Position

Summarized financial information of HHSC's statement of revenue, expenses, and changes in net position for the years ended June 30, 2016 and 2015 is as follows:

	2016	2015
Operating revenue	$ 642,883,682	$ 620,537,502
Operating expenses:		
Salaries and wages	310,868,241	311,684,721
Employee benefits	166,477,967	168,013,909
Purchased services and professional fees	114,539,125	100,463,590
Medical supplies and drugs	80,916,401	76,988,122
Depreciation	40,935,072	37,180,988
Insurance	5,304,148	5,558,652
Other	63,237,754	65,688,088
Total operating expenses	782,278,708	765,578,070
Operating loss	(139,395,026)	(145,040,568)
Nonoperating revenue:		
General appropriations from the State of Hawaii	121,440,000	106,440,001
Other nonoperating revenue - Net	4,770,025	12,547,965
Total nonoperating revenue	126,210,025	118,987,966
Excess of expenses over revenue before capital contributions and transfer from affiliate	(13,185,001)	(26,052,602)
Capital contributions	25,040,520	48,162,501
Asset impairment	(3,521,882)	-
Change in reporting entity	963,960	-
Increase in net position	**$ 9,297,597**	**$ 22,109,899**

For the years ended June 30, 2016 and 2015, HHSC's operating expenses exceeded its operating revenue by $139.4 million and $145.0 million, respectively. General appropriations from the State of Hawaii totaled $121.4 million and $106.4 million in 2016 and 2015, respectively. In addition, the appropriations from the State of Hawaii for capital contributions totaled $25.0 million and $48.1 million in 2016 and 2015, respectively. These items, along with the other nonoperating revenue, contributed to an increase in net position of $9.3 million in 2016 and $22.1 million in 2015.

Operating expenses for the fiscal year ended June 30, 2016 were approximately 2.2 percent higher than 2015. Operating expenses for the fiscal year ended June 30, 2016 increased $16.7 million from fiscal year 2015, which was primarily due to increases in purchased services of approximately $14.1 million, with the remainder due to normal inflationary cost increases. The increase in purchased services and professional fees is primarily due to the use of consultants to assist in the implementation of the Siemens Soarian electronic medical records system and to perform helpdesk functions for the product, as well as consultants used to assist in the preparation of HHSC's facilities for the conversion to the ICD-10 coding standard.

Operating revenue for the fiscal year ended June 30, 2016 was approximately 3.6 percent higher than 2015. The increase in operating revenue is primarily due to an increase in acute patient days from fiscal year 2015, coupled with an increase in payments from various health plans related to uncompensated care programs. Additional increases in revenue is driven by third-party payor contract negotiations, clinical documentation improvement initiatives, and strategic pricing initiatives.

Operating expenses for the fiscal year ended June 30, 2015 were approximately 3.9 percent higher than 2014. Operating expenses for the fiscal year ended June 30, 2015 increased $28.5 million from fiscal year 2014, which was primarily due to increases in payroll expenses of $16.1 million and nonpayroll expenses of $12.4 million. The increase in payroll expenses is primarily due to collective bargaining pay increases as stipulated under bargaining unit contracts negotiated by the State of Hawaii, which were offset by contingency plan payroll savings of approximately $11.7 million, primarily through attrition and retirement savings. The increase in nonpayroll expenses is primarily due to $3.2 million in purchased services and professional fees and $5.2 million, with the remainder due to normal inflationary cost increases. The increase in purchased services and professional fees is primarily due to the use of consultants to assist in the implementation of the Siemens Soarian electronic medical records system and to perform helpdesk functions for the product, as well as consultants used to assist in the preparation of HHSC's facilities for the conversion to the ICD-10 coding standard. The increase in depreciation expense is due to a full year of depreciation on the electronic medical records system at Maui Memorial Medical Center as opposed to only four months of depreciation in 2014, as well as the depreciation on the electronic medical records system at Kula Hospital and Lanai Community Hospital, which went live on the system in March 2015.

Operating revenue for the fiscal year ended June 30, 2015 was approximately 7.6 percent higher than 2014. The increase in operating revenue is primarily due to a 3.5 percent increase in acute patient days from fiscal year 2014, $10 million in additional revenue as a result of catch-up interim settlements for HHSC's critical access hospitals as a result of the establishment of the State of Hawaii's QUEST Integration program, and additional revenue received from third-party payor contract negotiations, clinical documentation improvement initiatives, and strategic pricing initiatives.

Fiscal year 2016 was a very difficult year for HHSC. HHSC started the fiscal year anticipating having to pay for increased costs of $16.2 million in collective bargaining raises and $34.7 million in projected fringe benefit rate increases assessed by the State of Hawaii due to a 10 percent increase in the fringe benefit rate, with only $1.9 million in funding provided to cover those costs. As a result, HHSC management and governance developed contingency plans to deal with the deficit caused by these projected cost increases. These plans were implemented at the start of fiscal year 2016 and included the following actions:

EAST HAWAII REGION:

- Closed home care services
- Closed operations of one wing of adult inpatient psychiatry care at Hilo Medical Center
- Reduced the number of long-term care beds in service at Hilo Medical Center, Hale Ho'ola Hamakua, and Ka'u Hospital
- Reduced 87 FTEs - Combination of Reduction-in-Force (RIF), attrition, and elimination of traveler contracts

WEST HAWAII REGION:

- Closed operations of the 18-bed skilled nursing facility at Kona Community Hospital
- Reduced 24 FTEs via RIF

KAUAI REGION:

- Reduced physician costs
- Reduced 23 FTEs via RIF

OAHU REGION:

- Closed operations of 38 beds (25 percent of capacity) at Leahi Hospital
- Closed operations of 38 beds (25 percent of capacity) at Maluhia
- Reduced 42 FTEs via RIF

The fringe benefit rate did not actually increase until March 2016, when it increased from 42.99 percent to 49.54 percent. As a result, HHSC was forced to absorb approximately $14.2 million of the expected $34.7 million increase in the fringe benefit rate assessment. That, in conjunction with nearly $7 million in increased revenue from a strategic pricing initiative and clinical documentation improvement, allowed HHSC to reduce its projected net cash flow deficit of $15 million to a net cash flow surplus of $16.3 million.

FUTURE OUTLOOK:

As long as the State of Hawaii continues to impose collective bargaining pay and fringe benefit increases upon HHSC without providing funding to fully cover those costs, HHSC management believes continued increasing in General Fund support will be necessary to maintain the basic safety-net services that its facilities currently provide to the communities that they serve. If HHSC's facilities are forced to further reduce services, it will further reduce access to care in communities where there is already a shortage of healthcare services that the communities need and deserve.

Given the likely financial shortfalls that HHSC is likely to face, management believes that the challenges HHSC faces in maintaining and growing health services in a sustainable way cannot be resolved by the system in its current form. The best alternative for communities to receive the health care they deserve at the minimum cost to the State of Hawaii would be to find a private health system which would be interested in assuming operations of our hospitals. HHSC's boards believe a transition would allow HHSC's facilities to:

- Gain access to private capital to build and maintain infrastructure and address physical plant needs
- Optimize clinical practice and expand access to specialty services
- Implement private sector compensation packages to retain qualified medical service personnel
- Reduce waste and obtain efficiencies of scale
- Create a sustainable model of health care delivery that will lower costs and improve quality outcomes
- Reduce dependence on government subsidies

Whether this is a viable solution for all our facilities and desired by the communities they serve is unknown at this time.

Management has worked diligently with the Kaiser Permanente, the State Legislature, the State Administration, and the Hawaii public sector unions to facilitate the transition of HHSC's Maui Region facilities to Kaiser Permanente. However, due to a lawsuit filed by the United Public Workers union, the subsequent injunction, as well as delays incurred while the State Administration negotiated with both public sector unions to settle the lawsuit, the original transition date of July 1, 2016 has now been pushed back to July 1, 2017.

Contacting the Corporation's Financial Management

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Corporation's finances and to show the Corporation's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Corporation's corporate office at Hawaii Health Systems Corporation, 3675 Kilauea Avenue, Honolulu, HI 96816.

Statement of Net Position
June 30, 2016

Assets and Deferred Outflows of Resources

Current Assets	
Cash and cash equivalents - State of Hawaii (Note 2)	$ 1,138,522
Cash and cash equivalents	101,694,559
Patient accounts receivable - Less allowance for doubtful accounts of $39,094,347 (Note 2)	79,240,985
Investments (Note 3)	7,362,814
Supplies and other current assets	16,215,658
Due from the State of Hawaii (Note 5)	80,678,873
Estimated third-party payor settlements	19,634,620
Total current assets	305,966,031
Capital Assets - Net (Note 4)	358,553,697
Assets Limited as to Use (Note 2)	4,211,441
Other Assets	639,870
Total assets	669,371,039
Deferred Outflows of Resources - Pension (Note 7)	81,615,629
Total assets and deferred outflows of resources	**$ 750,986,668**

See Notes to Financial Statements.

Statement of Net Position (Continued)
June 30, 2016

Liabilities and Net Position

Current Liabilities	
Current portion of long-term debt (Note 9)	$ 1,843,484
Current portion of capital lease obligations (Note 9)	6,629,441
Accounts payable and accrued expenses	84,331,813
Current portion of accrued workers' compensation (Note 10)	3,651,000
Current portion of accrued vacation (Note 6)	18,755,699
Other current liabilities	1,771,621
Total current liabilities	116,983,058
Long-term Debt - Less current portion (Note 9)	38,045,921
Capital Lease Obligation - Less current portion (Note 9)	9,276,414
Other Liabilities	
Accrued vacation - Less current portion (Note 6)	20,967,335
Accrued workers' compensation - Less current portion (Note 10)	9,811,000
Other postemployment benefit liability (Note 8)	369,314,030
Due to the State of Hawaii (Note 5)	20,122,507
Pension liability (Note 7)	623,325,235
Patients' safekeeping deposits	252,024
Other liabilities	57,721
Total liabilities	1,208,155,245
Deferred Inflows of Resources - Pension (Note 7)	42,551,713
Total liabilities and deferred inflows of resources	1,250,706,958
Net Position	
Net investment in capital assets	310,465,416
Restricted for capital purchases (Note 2)	1,512,025
Unrestricted	(811,697,731)
Total net position	(499,720,290)
Total liabilities and net position	**$ 750,986,668**

Hawaii Health Systems Corporation

Statement of Revenue, Expenses, and Changes in Net Position
Year Ended June 30, 2016

Operating Revenue	
Net patient service revenue (net of provision for doubtful accounts of $24,853,414)	$ 631,378,822
Other revenue	11,504,860
Total operating revenue	642,883,682
Operating Expenses	
Salaries	310,868,241
Employee benefits	166,481,006
Medical supplies and drugs	80,916,401
Depreciation and amortization	40,935,072
Utilities	14,397,973
Repairs and maintenance	16,001,540
Other supplies	16,830,667
Purchased services	97,718,744
Professional fees	16,820,381
Insurance	5,304,148
Rent and lease	7,851,528
Other	8,153,007
Total operating expenses	782,278,708
Operating Loss	(139,395,026)
Nonoperating Revenue (Expenses)	
General appropriations from the State of Hawaii	121,440,000
Collective bargaining pay raise appropriation from the State of Hawaii	1,731,942
Loss on disposal of capital assets	(10,302)
Restricted contributions	2,679,725
Interest expense	(3,351,630)
Interest and dividend income	386,181
Other nonoperating revenue - Net	3,334,109
Total nonoperating revenue	126,210,025
Excess of Expenses Over Revenue Before Capital Contributions and Other	(13,185,001)
Capital Contributions	25,040,520
Special Item - Asset impairment (Note 4)	(3,521,882)
Change in Reporting Entity (Note 1)	963,960
Increase in Net Position	9,297,597
Net Position - Beginning of year	(509,017,887)
Net Position - End of year	**$ (499,720,290)**

See Notes to Financial Statements.

Hawaii Health Systems Corporation

Statement of Cash Flows
Year Ended June 30, 2016

Cash Flows from Operating Activities	
Cash received from government, patients, and third-party payors	$ 627,782,092
Cash payments to employees for services	(448,370,790)
Cash payments to suppliers for services and goods	(269,933,549)
Other receipts from operations	11,504,860
Net cash used in operating activities	(79,017,387)
Cash Flows from Noncapital Financing Activities	
Appropriations from the State of Hawaii	107,440,000
Collective bargaining funding from the State of Hawaii	1,731,942
Other nonoperating revenue - Net	6,013,834
Net cash provided by noncapital financing activities	115,185,776
Cash Flows from Capital and Related Financing Activities	
Purchase of capital assets	(5,763,590)
Interest paid	(3,351,630)
Repayments on long-term debt	(2,667,588)
Repayments on capital lease obligations	(10,232,858)
Proceeds from sale of assets	18,000
Net cash used in capital and related financing activities	(21,997,666)
Cash Flows from Investing Activities	
Interest income	386,181
Decrease in short-term investments and assets limited as to use	1,791,566
Net cash provided by investing activities	2,177,747
Net Increase in Cash and Cash Equivalents	16,348,470
Cash and Cash Equivalents - Beginning of year	86,484,611
Cash and Cash Equivalents - End of year	**$ 102,833,081**
Balance Sheet Classification of Cash and Cash Equivalents	
Cash and cash equivalents - State of Hawaii	$ 1,138,522
Cash and cash equivalents	101,694,559
Total cash and cash equivalents	**$ 102,833,081**

See Notes to Financial Statements.

A reconciliation of operating loss to net cash used in operating activities is as follows:

Cash Flows from Operating Activities	
Operating loss	$ (139,395,026)
Adjustments to reconcile operating loss to net cash from operating activities:	
Provision for doubtful accounts	24,853,414
Depreciation and amortization	40,935,072
Changes in assets and liabilities:	
Patient accounts receivable	(16,298,737)
Supplies and other assets	1,700,702
Accounts payable, accrued expenses, and other liabilities	(8,400,285)
Accrued workers' compensation liability	(317,000)
Postemployment benefit liability	31,065,305
Pension liability	39,327,996
Deferred outflows and inflows	(37,924,285)
Estimated third-party payor settlements	(12,151,407)
Accrued vacation	(2,413,136)
Net cash used in operating activities	**$ (79,017,387)**
Noncash Financing and Investing Activities	
Asset impairment	$ 3,521,882
Capital assets contributed by the State of Hawaii and others	28,111,724
Loss on disposal of capital assets	10,302
State of Hawaii appropriation to forgive amount payable to State of Hawaii	14,000,000
Capital assets acquired via accounts payable	951,281
Change in reporting entity	963,960
Change in due from the State of Hawaii	5,700,376
Assets acquired via capital lease	2,199,447

Note 1 - Organization

Structure - Hawaii Health Systems Corporation (HHSC or the "Corporation") is a public body corporate and politic and an instrumentality and agency of the State of Hawaii (the "State"). HHSC is managed by a chief executive officer under the control of a 18-member board of directors.

In June 1996, the legislature of the State passed Act 262, S.B. 2522. The act, which became effective in fiscal year 1997, transferred all facilities under the administration of the Department of Health - Division of Community Hospitals to HHSC. HHSC currently operates the following facilities:

East Hawaii Region:
- Hilo Medical Center
- Hale Ho'ola Hamakua
- Ka'u Hospital
- Yukio Okutsu Veterans Care Home (Yukio is not included in the East Hawaii Region audited financial statements)

West Hawaii Region:
- Kona Community Hospital
- Kohala Hospital

Maui Region:
- Maui Memorial Medical Center
- Kula Hospital
- Lanai Community Hospital

Kauai Region:
- Kauai Veterans Memorial Hospital
- Samuel Mahelona Memorial Hospital

Oahu Region:
- Leahi Hospital
- Maluhia

Kahuku Medical Center

Act 262 also amended a previous act to exempt all facilities from the obligation to pay previously allocated central service and departmental administration expenses by the State.

HHSC is considered to be administratively attached to the Department of Health of the State and is a component unit of the State. The accompanying financial statements relate only to HHSC and the facilities, and are not intended to present the financial position, results of operations, or cash flows of the Department of Health.

Negotiations between HHSC and the State relating to the transfer of assets and assumption of liabilities pursuant to Act 262 had not been finalized as of June 30, 2016. Accordingly, the assets, liabilities, and net assets of HHSC reflected in the accompanying statement of revenue, expenses, and changes in net assets may be significantly different from those eventually included in the final settlement.

Note 1 - Organization (Continued)

The financial statements are being presented for HHSC, Hawaii Health Systems Foundation (HHSF), Alii Community Care, Inc. (Alii), and Kona Ambulatory Surgery Center (KASC). HHSF and Alii are nonprofit organizations of which HHSC is the sole member. The purpose of HHSF is to raise funds and to obtain gifts and grants on behalf of HHSC. The purpose of Alii is to own, manage, and operate assisted-living and other healthcare facilities in the state.

HHSC obtained a controlling interest in the Kona Ambulatory Surgery Center during fiscal year 2016. Accounting standards require this transaction to be recorded as a change in reporting entity, which requires the KASC net assets be recorded on the Regions books at the start of the fiscal year, July 1, 2015. The impact of the change in reporting entity amounted to approximately $1.0 million.

In June 2007, the state legislature passed Act 290, S.B. 1792. This act, which became effective July 1, 2007, required the establishment of a 7- to 15-member regional system board of directors for each of the five regions of the HHSC system. Each regional board was given custodial control and responsibility for management of the facilities and other assets in their respective regions. This act also restructured the 13-member HHSC board of directors to 15 members, comprised of 10 members appointed by the governor from nominees submitted by legislative leadership, two at-large members at the governor's discretion, two physician members selected by the HHSC board, and the State Director of Health.

Act 290 also exempted the regions from the requirements of the State procurement code and other exemptions from State agency laws, such as tax clearance certificate requirements, the concession law, and the sunshine law.

In 2009, the legislature passed Act 182, S.B. 1673, effective July 1, 2009, which allowed the individual facilities or regions of HHSC to transition into a new legal entity in any form recognized under the laws of the State of Hawaii, including but not limited to a nonprofit corporation, a for-profit corporation, a municipal facility, a public benefit corporation, or a combination of the above. The act also amended the requirement for maintenance of services to outline a process that must be followed in order for a facility to substantially reduce or eliminate a direct patient care service. Furthermore, the act reconstituted the HHSC board of directors to a 12-member board of directors which includes the five regional chief executive officers, one representative each appointed by the East Hawaii, West Hawaii, Kauai, and Oahu regional boards, two members appointed by the Maui regional board, and the director of the Department of Health as an ex-officio nonvoting member.

Note 1 - Organization (Continued)

In June 2011, the legislature passed Act 126, S.B. 1300, effective July 1, 2011, which reconstituted the HHSC board of directors to a 13-member board of directors by adding an at-large voting member appointed by the governor of the State of Hawaii and changing the voting status of the director of the Department of Health from a nonvoting to a voting member.

In June 2013, the legislature passed Act 278, H.B. 1130, effective July 2013, which reconstituted the HHSC board of directors by adding five regional members appointed by the governor and making the five regional chief executive officers ex-officio, nonvoting members.

In June 2015, the legislature passed Act 103, H.B. 1075, effective June 10, 2015, which allowed for the transition of the management of the Maui Region facilities to a new entity. Following the State of Hawaii Legislature passing Act 103 H.B. 1075, the HHSC - Maui Region accounced it had entered into a letter of intent to affiliate of Kaiser Permanente in September 2015. In January 2016, a transition agreement was signed with an expected effective date of July 1, 2016. Due to legal challenges and other delays, the expected transition date has been pushed back to July 1, 2017.

Kahuku Medical Center - In June 2007, the state legislature passed Act 113, H.B. 843. This act amended Hawaii Revised Statutes 323F to allow for the assimilation of Kahuku Hospital into HHSC in a manner and to an extent that was to be negotiated between Kahuku Hospital and HHSC. The act also specified that none of the liabilities of Kahuku Hospital were to become the liabilities of HHSC, that HHSC could adjust the levels of services provided by Kahuku Hospital, and that the employees of Kahuku Hospital were not to be considered employees of the State. This act appropriated $3,900,000, which was disbursed through the Department of Health of the State, to pay for the cost of acquiring the assets of Kahuku Hospital and to operate the facility. On March 14, 2008, the asset purchase was completed for a purchase price of approximately $2,652,000 in cash, including transaction costs of $197,000 in cash, and the facility is now operating as Kahuku Medical Center. The purchase price was allocated to assets based on their respective estimated fair values at the acquisition date.

Note 1 - Organization (Continued)

Liquidity - During the year ended June 30, 2016, HHSC incurred losses from operations of approximately $139 million and had negative cash flows from operations of $79 million. Overall, days in accounts payable have decreased 5.5 days as compared to June 30, 2015 due to contingency plans prepared by management to decrease costs (primarily through attrition savings) as well as increases in reimbursement from negotiations with third-party payors and one-time settlements from the State Medicaid QUEST Integration program which allowed facilities to pay previously extended vendor payables. Days in accounts receivable have decreased as compared to June 30, 2015 due primarily to more efficient billings now that the organizations have been using the Soarian electronic medical records system and have seen improvements since implementation. Downward pressure on reimbursements was due to federal healthcare reform and federal deficit legislation. Although improvements continue to be seen by HHSC, management believes maintaining the current levels of service provided by HHSC will require continued funding by the State of Hawaii.

Note 2 - Summary of Significant Accounting Policies

Basis of Accounting - HHSC prepares its financial statements using the economic resources measurement focus and the accrual basis of accounting.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents - Cash and cash equivalents include short-term investments with original maturities of three months or less. It also includes amounts held in the State Treasury. The state director of finance is responsible for the safekeeping of all monies paid into the State Treasury (cash pool). HHSC's portion of this cash pool at June 30, 2016 is indicated in the accompanying statement of net position as "cash and cash equivalents - State of Hawaii." The Hawaii Revised Statutes authorize the director of finance to invest in obligations of, or 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. Cash and deposits with financial institutions are collateralized in accordance with state statutes. 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.

Note 2 - Summary of Significant Accounting Policies (Continued)

HHSC has cash in financial institutions that is in excess of available depository insurance coverage. The amount of uninsured and uncollateralized deposits totaled approximately $98,970,000 at June 30, 2016. Accordingly, these deposits were exposed to custodial credit risk. Custodial credit risk is the risk that in the event of a financial institution failure, HHSC's deposits might not be returned to it. HHSC believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, HHSC evaluates each financial institution with which it deposits funds; only those institutions with an acceptable estimated risk level are used as depositories.

Accounts Receivable - Patient accounts receivable are stated at net realizable value amounts. An allowance for uncollectible accounts is established on an aggregate basis by using historical write-off factors applied to unpaid accounts based on aging. Loss rate factors are based on historical loss experience and adjusted for economic conditions and other trends affecting HHSC's ability to collect outstanding amounts. Uncollectible amounts are written off against the allowance for doubtful accounts in the period they are determined to be uncollectible. An allowance for contractual adjustments is based on expected payment rates from payors based on current reimbursement methodologies.

Supplies - Supplies consist principally of medical and other supplies and are recorded at the lower of first-in, first-out cost or market.

Capital Assets - Capital assets assumed from the State at inception are recorded at cost less accumulated depreciation. Other capital assets are recorded at cost or estimated fair market value at the date of donation. Donated buildings, equipment, and land are recognized as revenue when all eligibility requirements have been met, generally at the date of donation. Equipment under capital leases is recorded at the present value of future payments. Buildings, equipment, and improvements are depreciated by the straight-line method using these asset lives:

Building and improvements	5-40 years
Equipment	3-20 years

Gains or losses on the sale of capital assets are reflected in other nonoperating revenue. Normal repairs and maintenance expenses are charged to operations as incurred.

Certain of HHSC's capital improvement projects are managed by the State Department of Accounting and General Services. The related costs for these projects are transferred to HHSC's capital asset accounts and are reflected as revenue below the nonoperating revenue category in the statement of revenue, expenses, and changes in net position.

Note 2 - Summary of Significant Accounting Policies (Continued)

Assets Limited as to Use - Assets limited as to use are restricted net position, patients' safekeeping deposits, restricted deferred contributions, restricted cash, and cash in escrow accounts related to future lease draws. Such restrictions have been externally imposed by contributors or by collateral agreements. Restricted resources are applied before unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position are available. Patients' safekeeping deposits represent funds received or property belonging to the patients that are held by HHSC in a fiduciary capacity as custodian. Receipts and disbursements of these funds are not reflected in HHSC's operations.

At June 30, 2016, assets limited as to use consisted of restricted cash of $4,211,441.

Deferred Outflows/Inflows of Resources - In addition to assets, the statement of net position will sometimes report a separate section for deferred outflow of resources. This separate financial statement element represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (expense/expenditure) until then. HHSC has only one item that qualifies for reporting in this category. It is the deferred outflow of resources related to the cost-sharing defined benefit pension plan (see Note 7).

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (revenue) until that time. HHSC has only one item that qualifies for reporting in this category. It is the deferred inflow of resources related to the cost-sharing defined benefit pension plan (see Note 7).

Accrued Vacation and Compensatory Pay - HHSC accrues all vacation and compensatory pay at current salary rates, including additional amounts for certain salary-related expenses associated with the payment of compensated absences (such as employer payroll taxes and fringe benefits), in accordance with GASB Statement No. 16, *Accounting for Compensated Absences*. Vacation is earned at a rate of one and three-quarters working days for each month of service. Vacation days may be accumulated to a maximum of 90 days.

Postemployment Benefits - HHSC records an expense for postemployment benefits expense, such as retiree medical and dental costs, over the years of service on an accrual basis based on an allocation from the State of Hawaii primarily based on full-time equivalents.

Note 2 - Summary of Significant Accounting Policies (Continued)

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

Net Position - Net position is classified in three components. Net investment in capital assets consists of capital assets net of accumulated depreciation and is reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted expendable net position is noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Corporation. Unrestricted net position is the remaining net assets that do not meet the definition of invested in capital assets - net of related debt or restricted.

Operating Revenue and Expenses - HHSC has defined its operating revenue and expenses as those relating to the provision of healthcare services. The revenue and expenses relating to capital and related financing activities, noncapital financing activities, and investing activities are excluded from that definition.

Net Patient Service Revenue - Net patient service revenue is recorded on an accrual basis in the period in which the related services are provided at established rates, less contractual adjustments and provision for doubtful accounts. HHSC, as a safety net provider, provides charity care to certain patients; the specific cost of such care for the year ended June 30, 2016 was approximately $5,450,000.

HHSC has agreements with third-party payors that provide for payments at amounts different from their established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per-diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are recorded on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. The adjustments to the final settlements did not have a significant impact on the fiscal year 2016 financial statements.

The estimated third-party payor settlements are based on estimates because complete information is not currently available to determine the final settlement amounts for certain cost report years. Management has used its best effort, judgment, and certain methodologies to estimate the anticipated final outcome.

Note 2 - Summary of Significant Accounting Policies (Continued)

A summary of the payment arrangements with major third-party payors is as follows:

- *Medicare* - Inpatient acute services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge referred to as the inpatient prospective payment system (IPPS). Under the IPPS, each case is categorized into a diagnosis-related group (DRG). Each DRG has a payment weight assigned to it based on the average resources used to treat Medicare patients in that DRG.

  Outpatient services rendered to Medicare beneficiaries are paid under a prospective payment system called ambulatory payment classifications (APC). Services in each APC are similar clinically and in terms of the resources they require. A payment rate is established for each APC and, depending on the services provided, hospitals may be paid for more than one APC for an encounter.

  Skilled nursing services provided to Medicare beneficiaries are paid on a per-diem prospective payment system covering all costs (routine, ancillary, and capital) related to the services furnished. The per-diem payments for each admission are case-mix adjusted using a resident classification system (resource utilization groups) based on data from resident assessments and relative weights developed from staff time data.

  All Medicare-certified hospitals and skilled nursing facilities are required to file annual Medicare cost reports. HHSC facilities required to file Medicare cost reports have been audited by the Medicare fiscal intermediary through fiscal year 2012.

- *Medicaid* - Inpatient acute services rendered to Medicaid program beneficiaries are reimbursed under a prospectively determined rate per day and per discharge with a cost settlement for capital costs. Medicaid long-term care services are reimbursed based on a price-based case mix reimbursement system. The case-mix reimbursement system uses the resource utilization groups classification system calculated from the minimum data set assessment. The case-mix reimbursement payment method takes into account a patient's clinical condition and the resources needed to provide care for the patient. Medicaid outpatient services are reimbursed based on a fee schedule using current procedure terminology (CPT) codes established for the State.

Note 2 - Summary of Significant Accounting Policies (Continued)

- *Critical Access Hospital (CAH)* - HHSC has eight facilities (Hale Ho'ola Hamakua, Kauai Veterans Memorial Hospital, Kahuku Medical Center, Ka'u Hospital, Kohala Hospital, Kula Hospital, Lanai Community Hospital, and Samuel Mahelona Memorial Hospital) that are designated as critical access hospitals (CAHs) by the Centers for Medicare and Medicaid Services (CMS). CAHs are limited-service hospitals located in rural areas that receive cost-based reimbursement. To be designated a CAH, a facility must, among other requirements: (1) be located in a county or equivalent unit of a local government in a rural area, (2) be located more than a 35-mile drive from a hospital or another healthcare facility, or (3) be certified by the State as being a necessary provider of healthcare services to residents in the area. These facilities are paid an interim reimbursement rate throughout the year based on each facility's expected costs per inpatient day or the allowable outpatient cost-to-charge. After the close of each fiscal year, the facility would receive retrospective settlements for the difference between interim payments received and the total allowable cost as documented in the Medicare cost reports.

- *Sole Community Hospital* - HHSC has three facilities (Hilo Medical Center, Kona Community Hospital, and Maui Memorial Medical Center) that are designated as sole community hospitals by the CMS. Inpatient case rates for services rendered to Medicare beneficiaries are finally determined upon the filing of the annual Medicare cost reports.

- *Hawaii Medical Service Association (HMSA)* - Inpatient services rendered to HMSA subscribers are reimbursed at prospectively determined case rates. The prospectively determined case rates are not subject to retroactive adjustment. In addition, outpatient surgical procedures and emergency room visits are reimbursed at a negotiated case rate. All other outpatient services are reimbursed based on a fee schedule using standard CPT codes.

- *Other Commercial* - HHSC has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment under these agreements includes prospectively determined rates per discharge, discounts from established rates, and prospectively determined daily rates.

State Appropriations - HHSC recognizes general and capital appropriations at the time allotments are made available to the facility for expenditure.

Note 2 - Summary of Significant Accounting Policies (Continued)

Effective July 1, 2008, HHSC - Corporate (Corporate) permanently allocated general appropriations to each facility. General appropriations are reflected as nonoperating revenue and capital appropriations are included in capital grants and contributions after the nonoperating revenue (expenses) subtotal in the statement of revenue, expenses, and changes in net position. If restrictions are placed on such appropriations, the restrictions are given separate and discrete accounting recognition.

Bond Interest - HHSC is allocated an amount for interest paid by the State of general obligation bonds whose proceeds were used for hospital construction. A corresponding contribution from the State is also allocated to HHSC. The bonds are obligations for the State, to be paid by the State's General Fund, and are not reported as liabilities of HHSC. For the year ended June 30, 2016, interest expense totaled approximately $9,289,000.

Risk Management - HHSC is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years. The facilities are self-insured for workers' compensation and disability claims and judgments as discussed in Note 10.

New Accounting Pronoucement - In February 2015, the Governmental Accounting Standards Board issued GASB Statement No. 72, *Fair Value Measurement and Application*. The requirements of this statement will enhance comparability of financial statements among governments by requiring measurement of certain assets and liabilities at fair value using a consistent and more detailed definition of fair value and acceptable valuation techniques. This statement also will enhance fair value application guidance and related disclosures in order to provide information to financial statement users about the impact of fair value measurements on a government's financial position. The Corporation adopted this standard as of June 30, 2016.

Note 2 - Summary of Significant Accounting Policies (Continued)

Upcoming Accounting Changes - In June 2015, the GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which addresses reporting by governments that provide postemployment benefits other than pensions (OPEB) to their employees and for governments that finance OPEB for employees of other governments. This OPEB standard will require governments to recognize on the face of the financial statements their proportionate share of the net OPEB liability related to their participation in an OPEB fund. The Corporation already conforms to this presentation and the net liability for the Corporation's participation in the Employer-Union Health Benefits Trust Fund is recognized on the face of the financial statements. The OPEB standard will also enhance accountability and transparency through revised note disclosures and required supplemental information (RSI). The Corporation is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Corporation's 2018 fiscal year.

Concentration of Credit Risk - Patient accounts receivable consist of amounts due from insurance companies and patients for services rendered by the facilities. The facilities grant credit without collateral to their patients, most of whom are local residents and are insured under third-party payor arrangements. The mix of receivables from patients and third-party payors as of June 30, 2016 was as follows:

	Percentage
Medicare	35 %
Medicaid	25
HMSA	10
Other third-party payors	17
Patient and other	13
Total	100 %

Note 3 - Fair Value Measurements

HHSC categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. Investments that are measured at fair value using the net asset value per share (or its equivalent) as a practical expedient are not classified in the fair value hierarchy below.

Note 3 - Fair Value Measurements (Continued)

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. HHSC’s assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

HHSC has the following recurring fair value measurements as of June 30, 2016: U.S. Treasury securities of $4,562,464 are valued using quoted market prices (Level 2 inputs), U.S. government agencies of $2,747,176 are valued using a matrix pricing model (Level 2 inputs), and money market funds of $53,174 are valued using a matrix pricing model (Level 2 inputs).

The fair value of U.S. Treasury obligations, U.S. government agencies, and money market funds at June 30, 2016 were determined primarily based on Level 2 inputs. HHSC estimates the fair value of these investments using other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

The Corporation also has assets that under certain conditions are subject to measurement at fair value on a nonrecurring basis. These assets include property and equipment which are measured at fair value when impairment exists. At June 30, 2016, the Corporation recognized noncash impairment charges of $3,521,882 to adjust these assets to their estimated fair values.

HHSC's investments are subject to several types of risk, which are examined in more detail below:

Custodial Credit Risk of Investments

Custodial credit risk is the risk that, in the event of the failure of the counterparty, HHSC will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. All of HHSC's investments are held by financial institutions registered in HHSC's name.

Interest Rate Risk

As a means of limiting its exposure to fair value losses arising from interest rates, HHSC's investment policy generally limits maturities on investments to not more than five years from the date of investment. All of HHSC's investments at June 30, 2016 have an original maturity date within five years from the date of investment.

Note 3 - Fair Value Measurements (Continued)

Credit Risk

HHSC's 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, bankers' acceptances, and money market funds maintaining a Triple-A rating. As of June 30, 2016, HHSC held investments in U.S. Treasury securities and U.S. government agency obligations.

Concentration of Credit Risk

HHSC's investment policy provides guidelines for portfolio diversification by placing limits on the amount that may be invested in any one issuer, types of investment instruments, and position limits per issue of an investment instrument. There were no investments that individually exceed 5 percent of HHSC's total investments at June 30, 2016.

Note 4 - Capital Assets

Transactions in the capital asset accounts for the year ended June 30, 2016 were as follows:

	Beginning of Year	Additions	Retirements	Transfers and Adjustments	End of Year
Assets not subject to depreciation:					
Land and land improvements	$ 7,770,788	$ -	$ -	$ 44,067	$ 7,814,855
Construction in progress	32,120,301	20,264,393	(797,859)	(22,974,522)	28,612,313
Assets subject to depreciation:					
Buildings and improvements	461,567,963	334,748	-	17,566,700	479,469,411
Equipment	239,882,469	16,426,901	(4,724,618)	5,363,755	256,948,507
Total	741,341,521	37,026,042	(5,522,477)	-	772,845,086
Less accumulated depreciation:					
Buildings and improvements	(208,855,941)	(16,806,688)	-	-	(225,662,629)
Equipment	(166,476,986)	(24,124,067)	1,972,293	-	(188,628,760)
Total	(375,332,927)	(40,930,755)	1,972,293	-	(414,291,389)
Capital assets - Net	$ 366,008,594	$ (3,904,713)	$ (3,550,184)	$ -	$ 358,553,697

The State Department of Accounting and General Services and others transferred capital assets, including construction in progress, aggregating approximately $28,112,000 to HHSC as a contribution of capital for the year ended June 30, 2016.

The addition of Kona Ambulatory Surgery Center assets are reflected in the beginning of year balances, due to the change in reporting entity being effective July 1, 2015.

Note 4 - Capital Assets (Continued)

In July 2011, HHSC entered into a $28.7 million contract with Siemens Healthcare to implement its Soarian Electronic Medical Records and Health Information Systems. West Hawaii Region and Corporate implemented the system in February 2013. Maui Memorial Medical Center implemented the system in March 2014. The remainder of the Maui region implemented the system in March 2015. Kauai region implemented the system in July 2015. The other HHSC facilities will not be implementing the system.

During 2016, certain components of the EHR system were determined to be unusable, and the assets were impaired.

Note 5 - State of Hawaii Advances and Receivable

In fiscal year 2003, HHSC received a $14,000,000 advance from the State to relieve its cash flow shortfall. During 2016, an appropriation was granted from the State to allow HHSC to forego any obligation to pay back this amount. The remaining amount due to the State of $20,122,507 at June 30, 2016 is made up of cash advances to the Department of Health - Division of Community Hospitals, which was assumed by HHSC at the date of its formation.

At June 30, 2016, $80,678,873 was due from the State for allotments made to HHSC before June 30, 2016.

Note 6 - Accrued Vacation

Transactions in this account during the year ended June 30, 2016 were as follows:

	Beginning of Year	Additions	Reductions	End of Year	Current Portion	Noncurrent Portion
Accrued vacation	$ 42,136,170	$ 20,793,039	$ (23,206,175)	$ 39,723,034	$ 18,755,699	$ 20,967,335

Note 7 - Cost-sharing Defined Benefit Pension Plan

Plan Description - All full-time employees of HHSC are eligible to participate in the Employees' Retirement System of the State of Hawaii (ERS), a cost-sharing, multiple-employer, public employee retirement system covering eligible employees of the state and counties. The ERS issues a publicly available financial report that can be obtained at ERS's website: http://ers.ehawaii.gov/.

Note 7 - Cost-sharing Defined Benefit Pension Plan (Continued)

Benefits Provided - The ERS is composed of a contributory retirement plan and a noncontributory retirement plan. Eligible employees who were in service and members of the existing contributory plan on June 30, 1984 were given an option to remain in the existing plan or join the noncontributory plan effective January 1, 1985. All new eligible employees hired after June 30, 1984 automatically become members of the noncontributory plan. Both plans provide death and disability benefits and cost-of-living increases. Benefits are established by State statute. In the contributory plan, employees may elect normal retirement at age 55 with five years of credited service or elect early retirement at any age with 25 years of credited service. Such employees are entitled to retirement benefits, payable monthly for life, of 2 percent of their average final salary, as defined, for each year of credited service. Benefits fully vest on reaching five years of service; retirement benefits are actuarially reduced for early retirement. Covered contributory plan employees are required by State statute to contribute 7.8 percent of their salary to the plan; HHSC is required by State statute to contribute the remaining amounts necessary to pay contributory plan benefits when due. In the noncontributory plan, employees may elect normal retirement age at 62 with 10 years of credited service or at age 55 with 30 years of credited service, or elect early retirement at age 55 with 20 years of credited service. Such employees are entitled to retirement benefits, payable monthly for life, of 1.25 percent of their average final salary, as defined, for each year of credited service. Benefits fully vest on reaching 10 years of service; retirement benefits are actuarially reduced for early retirement. HHSC is required by state statute to contribute all amounts necessary to pay noncontributory plan benefits when due.

On July 1, 2006, a new hybrid contributory plan became effective pursuant to Act 179, Session Laws of Hawaii of 2004. Participants prior to July 1, 2006 could choose to participate in this hybrid plan or remain in the existing plans. New employees hired from July 1, 2006 are required to join the hybrid plan. Participants will contribute 6 percent of their salary to this plan. Furthermore, members in the hybrid plan are eligible for retirement at age 62 with five years of credited service or at age 55 and 30 years of credited service. Members will receive a multiplier of 2 percent for each year of credited service in the hybrid plan. The benefit payment options are similar to the current contributory plan.

Note 7 - Cost-sharing Defined Benefit Pension Plan (Continued)

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 rate for fiscal year 2016 was 17 percent. Contributions to the pension plan from the Corporation were $47.2 million for the fiscal year ended June 30, 2016.

The employer is required to make all contributions for members in the ERS. For contributory plan employees hired prior to July 1, 2012, general employees are required to contribute 7.8 percent of their salary. Hybrid plan members hired prior to July 1, 2012 are required to contribute 6.0 percent of their salary. Hybrid plan members hired after June 30, 2012 are required to contribute 8.0 percent of their salary.

Net Pension Liability, Deferrals, and Pension Expense

At June 30, 2016, the Corporation reported a liability of $623 million for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Corporation's proportion of the net pension liability was based on the Corporation's actuarially required contribution for the year ended June 30, 2016, relative to all other contributing employers. At June 30, 2015, the Corporation's proportion was 7.14 percent, which was an decrease of 0.14 percent from its proportion measured as of June 30, 2014.

For the year ended June 30, 2016, the Corporation recognized pension expense of $48,690,000. At June 30, 2016, the Corporation reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	$ 5,942,191	$ (16,636,481)
Net difference between projected and actual earnings on plan investments	-	(22,214,434)
Changes in assumptions	14,111,255	-
Changes in proportion	829,117	(3,700,798)
Employer contributions to the plan subsequent to the measurement date	60,733,066	-
Total	$ 81,615,629	$ (42,551,713)

Note 7 - Cost-sharing Defined Benefit Pension Plan (Continued)

The $60,733,066 reported as deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2016. Other reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Years Ending June 30	Amount
2017	$ (9,496,376)
2018	(9,496,376)
2019	(9,496,375)
2020	7,537,435
2021	(717,458)

Actuarial Assumptions - The total pension liability in the June 30, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.0 %	
Salary increases	3.5 %	Average, including inflation
Investment rate of return	7.7 %	Per year, compounded annually, including inflation

The same rates were applied to all periods. There were no changes to ad hoc postemployment benefits, including COLA.

Postretirement mortality rates were based on Client Specific Tables. Preretirement mortality rates are based on the RP-2000 tables.

The actuarial assumptions used in the June 30, 2015 valuation were based on the results of an actuarial experience study for the five-year period ended June 30, 2010. ERS updates their experience studies every five years.

Discount Rate - The discount rate used to measure the total pension liability was 7.65 percent. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that contributions from the ERS will be made at statutorily required rates, actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability. There has been no change in the discount rate since the prior measurement date.

Note 7 - Cost-sharing Defined Benefit Pension Plan (Continued)

Projected Cash Flows

Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

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

Asset Class	Target Allocation (%)	Long-term Expected Real Rate of Return
Domestic equity	30 %	8.5 %
International equity	26	9.3
Real estate	7	9.2
Total fixed income	20	3.1
Private equity	7	11.9
Real return	5	6.7
Other	5	7.7

Sensitivity of the Net Pension Liability to Changes in the Discount Rate - The following presents the net pension liability of the Corporation, calculated using the discount rate of 7.65 percent, as well as what the Corporation's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.65 percent) or 1 percentage point higher (8.65 percent) than the current rate:

	1% Decrease (6.65%)	Current Discount Rate (7.65%)	1% Increase (8.65%)
Net pension liability	$ 785,039,724	$ 623,325,235	$ 461,610,746

Note 7 - Cost-sharing Defined Benefit Pension Plan (Continued)

Pension Plan Fiduciary Net Position - Detailed information about the pension plan's fiduciary net position is available in a separately issued ERS financial report, which is available at http://www.ers.ehawaii.gov. The plan’s fiduciary net position is determined on the same basis used by the pension plan. The ERS financial statements are prepared using the accrual basis of accounting under which expenses are recorded when the liability is incurred and revenue is recorded in the accounting period in which it is earned and becomes measurable. Employer and member contributions are recognized in the period in which the contributions are due. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. Investment purchases and sales are recorded as of their trade date. Administrative expenses are financed exclusively with investment income.

Note 8 - Employee Benefits

Postemployment Health Care and Life Insurance Benefits - In addition to providing pension benefits, the State provides certain postretirement healthcare benefits (medical, prescription drug, vision, and dental) to all qualified employees and their dependents. Pursuant to Act 88 SLH of 2001, the State contributes to the Hawaii Employer-Union Health Benefits Trust Fund, an agent multiple-employer defined benefit plan. This plan is sponsored by and administered by the State of Hawaii.

For employees hired before July 1, 1996, the State pays the entire monthly healthcare premium for employees retiring with 10 or more years of credited service, and 50 percent of the monthly premium for employees retiring with fewer than 10 years of credited service. Retirees in this category can elect a family plan to cover dependents.

For employees hired after June 30, 1996 but before July 1, 2001, and who retire with less than 10 years of service, the State makes no contributions. For those retiring with at least 10 years but fewer than 15 years of service, the State pays 50 percent of the retired employees' monthly Medicare or non-Medicare premium. For those retiring with at least 15 years but fewer than 25 years of service, the State pays 75 percent of the base monthly contribution. For those employees retiring with at least 25 years of service, the State pays 100 percent of the base monthly contribution. Only single-plan coverage is provided for retirees in this category. Retirees in this category can elect a family plan to cover dependents.

Note 8 - Employee Benefits (Continued)

For employees hired on or after July 1, 2001, and who retire with less than 10 years of service, the State makes no contributions. For those retiring with at least 10 years but fewer than 15 years of service, the State pays 50 percent of the base monthly contribution. For those retiring with at least 15 years but fewer than 25 years of service, the State pays 75 percent of the base monthly contribution. For those employees retiring with at least 25 years of service, the State pays 100 percent 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 in plan costs.

Free life insurance coverage for retirees and free dental coverage for dependents under age 19 are also available. Retirees covered by the medical portion of Medicare are eligible to receive reimbursement of the basic medical coverage premium.

The State of Hawaii receives an annual actuarial valuation to compute the annual required contribution (ARC) necessary to fund the postretirement obligation for all state employees, including those employed by HHSC. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the current normal cost of benefits provided this year and to amortize any unfunded actuarial liabilities over a period not to exceed 30 years. Currently, the State contributes to the plan on a "pay-as-you-go" basis, only contributing the amounts necessary to pay for current year benefits.

For cost allocation purposes, the State allocates the full accrual ARC expense among its component units, including HHSC, based on respective percentages of full-time equivalents. The State requires HHSC to contribute to the plan at a rate of covered payroll necessary to fund its share of the annual "pay-as-you-go" contributions, which is significantly less than the actuarially determined contribution rate. HHSC then allocates its full accrual ARC expense among its various regions based on their respective percentages of full-time equivalents. The cumulative difference between the amounts the State requires HHSC to contribute and HHSC's allocation of the total plan ARC expense is recorded as other postretirement benefit liability on the balance sheet of each region. HHSC's actual cash contributions for postretirement benefits approximated $26.5 million and $29.3 million for the years ended June 30, 2016 and 2015, respectively.

Beginning of year	$ 338,248,725
Required contributions	57,589,884
Actual contributions	(26,524,579)
End of year	$ 369,314,030

Note 8 - Employee Benefits (Continued)

Sick Leave - Accumulated sick leave as of June 30, 2016 was approximately $81,454,000. Sick leave accumulates at the rate of 14 hours for each month of service, as defined, without limit. Sick pay can be taken only in the event of illness and is not convertible to pay upon termination of employment. Accordingly, no liability for sick pay is recorded in the accompanying financial statements.

Note 9 - Long-term Liabilities

Long-term liability activity for the year ended June 30, 2016 was as follows:

	2015	Current Year Additions	Current Year Reductions	2016	Amounts Due Within One Year
Long-term debt	$ 44,622,525	$ -	$ (4,733,120)	$ 39,889,405	$ 1,843,484
Capital lease obligations	$ 23,939,266	$ 2,199,447	$ (10,232,858)	$ 15,905,855	$ 6,629,441

The addition of Kona Ambulatory Surgery Center long-term debt of $1,961,172 is reflected in the beginning of year balances, due to the change in reporting entity being effective July 1, 2015.

The long-term debt obligations are summarized as follows:

Roselani Place - In September 2007, Alii exercised its option to purchase its 113-unit assisted-living and Alzheimer facility and personal property from the developer/landlord for $16 million. In connection with the purchase, Alii also assumed the land lease on which the facility is situated, and a parking license covering real property adjacent to the facility.

In connection with the purchase agreement, Alii also reached an agreement with the developer/landlord concerning an arbitration award that was rendered in favor of the developer/landlord in January 2006 for $1.9 million. The arbitration decision was on appeal to the Intermediate Court of Appeals of the State of Hawaii. Alii and the developer/landlord agreed to settle the $1.9 million judgment for $500,000. This settlement payment is in addition to the $16 million purchase price.

The note payable requires monthly payments of $126,433 including interest at 5.9 percent, through October 2027. The note is collateralized by certain property and equipment. At June 30, 2016, the balance payable was $12,538,134.

Note 9 - Long-term Liabilities (Continued)

Maui Bonds

In 2012, Maui Memorial Medical Center (MMMC) issued general obligation bonds. These bonds were executed in two parts, series 2012A and series 2012B. The series 2012A bonds were issued to refinance MMMC's existing $8 million loan which had been held with Bank of Montreal. Total borrowing under the first agreement was $8,100,000. These bonds carry an interest rate of 4.05 percent. The series 2012A bonds are secured by a loan note guarantee issued by the United States Department of Agriculture (USDA) through its Rural Development division. The series 2012B bonds provided initial funding for the purposes of construction of a physician clinic adjacent to the hospital, partially funding a building renovation, and equipment associated with imaging services. Total borrowing costs under the second agreement were $901,000. These bonds carry a variable interest rate that starts at 5 percent until September 1, 2017, at which point the rate shall reset on each September 1, occurring every five years thereafter at a rate equal to 3.75 percent over the prevailing five-year FHLB bulled rate (Seattle). In the event that such rate is no longer available or practicable, a similar index, as mutually agreed upon by the issuer and holders of the bonds, will be used. The series 2012B bonds are unsecured. The bonds are payable in annual installments ranging from $158,000 to $978,000. In connection with the series 2012A and series 2012B bond issuance, MMMC is subject to certain financial covenants. The total amount outstanding at June 30, 2016 on the series 2012A and 2012B revenue bonds is $8,565,000.

In January 2015, MMMC issued Revenue Bond Number 3, the proceeds of which were used to refinance the previously issued Series 2013 bonds. These bonds were issued under the existing master trust indenture dated April 1, 2008. Monthly payments are due in the amount of $46,433, including principal and interest, through January 2045 when all remaining principal and accrued interest are payable. Revenue Bond Number 3 carries an interest rate of 3.50 percent. In connection with Revenue Bond Number 3, MMMC is subject to certain financial covenants.

Hilo Residency Training Program - In June 2001, HHSC acquired land, building, and medical equipment of $11,893,162 from Hilo Residency Training Program, Inc. (HRTP) to ensure the uninterrupted operation of the Hilo Medical Center Cancer Treatment Center and its radiation and medical oncology services. As part of the acquisition, HHSC assumed HRTP's outstanding balances on the loans and notes payable of $11,893,162 from Central Pacific Bank and the United States Department of Agriculture (USDA). The assets and related liabilities have been recorded in the facility's accounting records. The loans and notes payable are collateralized by a security interest in the capital assets acquired from HRTP, as well as any rights, interest, and other tangible assets relating to such property. In October 2007, the loans and notes payable to Central Pacific Bank and the USDA were refinanced into a single note payable to Academic Capital.

Note 9 - Long-term Liabilities (Continued)

The note payable requires monthly payments, including interest, totaling $64,069 through September 2032. The note payable is secured by certain assets of Hilo Medical Center (HMC). At June 30, 2016, the balance payable was $8,023,621.

Yukio Okutsu Veterans' Home - In May 2008, the Yukio Okutsu Veterans' Home entered into a line of credit for $1.8 million, which calls for monthly interest-only payments at an interest rate of 5 percent. In November 2014, the Yukio Okutsu Veterans' Home signed an extension, which extended the balloon principal payment due from December 2015 to December 2016. The line of credit had a $0 balance at June 30, 2016.

KVMH's Port Allen Clinic - In April 2008, HHSC - Corporate entered into a promissory note with a bank to finance the leasehold improvements for KVMH's Port Allen Clinic. The note requires monthly principal and interest payments of $16,207 through maturity at November 23, 2017. The note is secured by a security interest in the leasehold improvements of the clinic. At June 30, 2016, the balance payable was $199,665.

Kahuku Medical Center - In July 2012, Kahuku Medical Center entered into a purchase and maintenance services agreement with Holden Hospital Supply, Inc. to finance the purchase and maintenance of an oxygen generator. The note requires monthly payments of $4,188 through maturity on June 30, 2019. The agreement also includes the financing of electrical and additional charges related to the oxygen generator. Interest is not a component of the agreement. At June 30, 2016, the balance of the loan was $96,335.

In April 2014, Kahuku Medical Center entered into a loan, secured by a mortgage, to finance the purchase of land. The agreement required monthly principal and interest payments of $12,481 through maturity at April 2019. At June 30, 2016, the balance of the loan was $413,656.

HHSC has entered into various capital leases, including a lease with Siemens for the financing of an electronic medical records system. The capital leases require monthly payments aggregating to approximately $750,000, including interest, per month. The capital leases expire at various times through 2027.

Note 9 - Long-term Liabilities (Continued)

The following is a schedule by year of principal and interest as of June 30, 2016:

Years Ending June 30	Long-term Debt Principal	Long-term Debt Interest	Capital Lease Obligation Principal	Capital Lease Obligation Interest
2017	$ 1,843,484	$ 1,909,874	$ 6,629,441	$ 461,973
2018	1,757,704	1,812,754	5,140,793	271,174
2019	1,781,290	2,020,037	1,427,616	163,295
2020	1,732,147	1,627,729	693,196	131,181
2021	1,826,468	1,530,441	421,037	106,197
2022-2026	10,788,850	6,010,342	1,426,971	257,268
2027-2031	7,980,975	3,270,890	166,801	3,353
2032-2036	4,507,851	1,848,745	-	-
Thereafter	7,670,636	1,250,712	-	-
Total payments	$ 39,889,405	$ 21,281,524	$ 15,905,855	$ 1,394,441

Note 10 - Commitments and Contingencies

Professional Liability - HHSC maintains professional and general liability insurance with a private insurance carrier with a $35 million limit per claim and a $39 million aggregate. HHSC has also purchased additional excess insurance with a $10 million per claim and aggregate limit. HHSC's general counsel advises that, in the unlikely event any judgments rendered against HHSC exceed HHSC's professional liability coverage, such amounts would likely be paid from an appropriation from the State's General Fund. Settled claims have not exceeded the coverage provided by the insurance carrier in any of the past three fiscal years.

Workers' Compensation Liability - HHSC is self-insured for workers' compensation claims. HHSC pays a portion of wages for injured workers (as required by law), medical bills, judgments as stipulated by the State's Department of Labor, and other costs. HHSC also directly provides treatment for injured workers. The estimated liability is based on actuarial projections of costs using historical claims-paid data. Estimates are continually monitored and reviewed and, as settlements are made or estimates adjusted, differences are reflected in current operations. HHSC has accrued a liability of $13,462,000 for unpaid claims as of June 30, 2016.

Estimated liability - Beginning of year	$ 13,779,000
Estimated claims incurred - Including changes in estimates	3,351,000
Claim payments	(3,668,000)
Estimated liability - End of year	$ 13,462,000

Note 10 - Commitments and Contingencies (Continued)

Operating Leases - HMC, MMMC, and Alii entered into various operating leases and related sublease agreements. Future minimum lease payments and sublease receipts at June 30, 2016 are as follows:

Years Ending June 30		Lease Payments	Sublease Receipts
2017		$ 1,912,135	$ 106,294
2018		1,169,499	-
2019		1,204,670	-
2020		1,240,802	-
2021		1,277,905	-
Thereafter		2,136,172	-
	Total	$ 8,941,183	$ 106,294

Ceded Lands - The Office of Hawaiian Affairs (OHA) and the State are presently in litigation involving the State's alleged failure to properly account for and pay to OHA monies due to OHA under the provisions of the Hawaii State Constitution and Chapter 10 of the Hawaii Revised Statutes for use by the State of certain ceded lands.

During the 2006 Legislative Session, the State of Hawaii Legislature enacted Act 178, which provided interim measures to ensure that a certain amount of proceeds was made available to OHA from the prorated portion of the public land trust for the betterment of the conditions of native Hawaiians. The act provided that the state agencies that collect receipts from the use of lands within the public land trust transfer a total of $3,775,000 to OHA within 30 days of the close of each fiscal quarter (or $15,100,000 per fiscal year), beginning with the 2006 fiscal year. In addition, the act appropriated $17,500,000 out of the State's general revenue to pay OHA for underpayments of the State's use of lands in the public land trust for the period from July 1, 2001 to June 30, 2005.

Note 10 - Commitments and Contingencies (Continued)

On September 20, 2006, the governor of the state of Hawaii issued Executive Order No. 06-06, which established procedures for the state agencies to follow in order to carry out the requirements of Act 178. Each state agency that collects receipts from the use of ceded or public land trust land is to determine OHA's share of such receipts by calculating the ceded/nonceded fraction of the parcel that generated the receipt, multiplying the receipt by the ceded/nonceded fraction, and multiplying that result by 20 percent. The resulting amounts are to be deposited into a trust holding account established for such purpose and within 10 days of the close of each fiscal quarter, the amounts are to be transferred to OHA. Within a specified period after the close of each quarter, the director of finance is to reconcile the actual amounts transferred to OHA with the required amount of $3,775,000 and adjust each specific agency's payments accordingly.

For the year ended June 30, 2016, there were no payments made to OHA.

Litigation - HHSC is a party to certain litigation arising in the normal course of business. In management's opinion, the outcome of such litigation will not have a material impact on HHSC's financial statements.

Supplemental Information

Hawaii Health Systems Corporation

Supplemental Schedule of Reconciliation of Cash on Deposit and Assets Limited as to Use with the State of Hawaii
June 30, 2016

	Appropriation Symbol		
Cash and cash equivalents - State of Hawaii			
Special funds:			
	S-14-303-H	$	540,582
	S-12-350-H		1
	S-12-351-H		1,273
	S-12-352-H		1
	S-12-353-H		72,947
	S-11-354-H		153,603
	S-10-355-H		111,744
	S-10-371-H		37,665
	S-10-358-H		2
	S-14-365-H		100,955
	S-14-312-H		69,721
	S-16-359-H		39,060
	S-16-373-H		3,013
Trust funds:			
	T-04-918-H		1,273
	T-04-921-H		6,682
Total per State		**$**	**1,138,522**
Assets limited as to use - Patient trust funds:			
	T-04-923-H	$	4,129
	T-04-919-H		1,044
	T-04-911-H		22,912
	T-09-909-H		9,334
	T-09-925-H		70,440
Total per State			107,859
Reconciling items:			
Patients' safekeeping deposits held by financial institutions			557,763
Restricted assets held by financial institutions			3,545,819
Total per HHSC		**$**	**4,211,441**

Hawaii Health Systems Corporation

Statement of Net Position of Facilities
June 30, 2016

	Facilities														
	Hilo Medical Center	Hale Ho'ola Hamakua	Ka'u Hospital	Yukio Okutsu Veterans Care Home - Hilo	Kona Community Hospital	Kohala Hospital	Maui Memorial Medical Center	Kula Hospital	Lanai Community Hospital	Leahi Hospital	Maluhia	Kahuku Medical Center	Kauai Veterans Memorial Hospital	Samuel Mahelona Memorial Hospital	Total Facilities
Assets															
Current Assets															
Cash and cash equivalents - State of Hawaii	$ 2	$ 2,546	$ 6,682	$ -	$ 153,603	$ 72,947	$ 111,744	$ 37,665	$ 2	$ 69,721	$ 100,955	$ -	$ 39,060	$ 3,013	$ 597,940
Cash and cash equivalents	13,388,565	44,189	14,880	518,128	12,910,415	3,518,305	36,872,484	8,313,051	57,124	1,507,966	2,967,925	562,675	6,548,847	3,220,170	90,444,724
Patient accounts receivable - Less allowances for doubtful accounts	22,145,537	1,709,450	717,022	1,260,611	10,237,453	1,000,534	28,034,953	3,920,428	453,464	1,462,257	1,404,326	2,456,078	2,183,624	1,711,999	78,697,736
Investments	7,362,814	-	-	-	-	-	-	-	-	-	-	-	-	-	7,362,814
Supplies and other current assets	3,995,047	231,487	135,562	10,467	2,361,230	59,245	6,164,498	258,443	127,678	123,163	1,273,243	591,545	493,408	110,989	15,936,005
Due from the State of Hawaii	22,187,406	-	-	-	7,082,342	703,240	19,642,000	3,249,000	2,282,000	8,170,000	5,095,000	1,626,000	3,875,037	6,407,848	80,319,873
Due from affiliates - Net	-	9,013,264	1,948,464	-	3,097,550	-	4,328,821	-	-	-	-	-	-	1,511,513	19,899,612
Estimated third-party payor settlements	5,133,635	252,508	27,916	9,792	2,781,968	257,227	5,308,626	262,092	64,429	1,857,872	1,197,605	472,500	1,443,508	564,942	19,634,620
Total current assets	74,213,006	11,253,444	2,850,526	1,798,998	38,624,561	5,611,498	100,463,126	16,040,679	2,984,697	13,190,979	12,039,054	5,708,798	14,583,484	13,530,474	312,893,324
Due from Affiliates - Net	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Capital Assets - Net	46,034,876	16,785,642	5,567,876	22,338,424	33,341,319	3,258,262	148,207,311	15,400,338	4,779,004	9,341,515	7,922,044	8,542,334	16,713,488	6,852,822	345,085,255
Assets Limited as to Use	490,015	13,878	3,399	-	292,224	-	2,101,486	62,079	3,216	92,410	57,710	3,037	10,395	15,678	3,145,527
Other Assets	300,451	-	-	-	477,434	-	282,937	3,435	-	-	-	-	-	-	1,064,257
Total assets	121,038,348	28,052,964	8,421,801	24,137,422	72,735,538	8,869,760	251,054,860	31,506,531	7,766,917	22,624,904	20,018,808	14,254,169	31,307,367	20,398,974	662,188,363
Deferred Outflows of Resources - Pension	20,734,366	1,659,308	1,065,791	-	8,477,083	1,037,148	27,536,974	3,530,646	538,245	3,572,966	2,958,904	-	5,653,098	2,261,221	79,025,750
Total assets and deferred outflows of resources	**$ 141,772,714**	**$ 29,712,272**	**$ 9,487,592**	**$ 24,137,422**	**$ 81,212,621**	**$ 9,906,908**	**$ 278,591,834**	**$ 35,037,177**	**$ 8,305,162**	**$ 26,197,870**	**$ 22,977,712**	**$ 14,254,169**	**$ 36,960,465**	**$ 22,660,195**	**$ 741,214,113**
Liabilities and Net Position															
Current Liabilities															
Current portion of long-term debt	$ 303,562	$ -	$ -	$ -	$ -	$ -	$ 366,652	$ -	$ -	$ -	$ -	$ 184,118	$ 184,528	$ -	$ 1,038,860
Current portion of capital lease obligations	1,685,427	-	-	-	101,269	-	1,271,632	-	-	-	126,118	518,082	260,941	-	3,963,469
Accounts payable and accrued expenses	26,576,740	978,517	824,073	618,595	8,830,601	515,506	29,874,101	1,831,835	1,215,901	1,604,243	1,502,914	1,000,948	4,366,710	1,347,108	81,087,792
Current portion of accrued workers' compensation liability	996,000	167,000	10,000	-	323,000	36,000	882,000	298,000	31,000	491,000	197,000	-	130,000	90,000	3,651,000
Current portion of accrued vacation	4,978,967	321,793	300,135	34,346	1,990,772	324,444	4,097,259	636,902	81,378	1,318,053	870,511	289,055	2,252,932	631,683	18,128,230
Estimated third party payor settlements	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Due from affiliates - Net	12,246,882	-	-	540,951	-	1,626,962	-	6,161,487	1,853,693	76,506	102,448	568,260	1,576,214	586,630	25,340,033
Other current liabilities	-	-	-	-	-	-	1,194,239	20,000	10,000	-	-	-	176,387	30,000	1,430,626
Total current liabilities	46,787,578	1,467,310	1,134,208	1,193,892	11,245,642	2,502,912	37,685,883	8,948,224	3,191,972	3,489,802	2,798,991	2,560,463	8,947,712	2,685,421	134,640,010
Long-term Debt - Less current portion	7,720,059	-	-	-	-	-	18,251,342	-	-	-	-	325,873	15,137	-	26,312,411
Capital Lease Obligations - Less current portion	2,342,395	-	-	-	378,596	-	3,838,821	-	-	-	65,904	-	112,134	-	6,737,850
Other Liabilities															
Accrued vacation - Less current portion	5,480,985	396,125	231,343	-	1,780,528	290,180	6,997,636	1,087,753	138,983	1,142,852	1,147,080	-	348,433	943,429	19,985,327
Accrued workers' compensation - Less current portion	2,610,000	171,000	136,000	-	1,220,000	111,000	3,414,000	524,000	52,000	141,000	316,000	-	629,000	194,000	9,518,000
Other postemployment benefit liability	95,564,159	7,653,366	5,194,499	-	37,427,152	4,987,331	129,485,898	15,187,742	2,733,206	14,543,510	12,304,898	-	23,485,681	9,279,613	357,847,055
Due to affiliates - Net	-	-	-	-	-	-	-	-	-	-	-	930,222	-	-	930,222
Due to the State of Hawaii - Less current portion	-	506,153	-	-	7,605,205	528,149	-	1,114,264	-	6,416,791	491,450	-	1,043,345	2,417,150	20,122,507
Pension liability	150,733,289	13,930,525	8,373,964	-	66,545,666	7,466,852	206,951,849	28,401,853	4,148,448	30,628,747	25,194,341	-	47,939,683	18,699,947	609,015,164
Patients' safekeeping deposits	30,767	13,878	3,399	-	-	-	-	62,079	3,216	83,076	31,294	3,037	6,644	14,634	252,024
Other liabilities	19,663	1,500	-	-	3,833	-	-	-	-	-	-	-	22,985	9,740	57,721
Total liabilities	311,288,895	24,139,857	15,073,413	1,193,892	126,206,622	15,886,424	406,625,429	55,325,915	10,267,825	56,445,778	42,349,958	3,819,595	82,550,754	34,243,934	1,185,418,291
Deferred Inflows of Resources - Pension	10,612,111	875,984	532,032	-	4,423,941	521,229	14,297,743	1,850,790	259,005	1,947,330	1,574,059	-	3,096,487	1,210,732	41,201,443
Total liabilities and deferred inflows of resources	321,901,006	25,015,841	15,605,445	1,193,892	130,630,563	16,407,653	420,923,172	57,176,705	10,526,830	58,393,108	43,924,017	3,819,595	85,647,241	35,454,666	1,226,619,734
Net Position															
Invested in capital assets - Net of related debt	33,983,433	16,785,642	5,567,876	22,338,424	32,861,454	3,258,262	132,185,843	15,400,338	4,779,004	9,341,515	7,730,022	7,514,261	16,140,748	6,852,822	314,739,644
Restricted for capital purchases	-	-	-	-	292,224	-	1,190,093	-	-	-	24,535	-	4,129	1,044	1,512,025
Unrestricted	(214,111,725)	(12,089,211)	(11,685,729)	605,106	(82,571,620)	(9,759,007)	(275,707,274)	(37,539,866)	(7,000,672)	(41,536,753)	(28,700,862)	2,920,313	(64,831,653)	(19,648,337)	(801,657,290)
Total net position	(180,128,292)	4,696,431	(6,117,853)	22,943,530	(49,417,942)	(6,500,745)	(142,331,338)	(22,139,528)	(2,221,668)	(32,195,238)	(20,946,305)	10,434,574	(48,686,776)	(12,794,471)	(485,405,621)
Total liabilities and net position	**$ 141,772,714**	**$ 29,712,272**	**$ 9,487,592**	**$ 24,137,422**	**$ 81,212,621**	**$ 9,906,908**	**$ 278,591,834**	**$ 35,037,177**	**$ 8,305,162**	**$ 26,197,870**	**$ 22,977,712**	**$ 14,254,169**	**$ 36,960,465**	**$ 22,660,195**	**$ 741,214,113**

	Corporate	Reclassifications and Eliminations	HHSC Combined	Hawaii Health Systems Foundation	Alii Community Care - Maui	Alii Community Care - Kona	Kona Ambulatory Surgery Center	Reclassifications and Eliminations	HHSC Consolidated
Assets									
Current Assets									
Cash and cash equivalents - State of Hawaii	$ 540,582	$ -	$ 1,138,522	$ -	$ -	$ -	$ -	$ -	$ 1,138,522
Cash and cash equivalents	11,011,646	-	101,456,370	40,037	66,376	81,457	50,319	-	101,694,559
Patient accounts receivable - Less allowances for							-		
doubtful accounts	-	-	78,697,736	-	22,466	235,421	285,362	-	79,240,985
Investments	-	-	7,362,814	-	-	-	-	-	7,362,814
Supplies and other current assets	24,565	-	15,960,570	-	27,105	56,899	171,084	-	16,215,658
Due from the State of Hawaii	359,000	-	80,678,873	-	-	-	-	-	80,678,873
Due from affiliates - Net	6,783,465	(26,270,255)	412,822	-	-	-	-	(412,822)	-
Estimated third-party payor settlements	-	-	19,634,620	-	-	-	-	-	19,634,620
Total current assets	18,719,258	(26,270,255)	305,342,327	40,037	115,947	373,777	506,765	(412,822)	305,966,031
Due from Affiliates - Net	-	-	-	-	-	-	-	-	-
Capital Assets - Net	1,544,315	-	346,629,570	-	9,300,920	105,853	2,517,354	-	358,553,697
Assets Limited as to Use	1,065,914	-	4,211,441	-	-	-	-	-	4,211,441
Other Assets	-	-	1,064,257	-	-	41,047	-	(465,434)	639,870
Total assets	21,329,487	(26,270,255)	657,247,595	40,037	9,416,867	520,677	3,024,119	(878,256)	669,371,039
Deferred Outflows of Resources - Pension	2,589,879	-	81,615,629	-	-	-	-	-	81,615,629
Total assets and deferred outflows of resources	**$ 23,919,366**	**$ (26,270,255)**	**$ 738,863,224**	**$ 40,037**	**$ 9,416,867**	**$ 520,677**	**$ 3,024,119**	**$ (878,256)**	**$ 750,986,668**
Liabilities and Net Position									
Current Liabilities									
Current portion of long-term debt	$ -	$ -	$ 1,038,860	$ -	$ 804,624	$ -	$ -	$ -	$ 1,843,484
Current portion of capital lease obligations	2,629,681	-	6,593,150	-	-	36,291	-	-	6,629,441
Accounts payable and accrued expenses	2,437,000	-	83,524,792	-	252,720	936,337	30,786	(412,822)	84,331,813
Current portion of accrued workers' compensation liability	-	-	3,651,000	-	-	-	-	-	3,651,000
Current portion of accrued vacation	627,469	-	18,755,699	-	-	-	-	-	18,755,699
Estimated third party payor settlements	-	-	-	-	-	-	-	-	-
Due from affiliates - Net	-	(25,340,033)	-	-	-	-	-	-	-
Other current liabilities	17,000	-	1,447,626	-	323,995	-	-	-	1,771,621
Total current liabilities	5,711,150	(25,340,033)	115,011,127	-	1,381,339	972,628	30,786	(412,822)	116,983,058
Long-term Debt - Less current portion	-	-	26,312,411	-	11,733,510	-	-	-	38,045,921
Capital Lease Obligations - Less current portion	2,518,153	-	9,256,003	-	-	20,411	-	-	9,276,414
Other Liabilities									
Accrued vacation - Less current portion	895,720	-	20,881,047	-	-	86,288	-	-	20,967,335
Accrued workers' compensation - Less current portion	293,000	-	9,811,000	-	-	-	-	-	9,811,000
Other postemployment benefit liability	11,466,975	-	369,314,030	-	-	-	-	-	369,314,030
Due to affiliates - Net	-	(930,222)	-	-	-	-	-	-	-
Due to the State of Hawaii - Less current portion	-	-	20,122,507	-	-	-	-	-	20,122,507
Pension liability	14,310,071	-	623,325,235	-	-	-	-	-	623,325,235
Patients' safekeeping deposits	-	-	252,024	-	-	-	-	-	252,024
Other liabilities	-	-	57,721	-	-	-	-	-	57,721
Total liabilities	35,195,069	(26,270,255)	1,194,343,105	-	13,114,849	1,079,327	30,786	(412,822)	1,208,155,245
Deferred Inflows of Resources - Pension	1,350,270	-	42,551,713	-	-	-	-	-	42,551,713
Total liabilities and deferred inflows of resources	36,545,339	(26,270,255)	1,236,894,818	-	13,114,849	1,079,327	30,786	(412,822)	1,250,706,958
Net Position									
Invested in capital assets - Net of related debt	976,067	-	315,715,711	-	(3,237,214)	49,151	2,517,354	(4,579,586)	310,465,416
Restricted for capital purchases	-	-	1,512,025	-	-	-	-	-	1,512,025
Unrestricted	(13,602,040)	-	(815,259,330)	40,037	(460,768)	(607,801)	475,979	4,114,152	(811,697,731)
Total net position	(12,625,973)	-	(498,031,594)	40,037	(3,697,982)	(558,650)	2,993,333	(465,434)	(499,720,290)
Total liabilities and net position	**$ 23,919,366**	**$ (26,270,255)**	**$ 738,863,224**	**$ 40,037**	**$ 9,416,867**	**$ 520,677**	**$ 3,024,119**	**$ (878,256)**	**$ 750,986,668**

Hawaii Health Systems Corporation

Statement of Revenue, Expenses, and Changes in Net Position of Facilities
Year Ended June 30, 2016

	Facilities										
	Hilo Medical Center	Hale Ho'ola Hamakua	Ka'u Hospital	Yukio Okutsu Veterans Care Home - Hilo	Kona Community Hospital	Kohala Hospital	Maui Memorial Medical Center	Kula Hospital	Lanai Community Hospital	Leahi Hospital	Maluhia
Operating Revenue											
Net patient service revenue - Net of provision for doubtful accounts	$ 165,375,558	$ 14,726,403	$ 8,009,049	$ 12,415,966	$ 73,813,426	$ 7,521,300	$ 230,992,734	$ 21,004,700	$ 3,043,760	$ 14,831,013	$ 14,518,759
Other revenue	2,799,383	134,069	19,308	-	784,179	6,036	1,959,746	73,283	9,161	215,990	20,617
Total operating revenue	168,174,941	14,860,472	8,028,357	12,415,966	74,597,605	7,527,336	232,952,480	21,077,983	3,052,921	15,047,003	14,539,376
Operating Expenses											
Salaries	75,406,264	6,716,991	4,488,022	4,918,299	30,852,003	4,177,004	101,989,308	12,039,741	2,405,385	11,488,752	11,023,297
Employee benefits	46,618,467	3,704,961	2,789,221	426,304	16,296,870	2,534,969	56,855,193	7,115,457	1,659,170	5,342,881	4,876,683
Purchased services	24,869,073	2,280,463	1,027,266	1,547,825	16,997,818	1,451,820	34,597,441	2,507,354	1,398,410	378,151	539,541
Medical supplies and drugs	23,209,355	765,173	202,540	540,126	7,431,580	32,405	42,417,539	774,195	328,690	426,134	278,977
Depreciation and amortization	6,956,583	925,601	709,570	746,578	5,403,412	335,706	16,403,378	1,860,095	306,242	563,595	472,316
Utilities	2,665,946	560,255	237,592	931,644	1,399,997	156,217	4,247,298	268,566	150,891	855,713	590,305
Repairs and maintenance	3,796,307	531,571	227,192	124,033	3,073,673	208,936	4,859,597	75,424	125,381	408,153	363,551
Other supplies	3,928,299	573,053	246,176	543,857	1,197,204	355,541	5,059,006	789,822	182,258	600,691	780,821
Professional fees	8,620,744	246,805	34,344	93,812	224,774	199,733	2,158,417	154,466	18,476	69,416	30,577
Insurance	760,483	65,235	115,132	1,203,565	232,293	19,283	1,929,297	105,181	15,581	134,175	96,157
Rent and lease	2,428,708	47,466	40,470	89,033	619,558	82,525	2,934,378	98,881	10,207	20,923	924
Other	1,899,866	127,177	147,291	744,500	625,652	86,550	1,746,470	109,542	108,025	42,337	64,644
Total operating expenses	201,160,095	16,544,751	10,264,816	11,909,576	84,354,834	9,640,689	275,197,322	25,898,724	6,708,716	20,330,921	19,117,793
Operating (Loss) Income	(32,985,154)	(1,684,279)	(2,236,459)	506,390	(9,757,229)	(2,113,353)	(42,244,842)	(4,820,741)	(3,655,795)	(5,283,918)	(4,578,417)
Nonoperating Revenue (Expenses)											
General appropriations from the State of Hawaii	26,214,000	2,393,000	1,776,000	-	14,012,000	1,257,000	31,287,000	4,051,000	1,458,000	7,960,000	4,194,000
Collective bargaining pay raise appropriations	489,040	24,347	22,290	-	209,705	17,624	612,071	40,291	14,571	56,108	37,479
Loss on disposal of capital assets	(12,664)	-	-	-	(6,486)	-	(77)	-	-	-	-
Restricted contributions	330,704	-	47,918	-	350,500	45,783	1,874,820	-	-	-	-
Interest expense	(482,617)	-	(26)	(29,379)	(109,958)	(3,373)	(1,124,889)	(4,566)	(37)	(2,942)	(250)
Interest and dividend income	88,306	7,556	4,862	-	29,465	13,552	136,868	30,842	2,399	8,462	7,540
Corporate allocation expense	(3,142,535)	(256,890)	(148,236)	-	(2,191,178)	(244,603)	(7,016,943)	(664,583)	(164,265)	(582,551)	(532,046)
Other nonoperating revenue (expenses) - Net	1,046,239	228,317	(5,244)	2,121	(2,275,799)	(15,299)	719,879	157,208	36,557	49,951	-
Total nonoperating revenue (expenses)	24,530,473	2,396,330	1,697,564	(27,258)	10,018,249	1,070,684	26,488,729	3,610,192	1,347,225	7,489,028	3,706,723
Excess of Revenue (Under) Over Expenses	(8,454,681)	712,051	(538,895)	479,132	261,020	(1,042,669)	(15,756,113)	(1,210,549)	(2,308,570)	2,205,110	(871,694)
Capital Contributions	2,342,537	-	(4,000)	-	6,376,775	188,781	6,677,638	(631,759)	(29,185)	976,116	193,880
Change in Reporting Entity	-	-	-	-	-	-	-	-	-	-	-
Asset Impairment	-	-	-	-	-	-	-	-	-	(1,288,820)	(1,138,683)
Transfer from (to) Affiliate	72,899,516	1,842,918	8,336,416	-	41,776,586	9,034,504	(14,211,256)	22,807,386	15,266,517	17,913,732	28,411,825
Increase (Decrease) in Net Position	**$ 66,787,372**	**$ 2,554,969**	**$ 7,793,521**	**$ 479,132**	**$ 48,414,381**	**$ 8,180,616**	**$ (23,289,731)**	**$ 20,965,078**	**$ 12,928,762**	**$ 19,806,138**	**$ 26,595,328**

	Facilities												
	Kahuku Medical Center	Kauai Veterans Memorial Hospital	Samuel Mahelona Memorial Hospital	Total Facilities	Corporate	Reclassifications and Eliminations	HHSC Combined	Hawaii Health Systems Foundation	Alii Community Care - Maui	Alii Community Care - Kona	Kona Ambulatory Surgery Center	Reclassifications and Eliminations	HHSC Consolidated
Operating Revenue													
Net patient service revenue - Net of provision for doubtful accounts	$ 12,872,261	$ 31,805,583	$ 15,746,321	$ 626,676,833	$ -	$ -	$ 626,676,833	$ -	$ -	$ 3,286,288	$ 1,415,701	$ -	$ 631,378,822
Other revenue	555,372	271,956	17,590	6,866,690	-	(474,587)	6,392,103	-	3,870,907	1,241,850	-	-	11,504,860
Total operating revenue	13,427,633	32,077,539	15,763,911	633,543,523	-	(474,587)	633,068,936	-	3,870,907	4,528,138	1,415,701	-	642,883,682
Operating Expenses													
Salaries	5,418,064	18,845,010	8,126,147	297,894,287	8,501,808	-	306,396,095	-	-	3,755,830	716,316	-	310,868,241
Employee benefits	2,049,198	6,612,623	3,452,267	160,334,264	4,597,646	-	164,931,910	-	-	1,535,464	13,632	-	166,481,006
Purchased services	1,471,975	4,524,858	1,790,295	95,382,290	2,694,697	(474,587)	97,602,400	-	43,636	72,708	-	-	97,718,744
Medical supplies and drugs	1,122,691	2,353,752	331,500	80,214,657	-	-	80,214,657	-	-	316,746	384,998	-	80,916,401
Depreciation and amortization	1,056,583	2,508,235	949,927	39,197,821	524,241	-	39,722,062	-	891,002	47,775	274,233	-	40,935,072
Utilities	402,584	817,911	438,430	13,723,349	309,100	-	14,032,449	-	365,501	23	-	-	14,397,973
Repairs and maintenance	661,979	661,494	246,968	15,364,259	(21,665)	-	15,342,594	-	60,166	133,565	465,215	-	16,001,540
Other supplies	448,049	1,154,505	494,440	16,353,722	59,888	-	16,413,610	-	393,781	23,276	-	-	16,830,667
Professional fees	1,127,890	648,650	395,810	14,023,914	252,176	-	14,276,090	-	2,482,139	(470,982)	533,134	-	16,820,381
Insurance	76,602	325,231	51,395	5,129,610	16,440	-	5,146,050	-	95,656	62,442	-	-	5,304,148
Rent and lease	174,865	248,716	56,065	6,852,719	218,115	-	7,070,834	-	157,528	623,166	-	-	7,851,528
Other	707,540	353,105	167,750	6,930,449	399,856	-	7,330,305	198	173,383	649,121	-	-	8,153,007
Total operating expenses	14,718,020	39,054,090	16,500,994	751,401,341	17,552,302	(474,587)	768,479,056	198	4,662,792	6,749,134	2,387,528	-	782,278,708
Operating (Loss) Income	(1,290,387)	(6,976,551)	(737,083)	(117,857,818)	(17,552,302)	-	(135,410,120)	(198)	(791,885)	(2,220,996)	(971,827)	-	(139,395,026)
Nonoperating Revenue (Expenses)													
General appropriations from the State of Hawaii	1,500,000	8,395,000	2,943,000	107,440,000	14,000,000	-	121,440,000	-	-	-	-	-	121,440,000
Collective bargaining pay raise appropriations	-	152,732	38,381	1,714,639	17,303	-	1,731,942	-	-	-	-	-	1,731,942
Loss on disposal of capital assets	8,925	-	-	(10,302)	-	-	(10,302)	-	-	-	-	-	(10,302)
Restricted contributions	-	-	-	2,649,725	-	-	2,649,725	-	-	30,000	-	-	2,679,725
Interest expense	(82,257)	(59,758)	-	(1,900,052)	(684,069)	-	(2,584,121)	-	(763,634)	(3,875)	-	-	(3,351,630)
Interest and dividend income	-	17,948	21,953	369,753	15,816	-	385,569	-	612	-	-	-	386,181
Corporate allocation expense	-	(1,086,171)	(440,998)	(16,470,999)	16,470,999	-	-	-	-	-	-	-	-
Other nonoperating revenue (expenses) - Net	-	558,782	248,219	750,931	20,267	-	771,198	-	-	1,988,317	-	574,594	3,334,109
Total nonoperating revenue (expenses)	1,426,668	7,978,533	2,810,555	94,543,695	29,840,316	-	124,384,011	-	(763,022)	2,014,442	-	574,594	126,210,025
Excess of Revenue (Under) Over Expenses	136,281	1,001,982	2,073,472	(23,314,123)	12,288,014	-	(11,026,109)	(198)	(1,554,907)	(206,554)	(971,827)	574,594	(13,185,001)
Capital Contributions	-	3,456,965	3,531,851	23,079,599	(251)	-	23,079,348	-	-	-	2,355,547	(394,375)	25,040,520
Change in Reporting Entity	-	-	-	-	-	-	-	-	-	-	1,609,613	(645,653)	963,960
Asset Impairment	(1,094,379)	-	-	(3,521,882)	-	-	(3,521,882)	-	-	-	-	-	(3,521,882)
Transfer from (to) Affiliate	-	60,499,723	13,215,806	277,793,673	(297,386,998)	-	(19,593,325)	-	19,593,325	-	-	-	-
Increase (Decrease) in Net Position	**$ (958,098)**	**$ 64,958,670**	**$ 18,821,129**	**$ 274,037,267**	**$ (285,099,235)**	**$ -**	**$ (11,061,968)**	**$ (198)**	**$ 18,038,418**	**$ (206,554)**	**$ 2,993,333**	**$ (465,434)**	**$ 9,297,597**

Required Supplemental Information

Required Supplemental Information
Schedule of Contributions
Employees' Retirement System of the State of Hawaii
Year Ended June 30

	2016	2015	2014
Contractually required contribution	$ 51,584,604	$ 49,213,969	$ 53,279,576
Contributions in relation to the contractually required contribution	51,584,604	50,272,620	47,500,308
Contribution (Excess) Deficiency	**$ -**	**$ (1,058,651)**	**$ 5,779,268**
Corporation's Covered Employee Payroll	$ 288,121,862	$ 285,988,382	$ 268,597,949
Contributions as a Percentage of Covered Employee Payroll	17.9 %	17.6 %	17.7 %

Required Supplemental Information
Schedule of the Proportionate Share of the Net Pension Liability
Employees' Retirement System of the State of Hawaii
Year Ended June 30

	2016	2015	2014
Corporation's proportion of the net pension liability (asset)	7.1 %	7.3 %	7.2 %
Corporation's proportionate share of the net pension liability (asset)	$ 623,325,233	$ 583,997,239	$ 638,368,793
Corporation's covered employee payroll	288,121,862	285,988,382	268,597,949
Corporation's Proportionate Share of the Net Pension Liability (Asset) as a Percentage of its Covered Employee Payroll	216.3 %	204.2 %	237.7 %
Plan Fiduciary Net Position as a Percent of Total Pension Liability	62.4	63.9	58.0

Note to Pension Required Supplemental Information Schedules
Year Ended June 30

The comparability of trend information is affected by changes in actuarial assumptions, benefit provisions, actuarial funding methods, accounting policies, and other changes. Those changes usually affect trends in contribution requirements and in ratios that use the pension and other postemployment benefit obligations as a factor.

The schedule of contributions is presented to show the responsibility of the Corporation in meeting the actuarial requirements to maintain the system on a sound financial basis.

The schedule of the proportionate share of the net pension liability and schedule of contributions are schedules that are required in implementing GASB Statement No. 68. The schedule of the proportionate share of the net pension liability represents, in actuarial terms, the accrued liability less the market value of assets. The schedule of contributions is a comparison of the Corporation's contributions to the actuarially determined contributions.

The information presented in the schedule of contributions was used in the actuarial valuation for purposes of determining the actuarially determined contribution rate. Additional information as of the latest actuarial valuation for the pension plan follows.

Valuation methods and assumptions used to determine contribution for fiscal year 2015:

Actuarial cost method	Entry age, normal
Amortization method	Level percent, closed
Remaining amortization period	28 years
Asset valuation method	Market
Inflation	3.0 percent
Salary increases	3.5 percent wage inflation
Investment rate of return	7.0 percent per year, compounded annually including inflation

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

Independent Auditor's Report

To Management and the Board of Directors
Hawaii Health Systems Corporation

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Hawaii Health Systems Corporation (HHSC or the "Corporation"), which comprise the basic statement of net position as of June 30, 2016 and the related basic statements of revenue, expenses, and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 28, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Hawaii Health Systems Corporation'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 HHSC's internal control. Accordingly, we do not express an opinion on the effectiveness of HHSC's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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 were not identified. However, as described in the accompanying schedule of findings, we identified certain deficiencies in internal control that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

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. We consider the deficiencies described in the accompanying schedule of findings as Findings 2016-1 and 2016-2 to be material weaknesses.

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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. We consider the deficiencies described in the accompanying schedule of findings as Findings 2016-3 through 2016-8 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Hawaii Health Systems Corporation'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*.

Hawaii Health Systems Corporation's Responses to Findings

Hawaii Health Systems Corporation's responses to the findings identified in our audit are described in the accompanying schedule of findings. Hawaii Health Systems Corporation's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

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 HHSC's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering HHSC's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Plante & Moran, PLLC

Grand Rapids, Michigan
December 28, 2016

Finding - 2016-1

Organization - Alii Community Care, Inc.

Finding Type - Material weakness

Criteria - Property and equipment lapse schedules for Roselani should be reviewed by a second individual to ensure proper depreciation calculations are being prepared. Reconciliation of the detailed lapse schedule to the general ledger is essential to ensure amounts presented in the financial statements are accurate.

Condition - A property and equipment lapse schedule is not being updated properly at Roselani. Also, depreciation expense had not been recorded correctly in fiscal year 2016.

Context - Property and equipment amounts recorded in the general ledger did not have adequate supporting documentation.

Cause - An adjustment to depreciation expense of $15,128 needed to be recorded in fiscal year 2016.

Effect - The statement of net position and statement of operations were misstated throughout the year. An adjusting journal entry was posted to correct this misstatement.

Recommendation - We recommend management at Roselani perform formal review of property and equipment accounts to ensure what is being reported is properly supported by lapse schedules or other detailed records. Additionally, management should document their review of a reconciliation between the detailed lapse schedule and the general ledger to ensure all asset activity is captured properly.

Views of Responsible Officials and Planned Corrective Action Plan - The ACC Board Management Liaison will work directly with the Roselani accountant to review property and equipment accounts to ensure what is being reported is properly supported by lapse schedules or other detailed reports. This review process will occur monthly and will include proper documentation of reconciliation activity between the lapse schedules and the general ledger to ensure accurate capturing of asset activity.

Finding - 2016-2

Organization - Alii Community Care, Inc.

Finding Type - Material weakness

Criteria - Financial statements should be reported on an accrual basis throughout the year at Alii - Kona.

Condition - Alii Community Care, Inc. reported financial results on a cash basis throughout 2016.

Context - Generally accepted accounting principles require the accrual basis of accounting.

Cause - Decision by management to report financial results on cash basis

Effect - The statement of operations was misstated throughout the year. Adjusting journal entries were posted to correct this misstatement.

Recommendation - We recommend that management review the decision to report financial results in accordance with generally accepted accounting principles on an interim basis.

Views of Responsible Officials and Planned Corrective Action Plan - The ACC Board will review and evaluate Alii Health Center's cash accounting methodology based on concerns raised by Plante & Moran, PLLC.

Finding - 2016-3

Organization - East Hawaii Region

Finding Type - Significant deficiency

Criteria - Account balances should be reconciled monthly and reviewed in a timely manner to ensure the balance in the general ledger is accurate.

Condition - Ka'u account balances were not appropriately stated on the trial balance received.

Context - The accounts payable, accounts receivable and related allowances, fixed assets, and cash balances had to be adjusted during the audit as a result of balances not being appropriately reconciled at June 30, 2016. These adjustments resulted in decreased expenses of approximately $374,000, increased assets of $138,000, and decreased liabilities of $236,000.

Cause - Appropriate review and monitoring at Ka'u was not fully in place at year end.

Effect - Multiple account adjustments were identified as a result of audit procedures.

Recommendation - We recommend the East Hawaii Region put appropriate review controls in place to ensure balances are appropriately stated at the end of each period.

Views of Responsible Officials and Planned Corrective Action Plan - Management has corrected the account balances and put procedures in place to properly review Ka'u account balances.

Finding - 2016-4

Organization - East Hawaii Region

Finding Type - Significant deficiency

Criteria - Accounts payable should be reviewed at year end and subsequent to year end to ensure all liabilities and expenses related to the year are appropriately recorded.

Condition - Accounts payable was not appropriately reviewed for cut-off at year end.

Context - Multiple items were improperly excluded from accounts payable at year end or were improperly duplicated in the accrual process.

Cause - Accounts payable was not appropriately reviewed throughout the year-end close process.

Effect - Accounts payable and related expense amounts were understated by approximately $150,000 at year end.

Recommendation - We recommend the East Hawaii Region closely monitor all invoices received at and subsequent to year end to ensure the appropriate liabilities and related expenses are recorded.

Views of Responsible Officials and Planned Corrective Action Plan - Management has corrected the error and put procedures in place to properly review accounts payable cutoff in the future.

Finding - 2016-5

Organization - Kahuku Medical Center

Finding Type - Significant deficiency

Criteria - Account balances should be reconciled and reviewed periodically to ensure the balance in the general ledger is accurate.

Condition - Account balances were not appropriately stated on the trial balance received.

Context - Lack of review led to multiple balances not being appropriately trued up at year end. Adjustments were made to following balances:

1) Unapplied cash balance
2) Depreciation expense
3) Expense classification for an invoice selected for testing as part of the A/P cycle
4) IBNR accrual for self-insurance claims

These adjustments resulted in increased expenses and decreased assets of approximately $205,000, in addition to a passed adjustment.

Cause - Appropriate review and monitoring was not fully in place at year end.

Effect - Multiple account adjustments were identified as a result of audit procedures.

Recommendation - We recommend that Kahuku Medical Center put appropriate review controls in place to ensure balances are appropriately stated at the end of each period.

Views of Responsible Officials and Planned Corrective Action Plan - Considering the mid-year transition of CFOs, existing and new personnel have dedicated abundant time and resources streamlining practices to improve the efficiency and effectiveness of the accounting function for KMC. As a result of the executed plan, management has corrected the account balances.

Finding - 2016-6

Organization - Maui Region

Finding Type - Significant deficiency

Criteria - Policies and procedures should be maintained to ensure all significant balance sheet accounts are reconciled monthly on a timely basis.

Condition - The patient accounts receivable account for MMMC was not reconciled in a timely manner for interim periods through the fiscal year.

Context - Gross accounts receivable and revenue was understated by approximately $900,000 as of April 30, 2016; the estimated net impact to accounts receivable and net patient service revenue was approximately $341,000.

Cause - Due to staff turnover, the completion and review of the reconciliation for the MMMC main patient accounts receivable account was not prepared and reviewed in a timely manner.

Effect - As a result of this deficiency, gross accounts receivable and revenue was understated as of April 30, 2016.

Recommendation - We recommend that all balance sheet accounts be reconciled monthly in a timely manner.

Views of Responsible Officials and Planned Corrective Action Plan - Management has corrected the issue.

Finding - 2016-7

Organization - Maui Region

Finding Type - Significant deficiency

Criteria - Policies and procedures should be maintained to ensure regular reviews of capital assets are performed so that all completed asset purchases are placed into service and depreciated on a timely basis.

Condition - Three assets at Kula which began being used in previous fiscal years were not placed into service as of June 30, 2016.

Context - Capital assets was overstated and depreciation expense understated by approximately $166,000 as of June 30, 2016.

Cause - Reviews of CIP were not performed throughout the year to ensure all assets were placed into service timely.

Effect - As a result of this deficiency, the capital asset and depreciation expense account balances were misstated as of June 30, 2016.

Recommendation - We recommend that regular reviews of CIP be performed to ensure all assets are placed into service timely.

Views of Responsible Officials and Planned Corrective Action Plan - Management has corrected the issue.

Finding - 2016-8

Organization - East Hawaii Region, Kahuku Medical Center, Kauai Region, Oahu Region, and West Hawaii Region

Finding Type - Significant deficiency

Criteria - Bank account signature authorities should be limited to current management members.

Condition - Former employees were still listed with signature authority on bank accounts held by the East Hawaii Region, Kahuku Medical Center, Kauai Region, Oahu Region, and West Hawaii Region.

Context - We identified that inappropriate signatory authorities existed on bank signature cards.

Cause - Lack of timely removal of signatory authorities on bank accounts

Effect - No financial statement effect was identified; however, internal controls are considered to be negatively impacted.

Recommendation - We recommend that management request that former employees be removed timely from bank accounts upon termination.

Views of Responsible Officials and Planned Corrective Action Plan - Management is actively correcting this issue and will regularly review listed signatory authorities for necessity of access to cash.