

Office of State Treasurer

BISMARCK, NORTH DAKOTA

Audit Report

For the Biennium Ended
June 30, 2017

Joshua C. Gallion
State Auditor



Office of the State Auditor
Division of State Audit

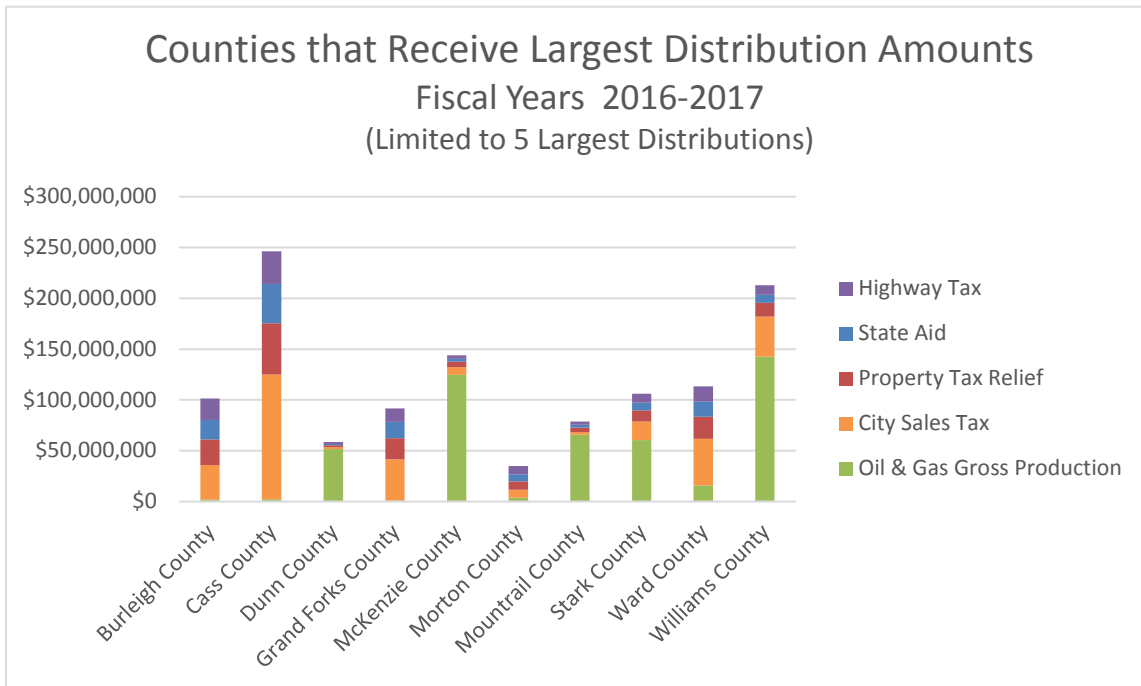
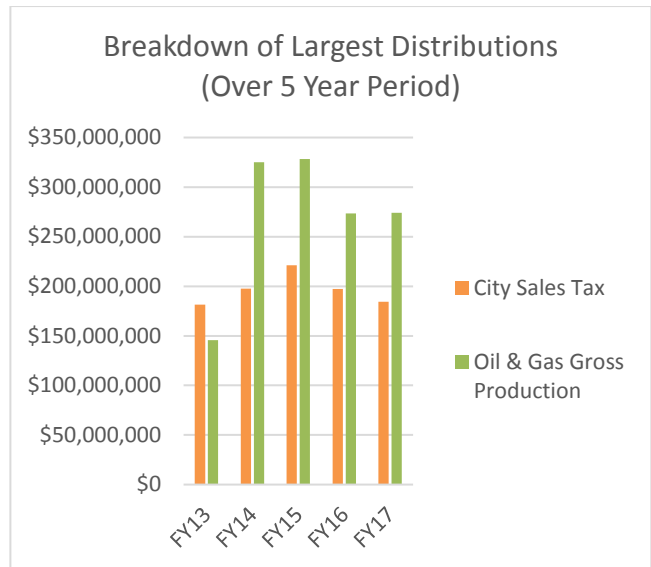
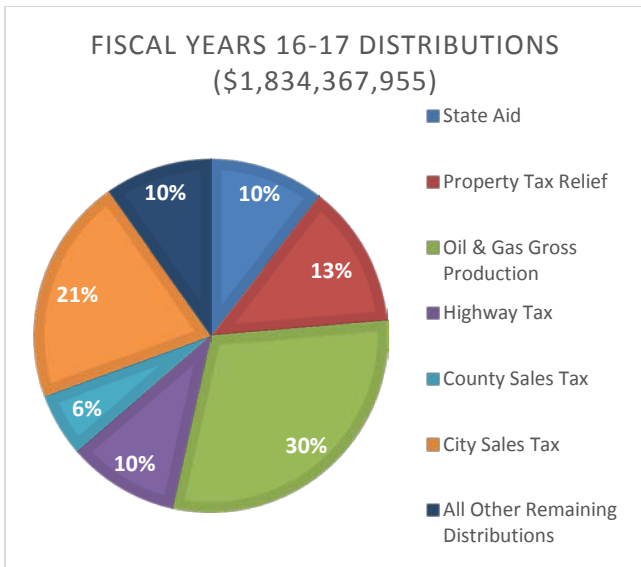
Office of the State Auditor

State Treasurer Report Highlights

Internal Control and Legislative Intent: We evaluated and tested high-risk areas of internal control and legislative intent. We did not note any deficiencies that are required to be brought to the attention of those charged with governance.

Financial:

- One of the biggest financial changes was a decrease in transfers in, which was primarily caused by the decline in oil and gas taxes collected by the State Tax Department.
- Investment earnings also decreased from fiscal year 2016 to 2017, primarily due to a loss on sale of investments and a decline in the market value of the legacy fund.



Source: Office of the State Treasurer's website.

**LEGISLATIVE AUDIT AND FISCAL REVIEW
COMMITTEE MEMBERS**

**Senator Jerry Klein – Chairman
Representative Chet Pollert – Vice Chairman**

Representatives

**Bert Anderson
Patrick Hatlestad
Mary Johnson
Keith Kempenich
Gary Kreidt
Andrew G. Maragos
Mike Nathe
Marvin E. Nelson
Wayne A. Trottier**

Senators

**Dwight Cook
Judy Lee
Richard Marcellais**

AUDITOR AND AGENCY PERSONNEL

State Auditor Personnel

**Cindi Pedersen, CPA, CM, Audit Manager
Krista Lambrecht, CPA, M.Acc, In-Charge
Elizabeth Rogers, Staff Auditor
Delan Hellman, Staff Auditor**

State Treasurer Contacts

**Kelly Schmidt, State Treasurer
Ryan Skor, CPA, Director of Finance**

Contents

<i>Transmittal Letter</i>	<i>1</i>
<i>Executive Summary</i>	<i>2</i>
<i>Introduction</i>	<i>2</i>
<i>Responses to LAFRC Audit Questions</i>	<i>2</i>
<i>LAFRC Audit Communications</i>	<i>3</i>
<i>Audit Objectives, Scope, and Methodology</i>	<i>4</i>
<i>Financial Statements</i>	<i>6</i>
<i>Statement of Revenues and Expenditures</i>	<i>6</i>
<i>Statement of Appropriations</i>	<i>7</i>
<i>Internal Control</i>	<i>9</i>
<i>Compliance with Legislative Intent</i>	<i>10</i>
<i>Operations</i>	<i>12</i>



STATE OF NORTH DAKOTA
OFFICE OF THE STATE AUDITOR
STATE CAPITOL
600 E. BOULEVARD AVENUE – DEPT 117
BISMARCK, NORTH DAKOTA 58505

Transmittal Letter

March 23, 2018

Members of the North Dakota Legislative Assembly
The Honorable Kelly Schmidt, State Treasurer

We are pleased to submit this audit of the Office of the State Treasurer for the biennium ended June 30, 2017. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

Cindi Pedersen, CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 328-2241. We wish to express our appreciation to Treasurer Schmidt and her staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

/S/

Joshua C. Gallion
State Auditor

Executive Summary

Introduction

The Office of State Treasurer receives and keeps all monies belonging to the state not required to be received or kept by another state entity. The Office of State Treasurer is responsible for the investment of certain special funds, as well as several trust funds, including the Veteran's Postwar Trust Fund.

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies. Those items and the Office of the State Auditor's responses are noted below.

Responses to LAFRC Audit Questions

1. What type of opinion was issued on the financial statements?

Financial statements were not prepared by the Office of the State Treasurer in accordance with generally accepted accounting principles, so an opinion is not applicable. The agency's transactions were tested and included in the state's basic financial statements on which an unmodified opinion was issued.

2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?

Yes.

3. Was internal control adequate and functioning effectively?

Yes.

4. Were there any indications of lack of efficiency in financial operations and management of the agency?

No.

5. Has action been taken on findings and recommendations included in prior audit reports?

There were no recommendations included in the prior audit report.

6. Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.

No, a management letter was not issued.

LAFRC Audit Communications

7. *Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.*

There were no significant changes in accounting policies, management conflicts of interest, contingent liabilities, or significant unusual transactions identified.

8. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

The Office of the State Treasurer's financial statements do not include any significant accounting estimates.

9. *Identify any significant audit adjustments.*

Significant audit adjustments were not necessary.

10. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

11. *Identify any serious difficulties encountered in performing the audit.*

None.

12. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

13. *Identify any management consultations with other accountants about auditing and accounting matters.*

None.

14. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance, Human Resource Management System (HRMS) and Tax Distribution and Outstanding Checks (TDOC) are high-risk information technology systems critical to the Office of State Treasurer.

Audit Objectives, Scope, and Methodology

Audit Objectives

The objectives of this audit of the Office of the State Treasurer for the biennium ended June 30, 2017 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the highest risk areas of the Office of the State Treasurer's operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to the Office of the State Treasurer and are they in compliance with these laws?
3. Are there areas of the Office of the State Treasurer's operations where we can help to improve efficiency or effectiveness?

Audit Scope

This audit of the Office of the State Treasurer is for the biennium ended June 30, 2017. We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The Office of the State Treasurer's sole location is its Bismarck office which was included in the audit scope.

Audit Methodology

To meet the objectives outlined above, we:

- Prepared financial statements from the legal balances on the state's accounting system tested as part of this audit and the audit of the state's Comprehensive Annual Financial Report.
- Performed detailed analytical procedures including computer-assisted auditing techniques. These procedures were used to identify high-risk transactions and potential problem areas for additional testing.
- Tested internal control and compliance with laws and regulations which included selecting representative samples to determine if controls were operating effectively and to determine if laws were being followed consistently. Non-statistical sampling was used and the results were projected to the population. Where applicable, populations were stratified to ensure that particular groups within a population were adequately represented in the sample, and to improve efficiency by gaining greater control on the composition of the sample.

- Interviewed appropriate agency personnel.
- Queried the ConnectND (PeopleSoft) system. Significant evidence was obtained from ConnectND.
- Observed the Office of the State Treasurer's processes and procedures.

In aggregate, there were no significant limitations or uncertainties related to our overall assessment of the sufficiency and appropriateness of audit evidence.

Financial Statements

Statement of Revenues and Expenditures

	<u>June 30, 2017</u>	<u>June 30, 2016</u>
<u>Revenues and Other Sources:</u>		
Investment Earnings	\$50,485,926	\$104,917,716
Mineral Lease Royalties	39,124,392	32,287,439
Fines and Court Fees	11,200,719	13,092,904
Mill Profits	4,616,603	4,434,894
General Property Tax	4,401,124	3,909,546
Miscellaneous Revenue	48,302	50,543
Transfers In	777,812,316	954,398,960
Total Revenues and Other Sources	<u>\$887,689,382</u>	<u>\$1,113,092,002</u>
<u>Expenditures and Other Uses:</u>		
Tax Distributions to Government Units	\$773,713,120	\$768,741,623
Other Distributions	2,187,907	2,558,923
Salaries and Benefits	649,068	678,413
IT – Data Processing	72,165	114,453
Professional Services	46,782	30,790
Other Operating Expenditures	25,931	22,023
Transfers Out	1,548,999,505	1,574,919,794
Total Expenditures and Other Uses	<u>\$2,325,694,478</u>	<u>\$2,347,066,019</u>

Statement of Appropriations

For the Biennium Ended June 30, 2017

Expenditures by Line Item:	Original <u>Appropriation</u>	<u>Adjustments</u>	Final <u>Appropriation</u>	<u>Expenditures</u>	Unexpended <u>Appropriation</u>
Salaries and Benefits	\$ 1,427,333	\$ 2,080	\$ 1,429,413	\$ 1,327,481	\$ 101,932
Operating Expenses	266,313		266,313	227,616	38,697
Technology Project Carryover		15,000	15,000	3,709	11,291
Coal Severance Payments	228,952		228,952	228,952	
Township Allocation	7,676,000		7,676,000	7,675,989	11
Property Tax Relief Credits	233,425,000	8,100,000	241,525,000	241,162,655	362,345
Totals	<u>\$ 243,023,598</u>	<u>\$ 8,117,080</u>	<u>\$251,140,678</u>	<u>\$250,626,402</u>	<u>\$ 514,276</u>
Expenditures by Source:					
General Fund	\$ 243,023,598	\$ 17,080	\$243,040,678	\$242,526,402	\$ 514,276
Other Funds		8,100,000	8,100,000	8,100,000	
Totals	<u>\$ 243,023,598</u>	<u>\$ 8,117,080</u>	<u>\$251,140,678</u>	<u>\$250,626,402</u>	<u>\$ 514,276</u>

Expenditures without Appropriations of Specific Amounts:

Transfers from the General Fund to the Lignite Research Fund, authorized by NDCC section 57-61-01.5 (\$2,446,273 of expenditures for this biennium).

Transfers from the General Fund to the Senior Citizens Services and Programs Fund as authorized by NDCC section 57-39.2-26.2 (\$6,797,666 of expenditures for this biennium).

Transfers from the General Fund to the Coal Conversion Tax Trust Fund as authorized by NDCC section 57-60-14(2) (\$1,726,467 of expenditures for this biennium).

Senior Citizens Services and Programs Fund has a continuing appropriation authorized by NDCC section 57-39.2-26.2 (\$6,797,666 of expenditures for this biennium).

Jobs Training Program Fund has a continuing appropriation authorized by NDCC section 52-02.1-03(2) (\$3,044,664 of expenditures for this biennium).

Federal Mineral Royalties Fund has a continuing appropriation authorized by NDCC section 15.1-27-25 (\$27,962,868 of expenditures for this biennium).

Highway Tax Distribution Fund has a continuing appropriation authorized by NDCC section 54-27-19 (\$565,566,170 of expenditures for this biennium).

State Aid Distribution Fund has a continuing appropriation authorized by NDCC section 57-39.2-26.1 (\$185,530,100 of expenditures for this biennium).

Veterans Postwar Trust Fund has a continuing appropriation authorized by NDCC section 34-14-14 (\$80,820 of expenditures for this biennium).

Prepaid Wireless 911 Fee Fund has a continuing appropriation authorized by NDCC section 57-40.6-15 (\$1,702,166 of expenditures for this biennium).

Coal Severance Tax Distribution Fund has a continuing appropriation authorized by NDCC section 57-61-10 (\$21,976,722 of expenditures for this biennium).

Federal Tax Replacement Fund has a continuing appropriation authorized by NDCC section 15.1-24-24 (\$12,695,347 of expenditures for this biennium).

Cigarette Tax Distribution Fund has a continuing appropriation authorized by NDCC section 57-36-31 (\$3,280,266 of expenditures for this biennium).

Telecommunications Carriers Fund has a continuing appropriation authorized by NDCC section 57-34-05 (\$16,800,000 of expenditures for this biennium).

Oil and Gas Production Tax Distribution Fund has a continuing appropriation authorized by NDCC section 57-51-15 (\$1,519,750,573 of expenditures for this biennium).

State Taxes Distribution Fund has a continuing appropriation authorized by Article X, section 10, of the North Dakota Constitution (\$8,332,747 of expenditures for this biennium).

Township Road and Bridge has a continuing appropriation authorized by NDCC section 54-27-19.1 (\$14,558,123 of expenditures for this biennium).

Tribal Sales Tax Fund has a continuing appropriation authorized by NDCC section 57-39.8-02 (\$640,293 of expenditures for this biennium).

Coal Conversion Tax Trust Fund has a continuing appropriation authorized by NDCC section 57-60-14 (\$54,291,470 of expenditures for this biennium).

Electric Generation and Transmission Fund has a continuing appropriation authorized by NDCC section 57-33.2-19 (\$23,650,235 of expenditures for this biennium).

Oil Extraction Tax Development Trust Fund has a continuing appropriation authorized by NDCC section 57-51.1-07 (\$1,429,727,006 of expenditures for this biennium).

Estate Tax Distribution Fund has a continuing appropriation authorized by NDCC section 57-37.1-08 (\$175 of expenditures for this biennium).

Oil Tax Resources Trust Fund upon legislative appropriation for the State Water Commission as noted in Senate Bill 2020 sections 3, 4, and 5 of the 2015 Legislative Session, is authorized by NDCC section 57-51.1-07(1) (\$528,482,610 of expenditures for this biennium).

Air Transportation Fund has a continuing appropriation authorized by NDCC section 57-32-04 (\$360,710 of expenditures for this biennium).

Internal Control

In our audit for the biennium ended June 30, 2017, we identified the following areas of the Office of State Treasurer's internal control as being the highest risk:

Internal Controls Subjected to Testing:

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenditures.
- Controls surrounding investment activities.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.

The criteria used to evaluate internal control is published in the publication *Standards for Internal Control in the Federal Government* issued by the Comptroller General of the United States (Green Book, GAO-14-704G). Agency management must establish and maintain effective internal control in accordance with policy of the Office of Management and Budget (OMB Policy 216).

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered necessary based on our assessment of audit risk. We concluded internal control was adequate.

Auditors are required to report deficiencies in internal control that are significant within the context of the objectives of the audit. 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: misstatements in financial or performance information, violations of laws and regulations, or impairments of effectiveness or efficiency of operations, on a timely basis. Considering both qualitative and quantitative factors, we did not identify any significant deficiencies in internal control.

Compliance with Legislative Intent

In our audit for the biennium ended June 30, 2017, we identified and tested Office of State Treasurer's compliance with legislative intent for the following areas we determined to be significant and of higher risk of noncompliance:

- Properly distributed \$8,000,000 of general fund moneys to counties for allocation to townships in non-oil-producing counties (2015 North Dakota Legislative Session, House Bill 1012, section 8).
- Proper distribution of the following funds:
 - Jobs Training Program Fund (NDCC 52-02.1-03)
 - Highway Tax Distribution Fund (NDCC 54-27-19)
 - Township Road and Bridge Fund (NDCC 54-27-19.1)
 - City Lodging Tax Suspense Fund (NDCC 57-01-02.1)
 - City Sales Tax Suspense Fund (NDCC 57-01-02.1)
 - City Motor Vehicle Rental Tax Fund (NDCC 57-01-02.1)
 - City Restaurant and Lodge Tax Fund (NDCC 57-01-02.1)
 - Homestead Tax Credit (NDCC 57-02-08.2)
 - Disabled Veterans Homestead Tax Credit (NDCC 57-02-08.8)
 - State Paid Property Tax Relief Credit (NDCC 57-20-07.2)
 - Air Transportation Tax Fund (NDCC 57-32-04)
 - Electric Generation, Transmission, and Distribution Tax Fund (NDCC 57-33.2-19)
 - Telecommunications Carriers Tax Fund (NDCC 57-34-05)
 - Cigarette Tax Fund (NDCC 57-36-31)
 - State Aid Distribution Fund (NDCC 57-39.2-26.1)
 - Oil and Gas Production Tax Distribution Fund (NDCC 57-51-15)
 - Oil Extraction Tax Development Fund (NDCC 57-51.1-07)
- Compliance with appropriations and related transfers (2015 North Dakota Session Laws, Senate Bill 2005).
- Compliance with Emergency Commission or Budget Section changes to appropriations (NDCC 54-16-03).
- Compliance with credits to appropriations in accordance with OMB Policy 214.
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with payroll-related laws including statutory salaries for applicable elected positions and certification of payroll.
- Proper statutory authority for investments.
- Proper deposit of all investment interest.
- Proper legislative authority for all funds and non-appropriated expenditures (NDCC 54-44.1-09).
- Proper deposit of fees collected by the counties and submitted to the Office of the State Treasurer.

The criteria used to evaluate legislative intent are the laws as published in the *North Dakota Century Code* and the *North Dakota Session Laws*.

Government Auditing Standards require auditors to report all instances of fraud and illegal acts unless they are inconsequential within the context of the audit objectives. Further, auditors are

required to report significant violations of provisions of contracts or grant agreements, and significant abuse that has occurred or is likely to have occurred.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. Thus, we concluded there was compliance with the legislative intent identified above.

Operations

This audit did not identify areas of Office of State Treasurer's operations where we determined it was practical at this time to help to improve efficiency or effectiveness.

You may obtain audit reports on the internet at:

www.nd.gov/auditor

or by contacting the Office of the State Auditor at:

Email: ndsao@nd.gov

Phone: (701) 328-2241

Office of the State Auditor

600 East Boulevard Avenue – Department 117

Bismarck, ND 58505-0060