

PALMETTO RAILWAYS
FINANCIAL STATEMENTS
YEAR ENDED DECEMBER 31, 2016



**South Carolina
Office of the State Auditor**

**George L. Kennedy, III, CPA
State Auditor**

April 12, 2017

The Honorable Henry McMaster, Governor
and
Mr. Robert M. Hitt III, Secretary of Commerce
South Carolina Department of Commerce
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina Department of Commerce – Division of Public Railways d/b/a Palmetto Railways, for the fiscal year ended December 31, 2016, was issued by Greene, Finney & Horton, LLP, Certified Public Accountants, under contract with the South Carolina Office of the State Auditor.

If you have any questions regarding this report, please let us know.

Respectfully submitted,

A handwritten signature in blue ink that reads "George L. Kennedy, III".

George L. Kennedy, III, CPA
State Auditor

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PALMETTO RAILWAYS
TABLE OF CONTENTS
YEAR ENDED DECEMBER 31, 2016

	<u>PAGE</u>
INDEPENDENT AUDITOR'S REPORT.....	1
MANAGEMENT'S DISCUSSION AND ANALYSIS	3
<u>BASIC FINANCIAL STATEMENTS</u>	
Statement of Net Position-Enterprise Funds.....	10
Statement of Revenues, Expenses, and Changes in Fund Net Position-Enterprise Funds.....	11
Statement of Cash Flows-Enterprise Funds	13
Notes to Financial Statements.....	15
<u>REQUIRED SUPPLEMENTARY INFORMATION – PENSION SCHEDULES</u>	
Schedule of Palmetto Railways' Proportionate Share of the Net Pension Liability – South Carolina Retirement System.....	47
Schedule of Palmetto Railways' Contributions – South Carolina Retirement System.....	48
Schedule of Palmetto Railways' Proportionate Share of the Net Pension Liability – Police Officers Retirement System.....	49
Schedule of Palmetto Railways' Contributions – Police Officers Retirement System.....	50
Independent Auditor's Report – 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	51



INDEPENDENT AUDITOR'S REPORT

Mr. George L. Kennedy, CPA
State Auditor
Office of the State Auditor
Columbia, South Carolina

Report on the Financial Statements

We have audited the accompanying financial statements of the South Carolina Department of Commerce – Division of Public Railways d/b/a Palmetto Railways (the “Division”) as of and for the year ended December 31, 2016, and the related notes to the financial statements, as listed in the table of contents.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Division as of December 31, 2016, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Division and do not purport to, and do not present fairly the financial position of the State of South Carolina or the South Carolina Department of Commerce as of December 31, 2016, the changes in their financial position, or, where applicable, their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and pension schedules, as listed 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 GASB who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated April 12, 2017 on our consideration of the Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.



Greene, Finney & Horton, LLP
Mauldin, South Carolina
April 12, 2017

Management's Discussion and Analysis

Our discussion and analysis of South Carolina Department of Commerce – Division of Public Railways d/b/a Palmetto Railways (the “Division”) financial performance provides an overview of the financial activities for the fiscal year ended December 31, 2016. Please read these comments in conjunction with the financial statements.

Using This Annual Report

This annual report consists of a series of financial statements. The *Statement of Net Position*; the *Statement of Revenues, Expenses and Changes in Fund Net Position*; and *Statement of Cash Flows* provide information regarding the activities of the Division’s three operating subdivisions, a fund holding contributed land and land improvements, and as a whole.

The three operating subdivisions of the Division are:

- Charleston Subdivision (CHS)
- North Charleston Subdivision (NCS)
- Charity Church Subdivision (CCS)

All the subdivisions and the fund holding contributed land and land improvements (the “Economic Development Project Fund”) are enterprise fund activities, and all are reported on the accrual basis. CHS and NCS are combined in the financial statements.

These statements provide information on the Division’s net position, operations, and cash flows for the year ended December 31, 2016. This discussion and analysis is intended to serve as an introduction to the financial statements. The notes to the financial statements also contain details on some of the information presented in the financial statements.

Reporting on the Division as a whole

The subdivisions are enterprise funds for accounting and reporting purposes. Enterprise funds are used when governmental entities charge customers for services. Enterprise funds very closely resemble the financial statements of business entities. These statements offer short and long-term financial information about the Division’s activities. The Statement of Net Position presents information on all of the Division’s assets, liabilities, and net position. Net position represents assets and deferred outflows of resources less liabilities and deferred inflows of resources.

Over time, increases and decreases in net position, specifically unrestricted net position, may serve as a useful indicator of whether the financial position of the Division is improving or deteriorating. The Statement of Revenues, Expenses and Changes in Fund Net Position presents information showing how the Division’s net position changed during the fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are recorded in this statement for some items that will only result in cash flows in future fiscal periods.

Management Discussion and Analysis (Continued)

Financial Highlights

- Operating revenues increased in 2016 by \$2,474,291 or 17.6% due primarily to additional switching revenue related to the operations of Cosgrove Yard at NCS in late 2015 as well as starting a new rail car repair department that generates revenue.
- Capital contributions were \$18,936,802 in 2016 down from \$39,408,288 in the prior year. In 2016 land improvements and site development of the land contributed by South Carolina Department of Commerce continued for the Economic Development Project Fund.
- Gain on investments increased in 2016 by \$48,826 or 146.9% primarily due to a increase in state investment income during 2016.
- Other non-operating revenue increased \$112,686 or 8.5% due to an increase in rental income on the former Navy Base as well as an increase in other income which represents reimbursable grant revenue.
- Maintenance of way expenses remained relatively stable, with an increase of \$8,812 or 0.6%.
- Maintenance of equipment expenses increased \$391,130 or 29.5% due primarily to additional locomotive repairs and improvements required in 2016 as well as an additional mechanic on staff in 2016.
- Rail car repair expenses increased by \$826,570 or 100.0% due to the department starting operations in August of 2016.
- Transportation expenses increased \$1,108,147 or 25.4% due primarily to additional personnel and other expenses associated with operating Cosgrove Yard for a full calendar year.
- General expenses increased \$1,033,434 or 24.2% primarily due additional administration employees, professional fees related to the Intermodal Container Transfer Facility, Camp Hall, and company website improvements. Other increases included facilities management expenses and appraisals associated with a future loan application.
- Current assets increased \$4,450,803 or 52.4% due to an increase in cash and investments being held for future Intermodal Container Transfer Facility expenses as well as an increase in operating cash, which resulted from Cosgrove Yard revenues.
- Capital assets increased by \$46,679,309 or 22.6% due to the land improvements through capital contributions noted above, further development of the Intermodal Container Transfer Facility, and track repairs at Cosgrove Yard.
- Deferred outflows of resources increased \$1,911,516 or 191.5% due to the increase in deferred pension charges associated with Governmental Accounting Standards Board (“GASB”) Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No.27* (“GASB #68”) and GASB Statement No. 71, *Pension Transitions for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68* (“GASB #71” and collectively “Statements”).
- Current liabilities increased \$36,501,266 or 642.3% primarily due to an interest-free note payable to the South Carolina Department of Commerce – SC Coordinating Council for Economic Development coming due within one year, partially offset by the \$2,000,000 settlement payable to City of North Charleston being paid in 2016.

Management Discussion and Analysis (Continued)

Financial Highlights (Continued)

- Other liabilities decreased \$5,310,000 or 25.8% primarily due to the short-term note payable referenced above, as well as the an increase in the net pension liability of \$2,865,000.
- Deferred inflows of resources decreased \$1,659 or 13.7% due to the increase in deferred pension charges associated with Governmental Accounting Standards Board (“GASB”) Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No.27* (“GASB #68”) and GASB Statement No. 71, *Pension Transitions for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68* (“GASB #71” and collectively “Statements”).
- Net position increased by \$21,852,021 or 11.5% from the prior year net position. Net investment in capital assets increased \$23,485,260 or 12.4%, and unrestricted net position decreased \$1,633,239 or 356.3% from the prior year unrestricted net position.

Financial Analysis

The following are the condensed financial statements of the Division for fiscal years 2016 and 2015, including information concerning the events and circumstances regarding the balances and changes:

Condensed Statement of Net Position

	2016	2015	Amount Change	% Change
Current and other assets, net	\$ 12,950,401	\$ 8,499,598	\$ 4,450,803	52.4%
Capital assets, net of depreciation	253,011,381	206,332,072	46,679,309	22.6%
Total Assets	265,961,782	214,831,670	51,130,112	23.8%
Deferred pension charges	2,909,727	998,211	1,911,516	191.5%
Total Deferred Outflows of Resources	2,909,727	998,211	1,911,516	191.5%
Total Assets & Deferred Outflows of Resources	\$ 268,871,509	\$ 215,829,881	\$ 53,041,628	24.6%
Current liabilities	\$ 42,184,069	\$ 5,682,803	\$ 36,501,266	642.3%
Net pension liability	9,719,261	6,854,261	2,865,000	41.8%
Other liabilities	5,555,000	13,730,000	(8,175,000)	-59.5%
Total Liabilities	57,458,330	26,267,064	31,191,266	118.7%
Deferred pension credits	10,440	12,099	(1,659)	-13.7%
Total Deferred Inflows of Resources	10,440	12,099	(1,659)	-13.7%
Net Position:				
Net investment in capital assets	213,494,335	190,009,075	23,485,260	12.4%
Unrestricted	(2,091,596)	(458,357)	(1,633,239)	356.3%
Total Net Position	211,402,739	189,550,718	21,852,021	11.5%
Total Liabilities, Deferred Inflows of Resources, & Net Position	\$ 268,871,509	\$ 215,829,881	\$ 53,041,628	24.6%

Management Discussion and Analysis (Continued)

Financial Analysis (Continued)

Changes in assets, liabilities, and net position are discussed in the Financial Highlights section above.

Condensed Statement of Revenues, Expenses and Changes in Fund Net Position

	<u>2016</u>	<u>2015</u>	<u>Amount Change</u>	<u>% Change</u>
Revenues:				
Operating revenues	\$ 16,542,083	\$ 14,067,792	\$ 2,474,291	17.6%
Capital contributions	18,936,802	39,408,288	(20,471,486)	-51.9%
Earnings on investments	15,596	(33,230)	48,826	146.9%
Other non-operating revenues	1,437,518	1,324,832	112,686	8.5%
Total Revenues	<u>36,931,999</u>	<u>54,767,682</u>	<u>(17,835,683)</u>	<u>-32.6%</u>
Expenses:				
Maintenance of way	1,587,683	1,578,871	8,812	0.6%
Maintenance of equipment	1,716,823	1,325,693	391,130	29.5%
Rail car repairs	826,570	-	826,570	100.0%
Transportation	5,472,600	4,364,453	1,108,147	25.4%
General	5,311,815	4,278,381	1,033,434	24.2%
Total Railroad	<u>14,915,491</u>	<u>11,547,398</u>	<u>3,368,093</u>	<u>29.2%</u>
Other non-operating expenses	164,487	54,302	110,185	202.9%
Total Expenses	<u>15,079,978</u>	<u>11,601,700</u>	<u>3,478,278</u>	<u>30.0%</u>
Change in Net Position	21,852,021	43,165,982	(21,313,961)	-49.4%
Net Position, Beginning of Year - As Previously Reported	189,550,718	152,002,040	37,548,678	24.7%
Cummulative Change in Accounting Principle	<u>-</u>	<u>(5,617,304)</u>	<u>5,617,304</u>	<u>100.0%</u>
Net Position, Beginning of Year - Restated	<u>189,550,718</u>	<u>146,384,736</u>	<u>43,165,982</u>	<u>100.0%</u>
Net Position, End of Year	<u>\$ 211,402,739</u>	<u>\$ 189,550,718</u>	<u>\$ 21,852,021</u>	<u>11.5%</u>

Changes in revenues and expenses are discussed in the Financial Highlights section above.

Detailed Information on the Funds

The Economic Development Project Fund is used to account for land and land improvement contributions received from the South Carolina Department of Commerce which purchased the land and funded the land improvements using proceeds from the State of South Carolina's General Obligation Bond Fund. Contributions received were \$18,936,802 and \$39,408,288 for the years ended December 31, 2016 and 2015, respectively.

Management Discussion and Analysis (Continued)

Financial Analysis (Continued)

Detailed Information on the Funds (Continued)

CHS and NCS had a combined increase in net position of \$1,819,351 or 2.4% from the beginning net position primarily due from transfers in of \$2,000,000 received from CCS income, offset by a loss before transfers of \$180,649. Net investment in capital assets increased \$4,235,029 or 5.5% while unrestricted net position decreased \$2,415,678 or 245.3%. These changes in net position are primarily due to the acquisition and construction of capital assets as well as the increase of the net pension liability. Major changes in assets and liabilities include an increase in cash and cash equivalents of \$3,205,117 or 250.7% and a \$27,429,078 or 29.4% increase in capital assets related primarily to the continuation of the Intermodal Container Transfer Facility project. An increase of \$29,000,000 in notes payable related to a loan from the South Carolina Department of Commerce – SC Coordinating Council for Economic Development to fund the cost of the Intermodal Container Transfer Facility and a \$2,000,000 decrease in settlements payable as a result of the final installment payment made to the City of North Charleston per the terms of the 2012 settlement agreement. Revenues and expenses increased from the prior year due to operating Cosgrove Yard for a full year and starting rail car repair operations.

CCS had an increase in net position of \$1,095,868 or 8.9% from the beginning net position primarily due to income before transfers of \$3,095,868 and transfers out of \$2,000,000 made to CHS and NCS. Net investment in capital assets increased slightly, by \$313,429 or 2.7%, while unrestricted net position increased \$782,439 or 148.7%. Major changes in assets and liabilities include a \$895,019 or 24.3% increase in cash and cash equivalents and a \$850,916 or 25.5% increase in non-current liabilities due to the net pension liability. Revenues and expenses were fairly consistent with the prior year.

Financing Activities

As the Intermodal Container Transfer Facility capital project continues, the loan from the South Carolina Department of Commerce – SC Coordinating Council for Economic Development had an outstanding balance at December 31, 2016 of \$37,000,000.

As part of the settlement agreement with the City of North Charleston, the Division assumed responsibility for payment of \$6,360,000 in Tax Increment Financing (“TIF”) Bonds. Principal and interest is payable in annual installments beginning September 2013 through September 2037 with variable interest (.43% at June 30, 2016), as determined by the remarketing agent, payable each month. The balance outstanding at December 31, 2016 was \$5,730,000.

More detailed information about the Division’s financing activities is presented in the Notes to the Financial Statements.

Management Discussion and Analysis (Continued)

Capital Asset Activities

Capital assets consist of land, land improvements, fencing, buildings, machinery and equipment, depreciable roads, non-depreciable roads, leasehold improvements, and projects under construction. The Division had \$253,011,381 invested in capital assets, net of accumulated depreciation, as of December 31, 2016, compared to \$206,332,072 as of December 31, 2015. The table below provides a summary.

	Capital Assets at December 31,	
	2016	2015
Land	\$ 77,053,362	\$ 77,053,362
Land improvements	80,442,535	61,505,733
Fencing	51,478	51,478
Buildings	18,340,121	17,943,469
Machinery and equipment	8,720,070	7,953,049
Depreciable road	1,192,360	1,192,360
Non-depreciable road	13,097,099	13,097,099
Leasehold improvements	700,665	184,106
Projects under construction	62,658,135	35,533,647
Total Capital Assets	<u>262,255,825</u>	<u>214,514,303</u>
Less: Accumulated Depreciation	(9,244,444)	(8,182,231)
Capital Assets, Net	<u>\$ 253,011,381</u>	<u>\$ 206,332,072</u>

Major additions in 2016 include the acquisition of land improvements through capital contributions by the South Carolina Department of Commerce and further development of the Intermodal Container Transfer Facility.

More detailed information about the Division's capital asset activities is presented in the Notes to the Financial Statements.

Economic Factors and Next Year Operations

- Freight traffic is expected to remain fairly stable in 2017.
- Administrative expenses are expected to be higher due to financing costs for the construction of various capital projects.
- The purchase of a 45+ mile railroad in Hampton and Colleton County will be completed in 2017.
- Capital expenditures will continue to be incurred as the permitting process, planning, and design continues for the construction of the Intermodal Container Transfer Facility as well as the Camp Hall project.
- Various properties located on the Navy Base will be sent to state surplus to be sold.

BASIC FINANCIAL STATEMENTS

PALMETTO RAILWAYS
STATEMENT OF NET POSITION - ENTERPRISE FUNDS
DECEMBER 31, 2016

	ECONOMIC DEVELOPMENT PROJECT FUND	CHS-NCS	CCS	INTERDIVISION ELIMINATIONS	TOTAL
ASSETS					
Current Assets:					
Cash and cash equivalents	\$ -	1,191,969	4,574,453	-	\$ 5,766,422
Cash and cash equivalents, restricted	-	3,291,543	-	-	3,291,543
Restricted cash - security deposits	-	109,215	-	-	109,215
Accounts receivable	-	1,810,245	424,295	-	2,234,540
Accounts receivable from other division	-	683,412	-	(683,412)	-
Interest receivable	-	250	1,259	-	1,509
Deposits to purchase land	-	253,040	-	-	253,040
Inventories	-	669,632	30,509	-	700,141
Prepayments	-	593,991	-	-	593,991
Total Current Assets	-	8,603,297	5,030,516	(683,412)	12,950,401
Property, Plant and Equipment:					
Land and non-depreciable assets	120,000,000	103,092,726	10,158,405	-	233,251,131
Other depreciable assets, net of accumulated depreciation	-	17,780,501	1,979,749	-	19,760,250
Total Property, Plant and Equipment	120,000,000	120,873,227	12,138,154	-	253,011,381
TOTAL ASSETS	120,000,000	129,476,524	17,168,670	(683,412)	265,961,782
DEFERRED OUTFLOWS OF RESOURCES					
Deferred pension charges	-	1,654,860	1,254,867	-	2,909,727
TOTAL DEFERRED OUTFLOWS OF RESOURCES	-	1,654,860	1,254,867	-	2,909,727
LIABILITIES					
Current Liabilities:					
Accounts payable to other division	-	-	683,412	(683,412)	-
Accounts payable - other	-	3,757,385	-	-	3,757,385
Security deposits	-	109,215	-	-	109,215
Accrued payroll	-	684,579	-	-	684,579
Payroll taxes withheld and accrued employee benefits	-	120,111	-	-	120,111
Accrued annual leave and benefits, current portion	-	115,655	40,388	-	156,043
Notes payable - Short-Term	-	37,000,000	-	-	37,000,000
TIF bonds payable - Short-Term	-	175,000	-	-	175,000
Unearned revenue	-	94,834	-	-	94,834
Total Current Liabilities	-	42,056,779	723,800	(683,412)	42,097,167
Non-current Liabilities:					
Accrued annual leave and benefits, Non-current portion	-	30,112	56,790	-	86,902
TIF bonds payable	-	5,555,000	-	-	5,555,000
Net pension liability	-	5,527,672	4,191,589	-	9,719,261
Total Non-current Liabilities	-	11,112,784	4,248,379	-	15,361,163
TOTAL LIABILITIES	-	53,169,563	4,972,179	(683,412)	57,458,330
DEFERRED INFLOWS OF RESOURCES					
Deferred pension credits	-	5,938	4,502	-	10,440
TOTAL DEFERRED INFLOWS OF RESOURCES	-	5,938	4,502	-	10,440
NET POSITION					
Net investment in capital assets	120,000,000	81,356,181	12,138,154	-	213,494,335
Unrestricted	-	(3,400,298)	1,308,702	-	(2,091,596)
TOTAL NET POSITION	\$ 120,000,000	77,955,883	13,446,856	-	\$ 211,402,739

The accompanying notes to the financial statements are an integral part of this statement.
See accompanying independent auditor's report.

PALMETTO RAILWAYS
STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN FUND NET POSITION - ENTERPRISE FUNDS
YEAR ENDED DECEMBER 31, 2016

	ECONOMIC DEVELOPMENT PROJECT FUND	CHS-NCS	CCS	TOTAL
Operating Revenues:				
Switching fees	\$ -	6,481,945	710,421	\$ 7,192,366
Freight charge	-	572,580	6,781,164	7,353,744
Rental revenue	-	320,075	-	320,075
Contractual services	-	40,787	3,490	44,277
Storage revenue	-	745,426	-	745,426
Dispatching service	-	-	54,775	54,775
Car repair	-	714,023	-	714,023
Other revenue	-	117,397	-	117,397
Total Operating Revenues	-	8,992,233	7,549,850	16,542,083
Operating Expenses:				
Railways Operating Expenses:				
Maintenance of Way:				
Depreciation	-	129,012	58,699	187,711
Other maintenance of way expenses	-	847,745	552,227	1,399,972
Total Maintenance of Way	-	976,757	610,926	1,587,683
Maintenance of Equipment:				
Depreciation	-	310,392	164,847	475,239
Other equipment expenses	-	809,582	432,002	1,241,584
Total Maintenance of Equipment	-	1,119,974	596,849	1,716,823
Car Repair:				
Depreciation	-	1,871	-	1,871
Other car repair expenses	-	824,699	-	824,699
Total Car Repair	-	826,570	-	826,570
Transportation:				
Other transportation expenses	-	3,813,855	1,658,745	5,472,600
Total Transportation	-	3,813,855	1,658,745	5,472,600
General:				
Administration	-	2,710,096	1,281,267	3,991,363
Insurance	-	849,681	470,771	1,320,452
Total General	-	3,559,777	1,752,038	5,311,815
Total Railway Operating Expenses	\$ -	10,296,933	4,618,558	\$ 14,915,491

The accompanying notes to the financial statements are an integral part of this statement.
See accompanying independent auditor's report.

PALMETTO RAILWAYS
**STATEMENT OF REVENUES, EXPENSES, AND
 CHANGES IN FUND NET POSITION - ENTERPRISE FUNDS**
 YEAR ENDED DECEMBER 31, 2016

	ECONOMIC DEVELOPMENT PROJECT FUND	CHS-NCS	CCS	TOTAL
Operating Income	\$ -	(1,304,700)	2,931,292	\$ 1,626,592
Non-operating Revenues (Expenses):				
Other rental income, net	-	1,219,476	100	1,219,576
Interest income and again (loss) on investments	-	1,286	14,310	15,596
Gain (loss) on sale or disposal of fixed assets	-	12,605	-	12,605
Other income, net	-	55,171	150,166	205,337
Industrial developmentn costs	-	(164,487)	-	(164,487)
Total Non-Operating Revenues (Expenses)	-	1,124,051	164,576	1,288,627
Income Before Capital Contributions and Transfers	-	(180,649)	3,095,868	2,915,219
Capital Contributions	18,936,802	-	-	18,936,802
Transfers Between Divisions	-	2,000,000	(2,000,000)	-
Change in Net Position	18,936,802	1,819,351	1,095,868	21,852,021
Net Position, Beginning of Year	101,063,198	76,136,532	12,350,988	189,550,718
Net Position, End of Year	\$ 120,000,000	77,955,883	13,446,856	\$ 211,402,739

The accompanying notes to the financial statements are an integral part of this statement.
 See accompanying independent auditor's report.

PALMETTO RAILWAYS
STATEMENT OF CASH FLOWS - ENTERPRISE FUNDS
YEAR ENDED DECEMBER 31, 2016

	ECONOMIC DEVELOPMENT PROJECT FUND	CHS-NCS	CCS	TOTAL
Cash Flows from Operating Activities:				
Cash received from customers	\$ -	9,094,575	7,499,752	\$ 16,594,327
Cash payments to suppliers and employees	-	(8,157,315)	(4,299,925)	(12,457,240)
Rents received	-	1,759,756	100	1,759,856
Security deposits	-	21,323	-	21,323
Other income received	-	55,171	150,166	205,337
Net Cash Provided By (Used In) Operating Activities	-	2,773,510	3,350,093	6,123,603
Cash Flows from Non-Capital Financing Activities:				
Cash received from/paid to other divisions	-	2,000,000	(2,000,000)	-
Net Cash Provided By (Used In) Non-Capital Financing Activities	-	2,000,000	(2,000,000)	-
Cash Flows from Capital and Related Financing Activities:				
Cash received from sale of fixed assets	-	12,605	-	12,605
Cash received from note	-	29,000,000	-	29,000,000
Proceeds received from transfer of assets to other division	-	365,449	-	365,449
Payments for TIF Bonds payable	-	(2,165,000)	-	(2,165,000)
Acquisition and construction of capital assets	-	(28,761,237)	(469,261)	(29,230,498)
Net Cash Provided By (Used In) Capital and Related Financing Activities	-	(1,548,183)	(469,261)	(2,017,444)
Cash Flows from Investing Activities:				
Investment income	-	1,113	14,187	15,300
Net Cash Provided By (Used In) Investing Activities	-	1,113	14,187	15,300
Net Increase (Decrease) in Cash and Cash Equivalents	-	3,226,440	895,019	4,121,459
Cash and Cash Equivalents, Beginning of Year	-	1,366,287	3,679,434	5,045,721
Cash and Cash Equivalents, End of Year	\$ -	4,592,727	4,574,453	\$ 9,167,180

The accompanying notes to the financial statements are an integral part of this statement.
See accompanying independent auditor's report.

PALMETTO RAILWAYS
STATEMENT OF CASH FLOWS - ENTERPRISE FUNDS
YEAR ENDED DECEMBER 31, 2016

	ECONOMIC DEVELOPMENT PROJECT FUND	CHS-NCS	CCS	TOTAL
Reconciliation of Operating Income (Loss) to Net Cash Flows from				
Operating Activities:				
Operating Income (Loss)	\$ -	(1,304,700)	2,931,292	\$ 1,626,592
Adjustments to reconcile operating income to net cash provided				
by (used in) operating activities:				
Depreciation	-	965,150	155,832	1,120,982
Non-Cash Pension expenses	-	637,526	314,299	951,825
Non-operating revenues (expenses)	-	1,110,160	150,266	1,260,426
(Increase) decrease in assets:				
Accounts receivable	-	(10,637)	(50,098)	(60,735)
Accounts receivable from other division	-	112,979	-	112,979
Inventories	-	12,958	(1,203)	11,755
Prepayments	-	(285,028)	-	(285,028)
Increase (decrease) in liabilities:				
Accounts payable - other	-	1,118,453	-	1,118,453
Accounts payable to other division	-	-	(112,979)	(112,979)
Security deposits	-	21,323	-	21,323
Payroll taxes withheld and accrued employee benefits	-	9,914	-	9,914
Accrued annual leave	-	40,093	(37,316)	2,777
Accrued salaries	-	328,914	-	328,914
Unearned revenue	-	16,405	-	16,405
Net Cash Provided By (Used In) Operating Activities	<u>\$ -</u>	<u>2,773,510</u>	<u>3,350,093</u>	<u>\$ 6,123,603</u>
Schedule of Non-cash Investing, Capital and Financing Activities:				
Change in capital acquisitions included in accounts payable	\$ -	6,520	-	\$ 6,520
Acquisition of capital assets through capital contributions	\$ 18,936,802	-	-	\$ 18,936,802

The accompanying notes to the financial statements are an integral part of this statement.
See accompanying independent auditor's report.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 1 - REPORTING ENTITY

South Carolina Department of Commerce – Division of Public Railways d/b/a Palmetto Railways (the Division) is part of the State of South Carolina Primary Government. The Division is reported as an enterprise fund in the State’s Comprehensive Annual Financial Report.

Effective July 1, 1993, as part of the Government Restructuring Act of 1993, Code Section 13-1-1310 created the Division of Public Railways within the Department of Commerce which is governed by the Secretary of the Department of Commerce.

The Department of Commerce is a cabinet agency operating under the governor and is subject to state laws and regulations. The Division however is not subject to the State Procurement Code or Appropriation Act. Also, the Division is not subject to State Human Resource Regulations. The Secretary of the Department of Commerce is responsible for oversight of the Division. The Division has powers of a body corporate including:

1. To sue or be sued, and make contracts.
2. To acquire by purchase or donation and to own, rent, lease, mortgage and dispose of real or personal property.
3. To operate, acquire, construct, maintain and control the tracks and equipment of the Division and be governed by rules and regulations of the Interstate Commerce Commission and its successor, the Surface Transportation Board.
4. To employ and dismiss the employees of the Division and to fix and to pay the compensation thereof.
5. To issue revenue bonds and other obligations, subject to approval by the State Fiscal Accountability Authority (SFAA), to defray the cost of acquisition of other railroads.

The individual subdivisions of the South Carolina Department of Commerce - Division of Public Railways d/b/a Palmetto Railways are funds of the State of South Carolina established by various sections of the Code of Laws of South Carolina. The accompanying financial statements present the financial position, results of operations, and the cash flows solely of the South Carolina Department of Commerce - Division of Public Railways d/b/a Palmetto Railways and do not include any other funds of the State of South Carolina.

The South Carolina Department of Commerce - Division of Public Railways d/b/a Palmetto Railways consists of three separate operating divisions: 1) the Charleston Subdivision (CHS) and the North Charleston Subdivision (NCS), 2) the Charity Church Subdivision (CCS), and 3) the Economic Development Project Fund. The functions of each of the divisions are outlined as follows:

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 1 - REPORTING ENTITY (CONTINUED)

- a. The Charleston Subdivision and the North Charleston Subdivision (CHS-NCS) have the responsibility of operations of the railroad yards at Charleston Harbor, Cosgrove Yard and the former Navy Base. Switching activity between privately owned railroad lines and seagoing vessels is the primary operation and revenue source.
- b. Operation and maintenance of the railroad line constructed in Berkeley County, South Carolina is the primary responsibility of the Charity Church Subdivision (CCS). The railroad was constructed with financing by Amoco Chemicals Corporation, its major customer. This came after requests from the Division and the SFAA to service the east side of the Cooper River north of Charleston, South Carolina were denied by the common carrier railroads operating in South Carolina.
- c. The Economic Development Project Fund is used to account for land and land improvement contributions received from the South Carolina Department of Commerce which were purchased using proceeds from the State of South Carolina's General Obligation Bond Fund.

The core of the financial reporting entity is the primary government which has a separately elected governing body. As required by generally accepted accounting principles, the financial reporting entity includes both the primary government and all its component units. Component units are legally separate organizations for which the elected officials or the primary government are financially accountable. In turn, component units may have component units.

An organization other than a primary government may serve as a nucleus for a reporting entity when it issues separate financial statements. That organization is identified herein as a primary entity.

The primary entity is financially accountable if it appoints a voting majority of the organization's governing body including situations in which the voting majority consists of the primary entity's officials serving as required by law (e.g., employees who serve in an ex officio capacity on the component unit's board are considered appointments by the primary entity) and (1) it is able to impose its will on that organization or (2) there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary entity. The primary entity also may be financially accountable if an organization is fiscally dependent on it even if it does not appoint a voting majority of the board. An organization is fiscally dependent on the primary entity that holds one or more of the following powers:

1. Determine its budget without another government's having the authority to approve and modify that budget.
2. Levy taxes or set rates or charges without approval by another government.
3. Issue bonded debt without approval by another government.

Based on the application of the above criteria, no component units are included in the reporting entity.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The Division adheres to generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board (“GASB”).

The Division maintains separate accounting of its three sub-divisions: 1) the Charleston Subdivision and the North Charleston Subdivision, 2) the Charity Church Subdivision, and 3) the Economic Development Project Fund. Presented here are the financial statements of the three funds of the South Carolina Department of Commerce - Division of Public Railways d/b/a Palmetto Railways.

The Division utilizes the accrual basis of accounting. Under the accrual basis of governmental accounting for enterprise funds, revenues are recognized in the accounting period in which they are earned and become measurable. Expenses are recognized in the period incurred, if measurable. Net position is reported in three components: (1) net investment in capital assets, (2) restricted and (3) unrestricted. The operating statement presents increases (e.g., revenues) and decreases (e.g., expenses) in total net position. The accounting principles utilized by the Division are in conformity with the uniform system of accounts for railroad companies prescribed by the Surface Transportation Board and generally accepted accounting principles.

Operating income includes revenues and expenses related to the primary continuing operations of the fund. Principal operating revenues are charges to customers for sales or services. Principal operating expenses are the costs of providing goods and services and include administrative expenses and depreciation of capital assets.

Fund Accounting

The Division uses funds to report its financial position and the results of its operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fund is a separate fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with related liabilities and residual equities or balances and changes therein which are segregated to carry on specific activities or attain certain objectives in accordance with applicable regulations, restrictions or limitations. Separate accounts are maintained for each fund however, in the accompanying financial statements, funds that have similar characteristics have been combined into fund types. Accordingly, all financial transactions have been reported by fund type.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fund Accounting (continued)

Funds are classified into three categories: governmental, proprietary, and fiduciary. Each category, in turn, is divided into separate "fund types." The Division reports activities of the enterprise "fund type" under the proprietary fund category. Enterprise funds account for activities that are self-sustaining, primarily through user charges or are used when management wants to control or measure costs of services.

Property, Plant, and Equipment

Except for track and roadway, capital assets with a per unit acquisition cost in excess of \$5,000 are capitalized and depreciated over the estimated useful lives of the assets using the straight-line method of depreciation. Estimated useful lives are as follows:

Buildings	15 - 40 years
Depreciable Road	75 years
Equipment	3 - 25 years
Leasehold Improvements	5 - 20 years

Track and roadway are capitalized at cost and depreciation is not recognized. Replacements and repairs are expensed in the period that costs are incurred. Betterments to track and roadway are capitalized.

Inventories

Inventories consisting of materials and supplies are stated at the lower of cost or market using the weighted average method.

Policy for Uncollectible Accounts

At year-end, management reviews past due accounts receivable and recognizes bad debt expense for those accounts determined to be uncollectible. This method is not in conformity with generally accepted accounting principles, which requires accounts receivable to be reported at net realizable value using an allowance for uncollectible accounts. However based on the Division's collection history, the results from using the direct write-off method are not materially different from the allowance method.

Intra-division Transactions and Balances

Transactions among the subdivisions of the Division have been eliminated for purposes of the combined financial statements presented herein. Administration overhead incurred is divided between CHS-NCS and CCS. Overhead of the subdivisions is split, 40% to CCS and 60% to CHS-NCS. Overhead expense includes superintendence, general administrative, and insurance.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Statement of Cash Flows

For purposes of this statement, the Division considers deposits with State of South Carolina cash management pool to be cash equivalents because they are readily convertible to cash with an insignificant risk of loss in value.

Cash and Cash Equivalents

The amounts shown in the financial statements as "*cash and cash equivalents*" represent cash on deposit with the State Treasurer and cash invested in various investments by the State Treasurer as part of the State's internal cash management pool.

Because the State's internal cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and invest in certain debt obligations of its political subdivisions, certificates of deposit, collateralized repurchase agreements, and certain corporate bonds. Most State agencies participate in the State's internal cash management pool; however, some agency accounts are not included in the pool because of restrictions on the use of funds. For those accounts, cash equivalents include investments in short-term, highly liquid securities having an original maturity of three months or less.

Cash equivalents: The pool includes some long-term investments such as obligations of the United States and certain agencies of the United States, obligations of the State of South Carolina and the State's internal cash management pool. The State's internal cash management pool is comprised of the general deposit account and several special deposit accounts. The State records each agency's equity interest in the general deposit account; however, all earnings on that account are credited to the General Fund of the State. Agencies record and report their deposits in the general deposit account at cost. However, agencies report their deposits in the special deposit accounts at fair value. Investments in the pool are recorded at fair value. Interest earned by the agencies' special deposit accounts is posted to the agency's account at the end of each month and is retained by the agency. Interest earnings are allocated based on the percentage of an agency's accumulated daily interest receivable to the total undistributed interest received by the pool. Reported interest income includes interest earnings, realized gains/losses and unrealized gains/losses on investments in the pool arising from changes in fair value.

The Division only has special deposit accounts. Realized gains and losses are allocated daily and are included in the accumulated income receivable. Unrealized gains and losses are allocated at year-end based on the agency's percentage of ownership in the pool.

Although the State's internal cash management pool includes some long-term investments, it operates as a demand deposit account; therefore, for credit risk information pertaining to the internal cash management pool, see the deposits disclosures in Note 3.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. Those estimates and assumptions affect the reported amounts of assets and deferred outflows of resources and liabilities and deferred inflows of resources and disclosure of these balances as of the date of the financial statements. In addition, they affect the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates and assumptions.

Deferred Outflows/Inflows of Resources

In addition to assets, the Statement of Net Position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. The Division currently has one type of deferred outflows of resources. The Division reports deferred pension charges in its Statement of Net Position in connection with its participation in the South Carolina Retirement System and the South Carolina Police Officers Retirement System. These deferred pension charges are either (a) recognized in the subsequent period as a reduction of the net pension liability (which includes pension contributions made after the measurement date) or (b) amortized in a systematic and rational method as pension expense in future periods in accordance with GAAP.

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, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Division currently has one type of deferred inflows of resources. The Division reports deferred pension credits in its Statement of Net Position in connection with its participation in the South Carolina Retirement System and South Carolina Police Officers Retirement System. These deferred pension credits are amortized in a systematic and rational method and recognized as a reduction of pension expense in future periods in accordance with GAAP.

Net Position

Net position represents the difference between assets and deferred outflows of resources and liabilities and deferred inflows of resources in the Statement of Net Position. Net position is classified as net investment in capital assets; restricted; and unrestricted. Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets. Outstanding debt which has not been spent is included in the same net position component as the unspent proceeds. Net position is reported as restricted when there are limitations imposed on their use either through enabling legislation or through external restrictions imposed by creditors, grantors, contributors, or laws or regulations of other governments.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Pensions

The Division recognizes a net pension liability for each qualified pension plan in which it participates, which represents the excess of the total pension liability over the fiduciary net position of the qualified pension plan, or the Division's proportionate share thereof in the case of a cost-sharing multiple-employer plan, measured as of the Division's fiscal year-end. Changes in the net pension liability during the period are recorded as pension expense, or as deferred outflows or inflows of resources depending on the nature of the change, in the period incurred. Those changes in net pension liability that are recorded as deferred outflows or inflows of resources that arise from changes in actuarial assumptions or other inputs and differences between expected or actual experience are amortized over the weighted average remaining service life of all participants in the respective qualified pension plan and recorded as a component of pension expense beginning with the period in which they are incurred. Projected earnings on qualified pension plan investments are recognized as a component of pension expense. Differences between projected and actual investment earnings are reported as deferred outflows or inflows of resources and amortized as a component of pension expense on a closed basis over a five-year period beginning with the period in which the difference occurred.

Other Postemployment Benefits

Other post-employment benefits ("OPEB") cost for retiree healthcare and similar non-pension retiree benefits is required to be measured and disclosed using the accrual basis of accounting (see Note 11 for more information). Annual OPEB cost is equal to the annual required contributions to the OPEB Plan, calculated in accordance with GAAP.

NOTE 3 - DEPOSITS

All deposits of the Division are under the control of the State Treasurer who, by law, has sole authority for investing state funds.

State law requires full collateralization of all State Treasurer bank balances. The State Treasurer must correct any deficiencies in collateral within seven days. At December 31, 2016, all State Treasurer bank balances were fully insured or collateralized with securities held by the State or by its agents in the State's name.

With respect to investments in the State's cash management pool, all of the State Treasurer's investments are insured or registered or are investments for which the securities are held by the State or its agent in the State's name. Information pertaining to the reported amounts, fair values, and credit risk of the State Treasurer's investments is disclosed in the Comprehensive Annual Financial Report of the State of South Carolina.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 4 - PROPERTY, PLANT, EQUIPMENT, AND DEPOSITS TO PURCHASE LAND

Property, plant, and equipment are stated at original cost with the exception of certain assets received from the South Carolina Ports Authority (SCPA). Assets of \$451,136 acquired by the Division from SCPA during the organization of the South Carolina Department of Commerce - Division of Public Railways are stated at the cost to SCPA, less accumulated depreciation at the time of organization. Also, in 1997 CHS-NCS exchanged certain assets with the SCPA. The assets received from the SCPA were recorded on CHS-NCS's books at book value of assets as recorded by the SCPA. Amounts recorded included track and land improvements of \$1,324,462 and an engine house in the amount of \$1,182,402. Depreciation is computed on the straight-line method. In 2005 a capital contribution was recorded for land, land improvements and track on CCS. The amounts recorded were \$201,000 for land, \$308,229 for land improvements and \$749,746 for non-depreciable road.

On July 26, 2010, the Division entered into a Purchase and Sales Agreement with Greystar GP, LLC. The agreement required the Division to provide the necessary funds to Greystar to purchase loan documents and the right to foreclosure under a Mortgage Loan and Sale agreement Greystar had entered into with Capmark Finance Inc., also on that date. The purchase price was \$21,390,500. On August 27, 2010, Greystar assigned the Mortgage Loan and Sale agreement to CHSA, LLC, and also assigned 100% of CHSA, LLC to the Division. On December 7, 2010, the mortgage was satisfied by foreclosure at the former Navy Base. The property, which includes 240 acres of land and approximately 65 buildings, was deeded to the Division for nominal consideration on December 15, 2010 and is reported on CHS-NCS's books at the fair value as of the date of acquisition. CHSA, LLC had no ongoing operations during the year ended December 31, 2016.

On December 5, 2012 the Division agreed to sign a Settlement Agreement and Release (the "Agreement") to settle and release six civil actions in which the Division was the defendant. As part of the agreement, the Division assumed \$6,360,000 in Tax Increment Financing ("TIF") Bonds for the Navy Base Redevelopment Project. The Division also agreed to pay \$8,000,000 to the City of North Charleston (the "City") to mitigate rail access impacts. The \$6,360,000 and \$8,000,000 are included as construction in progress of the proposed Intermodal Container Transfer Facility. The Agreement also required the Division and the City to transfer property to one another. The first transfer occurred in August 2014. See Notes 14 and 15.

On October 9, 2013, the Division purchased land and several office and warehouse buildings on the former Navy Yard from the Noisette Company, LLC, Navy Yard New Market I, LLC and 10 Storehouse Row, LLC. The purchase price was \$10,668,000.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 4 - PROPERTY, PLANT, EQUIPMENT, AND DEPOSITS TO PURCHASE LAND (CONTINUED)

During 2016 the Division recorded an additional \$18,936,802 in land improvements to the 468 acres of land acquired in December 2013 related to a lease agreement with the Boeing Company. See Note 6. The land purchase price of \$49,092,700 and the land improvement costs were paid by the South Carolina Department of Commerce, who subsequently donated the assets to the Division.

A summary of property, plant, and equipment by subdivision is as follows:

	<u>CHS-NCS</u>				Balance 12/31/2016
	Balance 12/31/2015*	Transfers In (Out)	Additions	Deletions	
Non-depreciable capital assets:					
Land	\$ 27,333,243	-	-	-	\$ 27,333,243
Land improvements	3,507,686	-	-	-	3,507,686
Non-depreciable road	9,593,662	-	-	-	9,593,662
Projects under construction	35,533,647	(882,008)	28,006,496	-	62,658,135
Total non-depreciable capital assets	<u>75,968,238</u>	<u>(882,008)</u>	<u>28,006,496</u>	<u>-</u>	<u>103,092,726</u>
Depreciable capital assets:					
Fencing	51,478	-	-	-	51,478
Buildings	17,029,196	-	312,225	-	17,341,421
Machinery and equipment	5,993,122	-	440,956	58,769	6,375,309
Depreciable road	246,509	-	-	-	246,509
Leasehold improvements	184,106	516,559	-	-	700,665
Total depreciable capital assets	<u>23,504,411</u>	<u>516,559</u>	<u>753,181</u>	<u>58,769</u>	<u>24,715,382</u>
Accumulated depreciation:					
Fencing	51,478	-	-	-	51,478
Buildings	2,182,760	-	486,906	-	2,669,666
Machinery and equipment	3,534,291	-	408,114	58,769	3,883,636
Depreciable road	75,865	-	1,255	-	77,120
Leasehold improvements	184,106	-	68,875	-	252,981
Total accumulated depreciation	<u>6,028,500</u>	<u>-</u>	<u>965,150</u>	<u>58,769</u>	<u>6,934,881</u>
Net depreciable capital assets	<u>17,475,911</u>	<u>516,559</u>	<u>(211,969)</u>	<u>-</u>	<u>17,780,501</u>
Net capital assets	<u>\$ 93,444,149</u>	<u>(365,449)</u>	<u>27,794,527</u>	<u>-</u>	<u>\$ 120,873,227</u>

*The balances at December 31, 2015 are shown adjusted for classification changes.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

**NOTE 4 - PROPERTY, PLANT, EQUIPMENT, AND DEPOSITS TO PURCHASE LAND
(CONTINUED)**

	<u>CCS</u>				Balance 12/31/2016
	Balance 12/31/2015	Transfers In (Out)	Additions	Deletions	
Non-depreciable capital assets:					
Land	\$ 627,419	-	-	-	\$ 627,419
Land improvements	6,027,549	-	-	-	6,027,549
Non-depreciable road	3,503,437	-	-	-	3,503,437
Total non-depreciable capital assets	<u>10,158,405</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>10,158,405</u>
Depreciable capital assets:					
Buildings	914,273	-	84,427	-	998,700
Machinery and equipment	1,959,927	365,449	19,385	-	2,344,761
Depreciable road	945,851	-	-	-	945,851
Total depreciable capital assets	<u>3,820,051</u>	<u>365,449</u>	<u>103,812</u>	<u>-</u>	<u>4,289,312</u>
Accumulated depreciation:					
Buildings	860,795	-	26,527	-	887,322
Machinery and equipment	854,559	-	115,892	-	970,451
Depreciable road	438,377	-	13,413	-	451,790
Total accumulated depreciation	<u>2,153,731</u>	<u>-</u>	<u>155,832</u>	<u>-</u>	<u>2,309,563</u>
Net depreciable capital assets	<u>1,666,320</u>	<u>365,449</u>	<u>(52,020)</u>	<u>-</u>	<u>1,979,749</u>
Net capital assets	<u>\$ 11,824,725</u>	<u>365,449</u>	<u>(52,020)</u>	<u>-</u>	<u>\$ 12,138,154</u>
<u>Economic Development Project Fund</u>					
	Balance 12/31/2015*	Transfers In (Out)	Additions	Deletions	Balance 12/31/2016
Non-depreciable capital assets:					
Land	\$ 49,092,700	-	-	-	\$ 49,092,700
Land Improvements	51,970,498	-	18,936,802	-	70,907,300
Total non-depreciable capital assets	<u>101,063,198</u>	<u>-</u>	<u>18,936,802</u>	<u>-</u>	<u>120,000,000</u>
Net capital assets	<u>\$ 101,063,198</u>	<u>-</u>	<u>18,936,802</u>	<u>-</u>	<u>\$ 120,000,000</u>

*The balances at December 31, 2015 are shown adjusted for classification changes.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 4 - PROPERTY, PLANT, EQUIPMENT, AND DEPOSITS TO PURCHASE LAND
(CONTINUED)

	<u>COMBINED</u>				Balance 12/31/2016
	Balance 12/31/2015*	Transfers In (Out)	Additions	Deletions	
Non-depreciable capital assets:					
Land	\$ 77,053,362	-	-	-	\$ 77,053,362
Land improvements	61,505,733	-	18,936,802	-	80,442,535
Non-depreciable road	13,097,099	-	-	-	13,097,099
Projects under construction	35,533,647	(882,008)	28,006,496	-	62,658,135
Total non-depreciable capital assets	<u>187,189,841</u>	<u>(882,008)</u>	<u>46,943,298</u>	<u>-</u>	<u>233,251,131</u>
Depreciable capital assets:					
Fencing	51,478	-	-	-	51,478
Buildings	17,943,469	-	396,652	-	18,340,121
Machinery and equipment	7,953,049	365,449	460,341	58,769	8,720,070
Depreciable road	1,192,360	-	-	-	1,192,360
Leasehold improvements	184,106	516,559	-	-	700,665
Total depreciable capital assets	<u>27,324,462</u>	<u>882,008</u>	<u>856,993</u>	<u>58,769</u>	<u>29,004,694</u>
Accumulated depreciation:					
Fencing	51,478	-	-	-	51,478
Buildings	3,043,555	-	513,433	-	3,556,988
Machinery and equipment	4,388,850	-	524,006	58,769	4,854,087
Depreciable road	514,242	-	14,668	-	528,910
Leasehold improvements	184,106	-	68,875	-	252,981
Total accumulated depreciation	<u>8,182,231</u>	<u>-</u>	<u>1,120,982</u>	<u>58,769</u>	<u>9,244,444</u>
Net depreciable capital assets	<u>19,142,231</u>	<u>882,008</u>	<u>(263,989)</u>	<u>-</u>	<u>19,760,250</u>
Net capital assets	<u>\$ 206,332,072</u>	<u>-</u>	<u>46,679,309</u>	<u>-</u>	<u>\$ 253,011,381</u>

*The balances at December 31, 2015 are shown adjusted for classification changes.

Depreciation expense for the period by subdivision and in total was as follows: CHS-NCS \$965,150 and CCS \$155,832, Total - \$1,120,982. Included in other rental income-net and leased track is \$387,285 of depreciation on buildings that are held for rent and \$68,876 in amortization of leased track, respectively. The cost of the leased buildings is \$14,243,177 and net book value is \$12,804,373. The majority of these assets were acquired as part of the Greystar purchase in paragraph 2 and the Noisette Company, LLC, Navy Yard New Market I, LLC and 10 Storehouse Row, LLC purchases in paragraph 4 of this note. See Note 9.

As of December 31, 2016, the Division had remaining construction commitments of \$9,553,695 relating to construction at the Intermodal Container Transfer Facility and \$3,507,583 related to the Camp Hall project. The Camp Hall project consists of building a rail connection from a new industrial site located in Berkeley County to the CSX Transportation mainline.

During the year ended December 31, 2016, CHS-NCS transferred one locomotive with a net book value of \$365,449 to CCS. This transfer is shown as net transfers in the CHS-NCS and CCS detailed schedules above and was paid to CHS-NCS by CCS.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 5 – ACCRUED ANNUAL LEAVE

Non-union employees are entitled to accrue and carry forward at calendar year end a maximum of 180 days sick leave and 45 days annual vacation leave. Upon termination of employment, employees are entitled to be paid for accumulated unused annual vacation leave up to the maximum of 45 days, but are not entitled to any payment for unused sick leave. Employees do not accrue or carry forward holiday leave, compensatory time, or overtime.

Union employees can earn up to 25 days annual vacation leave per year, but do not earn any sick leave. Union employees do not carry forward any unused vacation leave. Upon termination of employment, union employees are entitled to be paid for accumulated unused annual vacation leave up to 25 days. Union employees do not accrue or carry forward holiday leave, compensatory time, or overtime.

The Division calculates the gross compensated absences liability based on recorded balances of unused leave. The entire unpaid liability for which the employer expects to compensate employees through paid time off or cash payments, inventoried at fiscal year-end current salary costs and the cost of the salary-related benefit payments is recorded as a current liability. The net change in the liability is recorded in the current year in the applicable operating department.

NOTE 6 – UNEARNED REVENUE/OPERATING LEASES/OPERATING RENTAL REVENUE

Effective March 4, 1994, CHS-NCS began leasing land and improvements in Spartanburg County, South Carolina for \$200,000 a year. The lease is for ten years with two ten-year options to renew. During the lease term the lessee has the right to purchase the land and improvements for CHS-NCS's cost not to exceed \$5,000,000. The rent is paid at the beginning of each year's anniversary for one year effective March 4, 1994 and will be adjusted annually based on 90-day Treasury bill rates. The initial rent was based on a 4% annual return on the initial investment of \$2,000,000, which is why Treasury bill rates will be used to determine changes in the annual rent. The Division's total investment in this project ended up being \$4,365,595 which is the amount on which a new rental rate will be determined annually effective March 4. The annual rental rate determined at March 4, 2015 was \$200,000 and at March 4, 2016 was \$200,000. The land is used as a railroad spur to the BMW plant. In February 2014, this lease was extended for the final 10 year renewal term through March 3, 2024. During 2016, \$200,000 was recognized as operating rental revenue and \$33,333 was deferred revenue based on the terms of this agreement. Also effective March 4, 1996, the Division began receiving revenue on certain car hauls out of the BMW plant by Norfolk Southern. This amounted to \$550,080 in 2016 and is included in freight income.

On December 15, 2010 the Division was deeded over approximately 240 acres of property and approximately 65 buildings at the former Navy Base and on October 9, 2013 the Division purchased additional property and buildings, see Note 4 and Note 9. The property has several commercial leases ranging from month to month leases to nine year leases. See Note 9 for total revenue and expenses related to the property.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2016

NOTE 6 - UNEARNED REVENUE/OPERATING LEASES/OPERATING RENTAL REVENUE (CONTINUED)

In December 2013, the Division entered into agreements with the Boeing Company for the development of a total of approximately 468 acres of land through December 31, 2027 with one six-year and six five-year options to renew. In consideration for the exclusive use of the leased property, the Boeing Company agreed to pay \$1.00 per year for each year of the initial lease term. Additional rent provisions will be applicable for the extension terms. In consideration of the Boeing Company's planned improvements to and use of the property, the Boeing Company will have the option of purchasing the property, including any improvements, for a purchase price equal to the price paid on behalf of the Division to acquire the property. The option to purchase may be exercised at the end of the initial lease term or during any extension term.

Minimum rentals on non-cancelable leases based on current year rates are as follows:

2017	\$ 2,717,664
2018	1,762,011
2019	1,597,326
2020	1,382,640
2021	1,249,069
2022-2026	<u>1,438,277</u>
	<u>\$ 10,146,987</u>

NOTE 7 - LONG-TERM OBLIGATIONS

The following is a summary of changes in long-term obligation activity for the year ended December 31, 2016:

	January 1, 2016	Increases	Decreases	December 31, 2016	Due Within One Year
Compensated absences:					
CHS-NCS	\$ 105,674	123,937	83,844	145,767	\$ 115,655
CCS	134,494	18,581	55,897	97,178	40,388
	<u>240,168</u>	<u>142,518</u>	<u>139,741</u>	<u>242,945</u>	<u>156,043</u>
Note Payable	8,000,000	29,000,000	-	37,000,000	37,000,000
Legal Settlement	2,000,000	-	2,000,000	-	-
TIF Bonds Payable	5,895,000	-	165,000	5,730,000	175,000
Total long-term obligations	<u>\$ 16,135,168</u>	<u>29,142,518</u>	<u>2,304,741</u>	<u>42,972,945</u>	<u>\$ 37,331,043</u>

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 7 – LONG-TERM OBLIGATIONS (CONTINUED)

The note payable represents an interest free loan agreement with the South Carolina Department of Commerce – SC Coordinating Council for Economic Development in an amount not to exceed \$50 million. The loan matures and must be repaid in full by June 30, 2017, but is payable on demand with sixty days written notice from the Coordinating Council or the Division. The loan proceeds are being used for civil work costs related to the Intermodal Container Transfer Facility until the Division secures long-term financing for the project. Once obtained, the proceeds from the long-term financing will be used to repay the loan.

See Notes 14 and 15 for a detail description of the legal settlement and the TIF bonds payable.

NOTE 8 – OTHER REVENUE

The category under "Operating Revenues" entitled "Other Revenue," is used to report miscellaneous income. For the year ended December 31, 2016 it consists of offset charges of \$117,397 received by CHS-NCS from the SCPA - see Note 12.

NOTE 9 – OTHER RENTAL INCOME, NET, NON OPERATING REVENUES

The Division leases several buildings and parking spaces on the former Navy Base. The revenue and expenses for 2016 were as follows:

Rental revenue - Navy Base	\$ 2,646,921
Less: expenses	
Depreciation	387,285
Landscaping and janitorial	291,228
Professional fees	31,773
Utilities	306,999
Maintenance	222,104
Property tax and disposal fees	68,727
Insurance	29,950
Tenant Improvements	32,895
Other Services	56,484
	<u>1,427,445</u>
Net Income	<u>\$ 1,219,476</u>

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS

The Division participates in the State of South Carolina's retirement plans, which are administered by the South Carolina Public Employee Benefit Authority ("PEBA"), which was created on July 1, 2012 and administers the various retirement systems and retirement programs managed by its Retirement Division. PEBA has an 11-member Board of Directors ("PEBA Board"), appointed by the Governor and General Assembly leadership, which serves as co-trustee and co-fiduciary of the systems and the trust funds. By law, the Budget and Control Board (State Fiscal Accountability Authority (SFAA) effective July 1, 2015), which consists of five elected officials, also reviews certain PEBA Board decisions regarding the funding of the South Carolina Retirement Systems ("Systems") and serves as a co-trustee of the Systems in conducting that review.

PEBA issues a Comprehensive Annual Financial Report ("CAFR") containing financial statements and required supplementary information for the System' Pension Trust Funds. The CAFR is publicly available through the Retirement Benefits' link on the PEBA's website at www.peba.sc.gov, or a copy may be obtained by submitting a request to PEBA, PO Box 11960, Columbia, SC 29211-1960. The PEBA is considered a division of the primary government of the State of South Carolina and therefore, retirement trust fund financial information is also included in the comprehensive annual financial report of the state.

Plan Description

The South Carolina Retirement System ("SCRS"), a cost-sharing multiple-employer defined benefit pension plan, was established effective July 1, 1945, pursuant to the provisions of Section 9-1-20 of the South Carolina Code of Laws for the purpose of providing retirement allowances and other benefits for employees of the state, its public school districts, and political subdivisions.

The State Optional Retirement Program ("State ORP") is a defined contribution plan that is offered as an alternative to the SCRS to certain newly hired state, public school, and higher education employees. State ORP participants direct the investment of their funds into a plan administered by one of four investment providers.

The South Carolina Police Officers Retirement System ("PORS"), a cost-sharing multiple-employer defined benefit pension plan, was established effective July 1, 1962, pursuant to the provisions of Section 9-11-20 of the South Carolina Code of Laws for the purpose of providing retirement allowances and other benefits for police officers and firemen of the state and its political subdivisions.

Plan Membership

Membership requirements are prescribed in Title 9 of the South Carolina Code of Laws. A brief summary of the requirements under each system is presented below.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Plan Membership (Continued)

- SCRS - Generally, all employees of covered employers are required to participate in and contribute to the system as a condition of employment. This plan covers general employees and teachers and individuals newly elected to the South Carolina General Assembly beginning with the November 2012 general election. An employee member of the system with an effective date of membership prior to July 1, 2012, is a Class Two member. An employee member of the system with an effective date of membership on or after July 1, 2012 is a Class Three member.

- State ORP – As an alternative to membership in SCRS, newly hired state, public school, and higher education employees and individuals newly elected to the S.C. General Assembly beginning with the November 2012 general election have the option to participate in the State Optional Retirement Program (State ORP), which is a defined contribution plan. State ORP participants direct the investment of their funds into a plan administered by one of four investment providers. PEBA assumes no liability for State ORP benefits. Rather, the benefits are the liability of the investment providers. For this reason, State ORP programs are not part of the retirement systems' trust funds for financial statement purposes. Employee and Employer contributions to the State ORP are at the same rates as SCRS. A direct remittance is required from the employers to the member's account with investment providers for the employee contribution and a portion of the employer contribution (5 percent). A direct remittance is also required to SCRS for the remaining portion of the employer contribution and an incidental death benefit contribution, if applicable, which is retained by SCRS.

- PORS - To be eligible for PORS membership, an employee must be required by the terms of his employment, by election or appointment, to preserve public order, protect life and property, and detect crimes in the state; to prevent and control property destruction by fire; or to serve as a peace officer employed by the Department of Corrections, the Department of Juvenile Justice, or the Department of Mental Health. Probate judges and coroners may elect membership in PORS. Magistrates are required to participate in PORS for service as a magistrate. PORS members, other than magistrates and probate judges, must also earn at least \$2,000 per year and devote at least 1,600 hours per year to this work, unless exempted by statute. An employee member of the system with an effective date of membership prior to July 1, 2012, is a Class Two member. An employee member of the system with an effective date of membership on or after July 1, 2012, is a Class Three member.

Plan Benefits

Benefit terms are prescribed in Title 9 of the South Carolina Code of Laws. PEBA does not have the authority to establish or amend benefit terms without a legislative change in the code of laws. Key elements of the benefit calculation include the benefit multiplier, years of service, and average final compensation. A brief summary of benefit terms for each system is presented below.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Plan Benefits (Continued)

- SCRS - A Class Two member who has separated from service with at least five or more years of earned service is eligible for a monthly pension at age 65 or with 28 years credited service regardless of age. A member may elect early retirement with reduced pension benefits payable at age 55 with 25 years of service credit. A Class Three member who has separated from service with at least eight or more years of earned service is eligible for a monthly pension upon satisfying the Rule of 90 requirement that the total of the member's age and the member's creditable service equals at least 90 years. Both Class Two and Class Three members are eligible to receive a reduced deferred annuity at age 60 if they satisfy the five- or eight-year earned service requirement, respectively. An incidental death benefit is also available to beneficiaries of active and retired members of employers who participate in the death benefit program.

The annual retirement allowance of eligible retirees or their surviving annuitants is increased by the lesser of one percent or five hundred dollars every July 1. Only those annuitants in receipt of a benefit on July 1 of the preceding year are eligible to receive the increase. Members who retire under the early retirement provisions at age 55 with 25 years of service are not eligible for the benefit adjustment until the second July 1 after reaching age 60 or the second July 1 after the date they would have had 28 years of service credit had they not retired.

- PORS - A Class Two member who has separated from service with at least five or more years of earned service is eligible for a monthly pension at age 55 or with 25 years of service regardless of age. A Class Three member who has separated from service with at least eight or more years of earned service is eligible for a monthly pension at age 55 or with 27 years of service regardless of age. Both Class Two and Class Three members are eligible to receive a deferred annuity at age 55 with five or eight years of earned service, respectively. An incidental death benefit is also available to beneficiaries of active and retired members of employers who participate in the death benefit program. Accidental death benefits are also provided upon the death of an active member working for a covered employer whose death was a natural and proximate result of an injury incurred while in the performance of duty.

The retirement allowance of eligible retirees or their surviving annuitants is increased by the lesser of one percent or five hundred dollars every July 1. Only those annuitants in receipt of a benefit on July 1 of the preceding year are eligible to receive the increase.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Plan Contributions

Contributions are prescribed in Title 9 of the South Carolina Code of Laws. Upon recommendation by the actuary in the annual actuarial valuation, the PEBA Board may adopt and present to the SFAA for approval an increase in the SCRS and PORS employer and employee contribution rates, but any such increase may not result in a differential between the employee and total employer contribution rate that exceeds 2.9 percent of earnable compensation for the SCRS and 5 percent for the PORS. An increase in the contribution rates adopted by the PEBA Board may not provide for an increase of more than one-half of one percent in any one year. If the scheduled employee and employer contributions provided in statute or the rates last adopted by the PEBA Board are insufficient to maintain a thirty year amortization schedule of the unfunded liabilities of the plans, the PEBA Board shall increase the contribution rates in equal percentage amounts for the employer and employee as necessary to maintain the thirty-year amortization period; and, this increase is not limited to one-half of one percent per year.

As noted earlier, both employees and the Division are required to contribute to the Plans at rates established and as amended by the PEBA. The Division's contributions are actuarially determined but are communicated to and paid by the Division as a percentage of the employees' annual eligible compensation. Required employer and employee contribution rates for the past three years are as follows:

	SCRS and State ORP Rates				PORS Rates			
	Effective Date				Effective Date			
	7/1/2013	7/1/2014	7/1/2015	7/1/2016	7/1/2013	7/1/2014	7/1/2015	7/1/2016
Employer Rate:								
Retirement *	10.45%	10.75%	10.91%	11.41%	12.44%	13.01%	13.34%	13.84%
Incidental Death Benefit	0.15%	0.15%	0.15%	0.15%	0.20%	0.20%	0.20%	0.20%
Accidental Death Contributions	0.00%	0.00%	0.00%	0.00%	0.20%	0.20%	0.20%	0.20%
	<u>10.60%</u>	<u>10.90%</u>	<u>11.06%</u>	<u>11.56%</u>	<u>12.84%</u>	<u>13.41%</u>	<u>13.74%</u>	<u>14.24%</u>
Employee Rate	<u>7.50%</u>	<u>8.00%</u>	<u>8.16%</u>	<u>8.66%</u>	<u>7.84%</u>	<u>8.41%</u>	<u>8.74%</u>	<u>9.24%</u>

* Of the rate for the State ORP Plan, 5% of earnable compensation must be remitted by the employer direct to the ORP vendor to be allocated to the member's account with the remainder of the employer contribution remitted to the SCRS.

The required contributions and percentages of amounts contributed by the Division to the Plans for the past three years were as follows:

Year Ended December 31,	SCRS Contributions		State ORP Contributions		PORS Contributions	
	Required	% Contributed	Required	% Contributed	Required	% Contributed
2016	\$ 476,541	100%	68,637	100%	\$ 7,695	100%
2015	398,523	100%	51,822	100%	6,947	100%
2014	\$ 318,469	100%	21,989	100%	\$ 6,521	100%

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Plan Contributions (Continued)

Eligible payrolls of the Division covered under the Plans for the past three years were as follows:

Year Ended December 31,	SCRS Payroll	State ORP Payroll	PORS Payroll	Total Payroll
2016	\$ 4,211,589	606,014	55,000	\$ 4,872,603
2015	3,626,806	471,722	51,171	4,149,699
2014	\$ 2,961,075	204,452	49,680	\$ 3,215,207

Actuarial Assumptions and Methods

Actuarial valuations involve estimates of the reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and future salary increases. Actuarial assumptions and methods used during the annual valuation process are subject to periodic revision, typically with an experience study, as actual results over an extended period of time are compared with past expectations and new estimates are made about the future. South Carolina state statute requires that an actuarial experience study be completed at least once in each five-year period. The last experience study was performed on data through June 30, 2015 and was issued as of July 1, 2015.

The June 30, 2016 total pension liability, net pension liability, and sensitivity information were determined by the PEBA's consulting actuary, Gabriel, Roeder, Smith and Company ("GRS") and are based on the July 1, 2015 actuarial valuations as adopted by the PEBA Board and the SFAA which utilized membership data as of July 1, 2015. The total pension liability was rolled-forward from the valuation date to the plan's fiscal year ended June 30, 2016 using generally accepted actuarial principles. Information included in the following schedules is based on the certification provided by GRS.

The following table provides a summary of the actuarial assumptions and methods used in the July 1, 2014, valuations for the SCRS and PORS.

	SCRS	PORS
Actuarial Cost Method	Entry Age Normal	Entry Age Normal
Actuarial Assumptions:		
Investment Rate of Return*	7.50%	7.50%
Projected Salary Increases*	3.5% to 12.5% (varies by service)	4.0% to 10.0% (varies by service)
Benefit Adjustments	Lesser of 1% or \$500 annually	Lesser of 1% or \$500 annually

* Includes inflation at 2.75%.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Actuarial Assumptions and Methods (Continued)

The post-retiree mortality assumption is dependent upon the member’s job category and gender. This assumption includes base rates which are automatically adjusted for future improvement in mortality using published Scale AA projected from the year 2000. Assumptions used in the July 1, 2015 valuations for the SCRS and PORS are as follows:

Former Job Class	Males	Females
Educators and Judges	RP-2000 Males (with White Collar adjustment) multiplied by 110%	RP-2000 Females (with White Collar adjustment) multiplied by 95%
General Employees and Members of the General Assembly	RP-2000 Males multiplied by 100%	RP-2000 Females multiplied by 90%
Public Safety, Firefighters and members of the South Carolina National Guard	RP-2000 Males (with Blue Collar adjustment) multiplied by 115%	RP-2000 Females (with Blue Collar adjustment) multiplied by 115%

Long-term Expected Rate of Return

The long-term expected rate of return on pension plan investments, as used in the July 1, 2015 actuarial valuations, was based upon the 30 year capital markets outlook at the end of the third quarter 2015, as developed by the Retirement Systems Investment Commission (“RSIC”) in collaboration with its investment consultant, Aon Hewitt. The long-term expected rate of returns represent assumptions developed using an arithmetic building block approach, reflecting observable inflation and interest rate information available in the fixed income markets as well as Consensus Economic forecasts. Long-term assumptions for other asset classes are based on historical results, current market characteristics and professional judgment.

The expected returns, along with the expected inflation rate, form the basis for the target asset allocation adopted by the RSIC beginning January 1, 2016. The long-term expected rate of return is produced by weighting the expected future real rates of return by the target allocation percentage and by adding expected inflation and is summarized in the table below. For actuarial purposes, the 7.50 percent assumed annual investment rate of return set in statute and used in the calculation of the total pension liability includes a 4.75 percent real rate of return and a 2.75 percent inflation component.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Long-term Expected Rate of Return (Continued)

Allocation/Exposure	Target Allocation	Expected Arithmetic Real Rate of Return	Long Term Expected Portfolio Real Rate of Return
Global Equity	43.0%		
Global Public Equity	34.0%	6.52%	2.22%
Private Equity	9.0%	9.30%	0.84%
Real Assets	8.0%		
Real Estate	5.0%	4.32%	0.22%
Commodities	3.0%	4.53%	0.13%
Infrastructure	0.0%	6.26%	0.00%
Other Real Assets	0.0%	0.00%	0.00%
Opportunistic	20.0%		
GTAA/Risk Parity	10.0%	3.90%	0.39%
HF (Low Beta)	10.0%	3.87%	0.39%
Diversified Credit	17.0%		
Mixed Credit	5.0%	3.52%	0.17%
Emerging Markets Debt	5.0%	4.91%	0.25%
Private Debt	7.0%	4.47%	0.31%
Other Credit	0.0%	0.00%	0.00%
Conservative Fixed Income	12.0%		
Private Equity	10.0%	1.72%	0.17%
Real Estate (Broad Market)	0.0%	0.00%	0.00%
Commodities	2.0%	0.71%	0.01%
Total Expected Real Return	<u>100.0%</u>		<u>5.10%</u>
Inflation for Actuarial Purposes			<u>2.75%</u>
Total Expected Nominal Return			<u>7.85%</u>

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

The net pension liability (“NPL”) is calculated separately for each system and represents that particular system’s total pension liability determined in accordance with GASB No. 67 less that System’s fiduciary net position. NPL totals, as of June 30, 2016 measurement date, for the SCRS and PORS are presented in the following table:

System	Total Pension Liability	Plan Fiduciary Net Position	Employers' Net Pension Liability (Asset)	Plan Fiduciary Net Position as a Percentage of the Total Pension Liability
SCRS	\$ 45,356,214,752	23,996,362,354	\$ 21,359,852,398	52.9%
PORS	\$ 6,412,510,458	3,876,035,732	\$ 2,536,474,726	60.4%

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Pension Liabilities, Pension Expense, and Deferred Outflows/Inflows of Resources Related to Pensions (Continued)

The total pension liability is calculated by the Systems' actuary, and each plan's fiduciary net position is reported in the Systems' financial statements. The net pension liability is disclosed in accordance with the requirements of GASB No. 67 in the Systems' notes to the financial statements and required supplementary information. Liability calculations performed by the Systems' actuary for the purpose of satisfying the requirements of GASB Nos. 67 and 68 are not applicable for other purposes, such as determining the plans' funding requirements.

At December 31, 2016, the Division reported liabilities of approximately \$9,614,000 and \$106,000 for its proportionate share of the net pension liabilities for the SCRS and PORS ("Plans"), respectively. The net pension liabilities were measured as of June 30, 2016, and the total pension liabilities for the Plans used to calculate the net pension liabilities were determined based on the most recent actuarial valuation report as of July 1, 2015 that was projected forward to the measurement date. The Division's proportion of the net pension liabilities were based on a projection of the Division's long-term share of contributions to the Plans relative to the projected contributions of all participating South Carolina state and local governmental employers, actuarially determined. At the June 30, 2016 measurement date, the Division's SCRS proportion was 0.04501 percent, which was an increase of 0.00934 percent from its proportion measured as of June 30, 2015. At the June 30, 2016 measurement date, the Division's PORS proportion was 0.00416 percent, which was an increase of 0.00009 percent from its proportion measured as of June 30, 2015.

For the year ended December 31, 2016, the Division recognized pension expense of approximately \$1,463,000 and \$12,000 for the SCRS and PORS, respectively. At December 31, 2016, the Division reported deferred outflows of resources (deferred pension charges) and deferred inflows of resources (deferred pension credits) related to pensions from the following sources:

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

**Pension Liabilities, Pension Expense, and Deferred Outflows/Inflows of Resources
Related to Pensions (Continued)**

Description	Deferred Outflows of Resources	Deferred Inflows of Resources
SCRS		
Differences Between Expected and Actual Experience	\$ 99,657	\$ 10,440
Net Difference Between Projected and Actual Earnings on Pension Plan Investments	808,816	-
Changes in Proportionate Share and Differences Between Employer Contributions and Proportionate Share of Total Plan Employer Contributions	1,712,700	-
The Division's Contributions Subsequent to the Measurement Date	269,434	-
Total SCRS	<u>2,890,607</u>	<u>10,440</u>
PORS		
Differences Between Expected and Actual Experience	1,567	-
Net Difference Between Projected and Actual Earnings on Pension Plan Investments	11,976	-
Changes in Proportionate Share and Differences Between Employer Contributions and Proportionate Share of Total Plan Employer Contributions	1,661	-
The Division's Contributions Subsequent to the Measurement Date	3,916	-
Total PORS	<u>19,120</u>	<u>-</u>
Total SCRS and PORS	<u>\$ 2,909,727</u>	<u>\$ 10,440</u>

Approximately \$269,000 and \$4,000 that were reported as deferred outflows of resources related to the Division's contributions subsequent to the measurement date to the SCRS and PORS, respectively, will be recognized as a reduction of the net pension liabilities in the year ended December 31, 2017. Other amounts reported as deferred outflows of resources (deferred pension charges) and deferred inflows of resources (deferred pension credits) related to the SCRS and PORS will increase (decrease) pension expense as follows:

Year Ended June 30,	SCRS	PORS	Total
2017	\$ 829,529	3,511	\$ 833,040
2018	777,438	3,432	780,870
2019	773,146	5,246	778,392
2020	230,620	3,015	233,635
Total	<u>\$ 2,610,733</u>	<u>15,204</u>	<u>\$ 2,625,937</u>

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Discount Rate

The discount rate used to measure the total pension liability was 7.50 percent. The projection of cash flows used to determine the discount rate assumed that the funding policy specified in the South Carolina State Code of Laws will remain unchanged in future years. Based on those assumptions, each System's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

The following table presents the sensitivity of the Division's proportionate share of the net pension liability of the Plans to changes in the discount rate, calculated using the discount rate of 7.50 percent, as well as what it would be if it were calculated using a discount rate that is 1.00 percent lower (6.50 percent) or 1.00 percent higher (8.50 percent) than the current rate:

System	1.00% Decrease (6.50%)	Current Discount Rate (7.50%)	1.00% Increase (8.50%)
The Division's proportionate share of the net pension liability of the SCRS	\$ 11,992,756	9,613,642	\$ 7,633,120
The Division's proportionate share of the net pension liability of the PORS	138,422	105,619	76,139
Total Pension Liability	<u>\$ 12,131,178</u>	<u>9,719,261</u>	<u>\$ 7,709,259</u>

Plans Fiduciary Net Position

Detailed information regarding the fiduciary net position of the Plans administered by the PEBA is available in the separately issued CAFR containing financial statements and required supplementary information for the SCRS and PORS. The CAFR is publicly available through the Retirement Benefits' link on the PEBA's website at www.peba.sc.gov, or a copy may be obtained by submitting a request to PEBA, PO Box 11960, Columbia, SC 29211-1960.

Payable to Plans

The Division reported payables of approximately \$106,000 and \$1,000 to the PEBA as of December 31, 2016, representing required employer and employee contributions for the month of December 2016 for the SCRS and PORS, respectively. These amounts are included in Accounts Payable on the financial statements and were paid in January 2017.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 10 - PENSION PLANS AND EMPLOYEE BENEFIT PLANS (CONTINUED)

Railroad Retirement System

The Division contributed \$1,021,194 this year to the U.S. Railroad Retirement System, which covers all employees. CHS-NCS contributed \$685,127 and CCS \$336,067. Participation is mandatory. This program is a two-tier system, which is funded, based on each employee's gross annual wages. Effective January 1, 2016, wages up to \$118,500 were funded at 6.2 percent by the Division and 6.2 percent by the employee to meet Tier I funding requirements and all wages were funded at 1.45 percent by the Division to meet Tier I Medicare funding requirements. The Division funded wages up to \$88,200 at 13.1 percent to meet Tier II funding requirements. Employees paid 4.9 percent on wages up to \$88,200.

The U. S. Railroad Retirement Board, in accordance with the Railroad Retirement Acts, administers this plan.

Data concerning the actuarial status of the U.S. Railroad Retirement System as related to the Division is not available. The Division is not liable for any unfunded costs associated with the plan and recognized no contingent liability for such cost.

NOTE 11 - OTHER POSTEMPLOYMENT BENEFITS

In accordance with the South Carolina Code of Laws and the annual Appropriations Act, the State of South Carolina ("State") provides health, dental, and long-term disability benefits ("OPEB Plan") to retired State and school district employees and their covered dependents. The Division contributes to the South Carolina Retiree Health Insurance Trust Fund ("SCRHITF") and the South Carolina Long-Term Disability Insurance Trust Fund ("SCLTDITF"), cost-sharing multiple-employer defined benefit postemployment healthcare and long-term disability plans administered by the Insurance Benefits Division ("IB"), a part of the South Carolina Public Employee Benefit Authority ("PEBA").

Generally, retirees are eligible for the health and dental benefits if they have established at least ten years of retirement service credit. For new hires on May 2, 2008 and after, retirees are eligible for benefits if they have established twenty-five years of service for 100% employer funding and fifteen through twenty-four years of service for 50% employer funding. Benefits become effective when the former employee retires under a State retirement system. Basic long-term disability ("BLTD") benefits are provided to active State, public school district and participating local government employees approved for disability.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 11 – OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Section 1-11-710 of the South Carolina Code of Laws of 1976, as amended, requires these postemployment and long-term disability benefits be funded through annual appropriations by the State General Assembly for active employees to the IB and participating retirees to the PEBA, except the portion funded through the pension surcharge and provided from other applicable sources of the IB, for its active employees who are not funded by State General Fund appropriations. Employers participating in the SCRHITF are mandated by State statute to contribute at a rate assessed each year by the Office of the State Budget, 5.33% of annual covered payroll effective July 1, 2016, 5.33% of annual covered payroll effective July 1, 2015, 5.00% of annual covered payroll effective July 1, 2014, and 4.92% of annual covered payroll effective July 1, 2013. The actual required employer contribution surcharge amounts were approximately \$260,000, \$215,000, and \$160,000 for the years ended December 31, 2016, 2015, and 2014, respectively. The actual contribution rates and amounts were 100% of the required employer contribution surcharge percentages and amounts for the OPEB Plan for all years presented. The IB sets the employer contribution rate based on a pay-as-you-go basis. BLTD benefits are funded through a person's premium charged to State agencies, public school districts, and other participating local governments. The monthly premium per active employee paid to IB was \$3.22 for the years ended December 31, 2016, 2015, and 2014.

Effective May 1, 2008 the State established two trust funds through Act 195 for the purpose of funding and accounting for the employer costs of retiree health and dental insurance benefits and long-term disability insurance benefits. The SCRHITF is primarily funded through the payroll surcharge. Other sources of funding include additional State appropriated dollars, accumulated IB reserves, and income generated from investments. The SCLTDITF is primarily funded through investment income and employer contributions.

A copy of the complete financial statements for the benefit plans and the trust funds may be obtained from the South Carolina Public Employee Benefit Authority – Insurance Benefits Division, P.O. Box 11960, Columbia, SC 29211-1960.

NOTE 12 - TRANSACTIONS WITH STATE ENTITIES

During 2015, the Division entered into an interest free loan agreement with the South Carolina Department of Commerce – SC Coordinating Council for Economic Development in an amount not to exceed \$50 million. The loan matures and must be repaid in full by June 30, 2017, but is payable on demand with sixty days written notice from the Coordinating Council or the Division. The loan proceeds are being used for civil work costs related to the Intermodal Container Transfer Facility until the Division secures long-term financing for the project. Once obtained, the proceeds from the long-term financing will be used to repay the loan. See Note 7 regarding long-term obligations.

The SCPA pays CHS-NCS monthly offset charges. In 1988, the SCPA took possession of a certain area of trackage at the Port Terminal Railroad which caused CHS-NCS to incur additional operating costs. The SCPA continues to pay CHS-NCS for the additional costs, which equals the initial annual base amount of \$58,615 adjusted for changes in the consumer price index. The amount paid to CHS-NCS was \$117,397 in 2016 and is included in other operating revenues. See Note 8 regarding other revenue.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 12 - TRANSACTIONS WITH STATE ENTITIES (CONTINUED)

Services received at no cost from State agencies include banking and investment functions from the State Treasurer and retirement and insurance plan administration from the PEBA. The Division had financial transactions with various State agencies during the year. Payments made in 2016 to the State Fiscal Accountability Authority were primarily for insurance coverage.

NOTE 13 - OPERATING LEASES

The Division and the SCPA entered into an agreement, effective July 1, 1976, allowing the Division to lease the building known as the Shore Patrol Office for a period of twenty (20) years. The Division is now occupying these premises on a month-to-month lease. The monthly rental charge is \$300. The Division incurred \$3,600 for rental of this building in 2016. The Division is required to carry insurance for property damage and to maintain and repair the leased building. This amount is included in general administration expenses.

NOTE 14 - SETTLEMENT AGREEMENT AND RELEASE

On December 5, 2012 the Division, the City of North Charleston (“North Charleston”) and the North Charleston Sewer District (“Sewer District”) agreed to sign the Settlement Agreement and Release (the “Agreement”) to settle and release six civil actions in which North Charleston or the Sewer District were the plaintiff and the Division was the defendant. The effective date of the agreement was March 25, 2013, the date on which the consent order was entered adopting and incorporating the terms of the Agreement. The Agreement was necessary to obtain land in order for the Division to plan and construct an Intermodal Container Transfer Facility on the former Navy Base.

The terms of the agreement are as follows:

1. The Division will pay North Charleston \$8,000,000 over 4 years to mitigate rail access impacts. The first payment of \$2,000,000 was made on March 23, 2013. Thereafter, the \$2,000,000 payments will be made no later than the anniversary date of the first payment in 2014, 2015 and 2016. This has been paid in full as of December 31, 2016.
2. The Division will assume approximately \$6,500,000 in TIF Bonds for the Navy Base Redevelopment Project. See Note 15.
3. The Division will transfer to North Charleston certain buildings and land on the former Navy Yard as soon as practicable after the effective date.
4. North Charleston will transfer to the Division certain buildings and land on the former Navy Yard as soon as practicable after the effective date.
5. Before December 31, 2017, the Division will transfer to North Charleston additional buildings and land on the former Navy Yard.
6. Before December 31, 2017, North Charleston will transfer to the Division additional buildings and land on the former Navy Base.

In August 2014, the first round of transfers noted above in 3. and 4. occurred. The Division transferred approximately \$6,035,000 of land, buildings and deferred rent to the City of North Charleston and the Division received land and buildings from the City of the same approximate value.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 15 – NONCURRENT LIABILITY – TIF BONDS

As part of the Settlement Agreement and Release, see Note 14, the Division assumed responsibility for payment of \$6,360,000 in TIF Bonds from the City of North Charleston. Principal and interest is payable in annual installments beginning September 2013 through September 2037 with variable interest (.43% at June 30, 2016), as determined by the remarketing agent, payable each month. The balance outstanding at December 31, 2016 was \$5,730,000.

Future principal payments of the bonds are as follows:

2017	\$ 175,000
2018	180,000
2019	190,000
2020	195,000
2021	205,000
2022-2026	1,175,000
2027-2031	1,435,000
2032-2036	1,775,000
2037	<u>400,000</u>
Total	<u>\$ 5,730,000</u>

NOTE 16 - RISK MANAGEMENT

The Division is exposed to various risks of loss and maintains State or commercial insurance coverage for certain risks. Management believes such coverage is sufficient to preclude any significant uninsured losses to the Division. Settled claims have not exceeded this coverage in any of the past three years. There were no significant reductions in insurance coverage from coverage in the prior year. The Division pays insurance premiums to certain other State agencies and commercial insurers to cover risks that may occur in normal operations. The insurers promise to pay to or on behalf of the insured for covered losses sustained during the policy period in accord with the insurance policy and benefit program limits. State management believes it is more economical to manage certain risks internally and set aside assets for claim settlement. Several State funds accumulate assets and the State itself assumes substantially all risks for the following:

1. Claims of covered public employees for health and dental insurance benefits (PEBA – Insurance Benefits Division); and
2. Claims of covered public employees for long-term disability and group-life insurance benefits (PEBA – Insurance Benefits Division).

Employees elect health coverage through either a health maintenance organization or through the State’s self-insured plan. All of the other coverages listed above are through the applicable State self-insured plan except dependent and optional life premiums which are remitted to commercial carriers.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 16 - RISK MANAGEMENT (CONTINUED)

The Division and other entities pay premiums to the State's Insurance Reserve Fund ("IRF") which issues policies, accumulate assets to cover the risks of loss and pays claims incurred for covered losses related to the following Division assets, activities, and/or events.

1. Real property, its contents and other equipment - Coverage per loss for real property is based on current valuation with a \$250 deductible. Eighty percent of each loss is covered by the IRF.
2. Motor vehicles - Coverage is up to \$1,000,000 per loss with a \$500 deductible for comprehensive coverage and \$500 for collision.
3. Torts

The IRF is a self-insurer and purchases reinsurance to obtain certain services and specialized coverage and to limit losses in the areas of property, boiler and machinery, and automobile liability. The IRF's rates are determined actuarially.

State agencies are the primary participants in the PEBA – Insurance Benefits Division and in IRF.

The Division purchases insurance, which covers all subdivisions, through private carriers for liability and property loss on road and locomotive assets, and employee fidelity bond insurance coverage for all employees to cover losses of up to \$100,000 arising from theft or misappropriations. Management believes based on exposure and likelihood of loss that this coverage is sufficient.

The Division has purchased insurance, which covers all divisions, from a private carrier for liability under the Federal Employers Liability Act (FELA), which is similar to workmen's compensation insurance and covers all employees. The Division has elected to retain the risk of loss on this coverage for up to the first \$100,000 of costs per claim. Management has elected to retain this amount of risk because it feels that it is more economical than paying additional premiums for increased coverage. In the current year, no expenses were incurred on claims under the policy. Also a tax is paid to the U.S. Railroad Retirement System to cover all the Division employees for unemployment benefits. The Division has recorded insurance premium expenses in the applicable operating department corresponding to the employees for whom contributions are made or in insurance expense under administrative costs.

The Division's management believes risk of loss from business interruption is a remote likelihood, however the Division does have \$250,000 coverage through their equipment liability coverage policy for this risk.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 16 - RISK MANAGEMENT (CONTINUED)

The Division did not incur any significant losses in 2016 for self-insured risks. Also, no reserves have been established for potential losses for self-insured risks. The Division reports such expenses if information prior to issuance of the financial statement indicates that it is probable that an asset has been impaired or a liability has been incurred on or before fiscal year end and the amount is reasonably estimable. The recorded expense is valued at an estimate of the ultimate cost of settling the claim or of the asset loss.

NOTE 17 - COMMITMENTS, CONTINGENCIES AND LITIGATION

The Division is party to a number of civil lawsuits and other legal proceedings. At the current time management and legal counsel are unable to determine any ultimate outcome of existing and potential legal actions. The Division has undertaken condemnation actions on certain properties in connection with the Intermodal Container Transfer Facility to be constructed in North Charleston, South Carolina. The Division has determined just compensation in the outstanding condemnation actions to be in excess of \$14,400,000; however, the Division anticipates the resolution of the condemnation actions will involve exchanges of land in lieu of cash. In addition, the Division has begun condemnation actions on several properties that have been filed in the amount of approximately \$689,000, several condemnation actions are in pre-filing totaling approximately \$120,000, and anticipated condemnation cases are expected to be approximately \$6,930,000. The Division is also responsible for the construction of a new pump station for the North Charleston Sewer District that is being relocated for the Intermodal Container Transfer Facility. The construction of the new pump station is estimated to cost approximately \$6,681,000.

On October 18, 2016, Palmetto Railways signed a Memorandum of Agreement (MOA) with the Chicora-Cherokee Neighborhood Association, The Union Heights Community Council, The Lowcountry Alliance for Model Communities, and the Metanoia Community Development Corporation to take certain mitigation and enhancement actions that will reduce, avoid or offset potential impacts associated with the Intermodal Container Transfer Facility being built close to these communities. The MOA is contingent upon Palmetto Railways receiving all permits and records of decision necessary to begin construction of the facility. Palmetto Railways will fund \$3,000,000 to build a new recreation center and an additional \$1,000,000 over nine years to fund various community programs in the affected communities.

In September 2016, the Division entered into a lease agreement with the Hampton and Branchville Railroad Company to lease track for the storage of empty railcars. As part of the agreement, the Division has agreed to pay 25 percent of gross revenues earned during the lease to the Hampton and Branchville Railroad Company. The lease expires upon the closing date of the asset and purchase sale agreement between the Division and the Hampton and Branchville Railroad Company, which is anticipated to close in May 2017.

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2016

NOTE 18 – ENTERPRISE FUND INFORMATION

Charges for services	\$ 17,761,659
Capital grant and contributions	18,936,802
Less: expenses	<u>(15,079,978)</u>
Net program revenue	<u>21,618,483</u>
Interest income and gain (loss) on sale of investments	15,596
Miscellaneous revenue	205,337
Gain (loss) on sale or disposal of fixed assets	<u>12,605</u>
Net general revenue	<u>233,538</u>
Change in net position	<u>21,852,021</u>
Net position – beginning of year	<u>189,550,718</u>
Net position – end of year	<u>\$ 211,402,739</u>

This information is included only for the State of South Carolina GAAP reporting purposes and includes terminology and classifications which are not consistent with the financial statements.

NOTE 19 – INTERFUND BALANCES

Interfund balances at December 31, 2016 (which are expected to be received or paid within one year), consisted of the following individual fund receivables and payables:

Fund	Receivables	Payables
CHS-NCS	\$ 683,412	\$ -
CCS	-	683,412
Totals	<u>\$ 683,412</u>	<u>\$ 683,412</u>

The receivables and payables are primarily the result of expenses for CCS being paid using the CHS-NCS cash account. These interfund receivables and payables were relieved subsequent to December 31, 2016.

NOTE 20 – INTERFUND TRANSFERS

Transfers from (to) other funds for the year ended December 31, 2016 consisted of the following:

Fund	Transfers from	Transfers to
CHS-NCS	\$ 2,000,000	\$ -
CCS	-	2,000,000
Totals	<u>\$ 2,000,000</u>	<u>\$ 2,000,000</u>

PALMETTO RAILWAYS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE 20 – INTERFUND TRANSFERS (CONTINUED)

These transfers were made in order to help fund operations of the CHS-NCS Division.

NOTE 21 – SUBSEQUENT EVENTS

On March 9, 2017, the Division signed an Asset Purchase and Sale Agreement with Hampton & Branchville Railroad Company to purchase the railroad and related assets of a 45+ mile railroad in Hampton and Colleton County for \$6,500,000.

On March 2, 2017, the Division sold 9.3 acres of land in North Charleston for \$2,100,000.

PALMETTO RAILWAYS

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF PALMETTO RAILWAYS' PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
SOUTH CAROLINA RETIREMENT SYSTEM**

LAST THREE FISCAL YEARS

	Year Ended December 31,		
	2016	2015	2014
Palmetto Railways' Proportion of the Net Pension Liability	0.04501%	0.03567%	0.03140%
Palmetto Railways' Proportionate Share of the Net Pension Liability	\$ 9,613,642	6,765,556	\$ 5,406,556
Palmetto Railways' Covered-Employee Payroll	\$ 4,064,539	3,157,875	\$ 2,748,612
Palmetto Railways' Proportionate Share of the Net Pension Liability as a Percentage of its Covered-Employee Payroll	236.52%	214.24%	196.70%
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	52.906%	56.992%	59.919%

Notes to Schedule:

The amounts presented for each fiscal year were determined as of June 30th of the year presented. Only three years of data were available; thus, only three years were presented.

PALMETTO RAILWAYS

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF PALMETTO RAILWAYS' CONTRIBUTIONS
SOUTH CAROLINA RETIREMENT SYSTEM**

LAST THREE FISCAL YEARS

	Year Ended December 31,		
	2016	2015	2014
Contractually Required Contribution	\$ 514,877	426,759	\$ 330,236
Contributions in Relation to the Contractually Required Contribution	514,877	426,759	330,236
Contribution Deficiency (Excess)	<u>\$ -</u>	<u>-</u>	<u>\$ -</u>
Palmetto Railways' Covered-Employee Payroll	\$ 4,211,589	3,626,806	\$ 2,961,075
Contributions as a Percentage of Covered-Employee Payroll	12.23%	11.77%	11.15%

Notes to Schedule:

Only three years of data were available; thus, only three years were presented.

PALMETTO RAILWAYS

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF PALMETTO RAILWAYS' PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
POLICE OFFICERS RETIREMENT SYSTEM**

LAST THREE FISCAL YEARS

	Year Ended December 31,		
	2016	2015	2014
Palmetto Railways' Proportion of the Net Pension Liability	0.00416%	0.00407%	0.00406%
Palmetto Railways' Proportionate Share of the Net Pension Liability	\$ 105,619	88,706	\$ 77,745
Palmetto Railways' Covered-Employee Payroll	\$ 53,086	50,425	\$ 48,840
Palmetto Railways' Proportionate Share of the Net Pension Liability as a Percentage of its Covered-Employee Payroll	198.96%	175.92%	159.18%
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	60.44%	64.57%	67.55%

Notes to Schedule:

The amounts presented for each fiscal year were determined as of June 30th of the year presented. Only three years of data were available; thus, only three years were presented.

PALMETTO RAILWAYS

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF PALMETTO RAILWAYS' CONTRIBUTIONS
POLICE OFFICERS RETIREMENT SYSTEM**

LAST THREE FISCAL YEARS

	Year Ended December 31,		
	2016	2015	2014
Contractually Required Contribution	\$ 7,695	6,947	\$ 6,521
Contributions in Relation to the Contractually Required Contribution	7,695	6,947	6,521
Contribution Deficiency (Excess)	<u>\$ -</u>	<u>-</u>	<u>\$ -</u>
Palmetto Railways' Covered-Employee Payroll	\$ 55,000	51,171	\$ 49,680
Contributions as a Percentage of Covered-Employee Payroll	13.99%	13.58%	13.13%

Notes to Schedule:

Only three years of data were available; thus, only three years were presented.



**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

Mr. George L. Kennedy, CPA
 State Auditor
 Office of the State Auditor
 Columbia, South Carolina

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the South Carolina Department of Commerce – Division of Public Railways d/b/a Palmetto Railways (the “Division”) as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the Division’s basic financial statements, and have issued our report thereon dated April 12, 2017.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

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

Purpose of this Report

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



Greene, Finney & Horton, LLP
Mauldin, South Carolina
April 12, 2017