



Financial Statements
June 30, 2017 and 2016

Office of the State Auditor

**OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota**

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June 30, 2017 and 2016**

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Independent Auditor's Report

Governor of North Dakota
The Legislative Assembly

Office of the State Auditor
Bismarck, North Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Office of the State Auditor, as of and for the years ended June 30, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the Office of the State Auditor's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the 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 opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Office of the State Auditor as of June 30, 2017 and 2016, and the respective changes in financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements of the Office of the State Auditor are intended to present the financial position and the changes in financial position of only that portion of the governmental activities, each major fund, and the aggregate remaining fund information of the State of North Dakota that is attributable to the transactions of the Office of the State Auditor. They do not purport to, and do not, present fairly the financial position of the State of North Dakota as of June 30, 2017 and 2016, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America. Our opinions are not modified with respect to this matter.

Other Matters

Required Supplementary Information

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

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 5, 2018, on our consideration of the Office of the State Auditor's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 Office of the State Auditor's internal control over financial reporting and compliance.



Bismarck, North Dakota
January 5, 2018

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the Office of the State Auditor's (Office) financial report presents a discussion and analysis of the Office's financial performance, providing an overview of the activities for the biennium ended June 30, 2017. Please read it with the Office's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

Agency-wide:

The liabilities and deferred inflows of resources of the Office exceeded its assets and deferred outflows of resources (reported as net position) at June 30, 2017 and 2016 by \$3,379,993 and \$2,354,549, respectively. The June 30, 2017 net position decreased \$1,025,444 from the previous fiscal year-end and the June 30, 2016 net position increased \$320,065 from the previous fiscal year-end. The decrease in net position at June 30, 2017 is mainly due to an increase in the net pension liability. The increase in net position at June 30, 2016 over the prior year is mainly due to changes in deferred outflows and inflows for pensions.

Fund Level:

At the close of fiscal years 2017 and 2016, the Office's governmental funds reported combined ending fund balances of \$195,308 and \$194,537, respectively. The June 30, 2017 fund balance increased \$771 over the previous fiscal year-end and the June 30, 2016 fund balance increased \$15,586 over the previous fiscal year-end.

Long-term Debt:

The Office's long-term debt (compensated absences and capital lease payable due in more than one year, and net pension liability) at June 30, 2017 and 2016 was \$4,151,586 and \$2,833,392, respectively. The June 30, 2017 balance increased \$1,318,194 over the previous fiscal year-end (mainly due to an increase in the net pension liability) and the June 30, 2016 balance increased \$1,287 over the previous fiscal year-end.

More detailed information regarding these activities and funds is included in the notes to the financial statements.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is an introduction to the Office's basic financial statements, which consists of three components: 1) agency-wide financial statements; 2) fund financial statements; and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.

Agency-wide Statements

The agency-wide financial statements provide a broad view of the Office's operations in a manner similar to a private-sector business. The statements provide both short-term and long-term information about the Office's financial position, which assists in assessing the Office's economic condition at the end of each fiscal year. These statements include all assets and liabilities using the accrual basis of accounting. The current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The Statement of Net Position presents all of the Office's (a) assets and deferred outflows of resources and (b) liabilities and deferred inflows of resources, with the difference between the two reported as "net position." Over time, increases and decreases in net position are an indicator of whether the Office's financial position is improving or deteriorating.

The Statement of Activities presents information showing how the Office's net position changed during each fiscal year. All changes in net position are reported as soon as the underlying events giving rise to the change occur, regardless of the timing of related cash flows. Therefore, revenues and expenses are reported in these statements for some items that will only result in cash flows in future fiscal periods (e.g. earned but unused vacation leave).

Both statements report governmental activities. The activities in this section are primarily supported by general fund appropriations, charges for services, and intergovernmental revenue.

The agency-wide financial statements can be found immediately following this discussion and analysis.

Fund Financial Statements

A fund is a fiscal and accounting entity with a self-balancing set of accounts the Office uses to track specific sources of funding and spending for a particular purpose. The Office, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance related legal requirements.

The basic fund financial statements begin immediately after the agency-wide statements and provide more detail about the major individual funds. The Office's funds are all governmental funds.

Governmental funds – all of the Office's basic services are reported in the governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the agency-wide financial statements. However, unlike the agency-wide financial statements, the governmental fund financial statements focus on the near-term inflows and outflows of spendable resources. They also focus on the balances left at year-end that are available for future spending. Such information may be useful in evaluating whether there are more or less financial resources that can be spent in the near future to finance the Office's programs. These funds are reported using *modified accrual* accounting, which measures cash and all other financial assets that can readily be converted to cash.

Because the focus of governmental funds is narrower than agency-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the agency-wide financial statements. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and the governmental activities.

Governmental funds include the general fund and special revenue funds. The Office has four governmental funds, of which three are considered major individual funds. Those three are the General Fund, Federal Fund, and the Operating Fund. Each of these major funds is presented in a separate column in the governmental fund balance sheet, and in the governmental fund statement of revenues, expenditures, and changes in fund balance. The remaining governmental fund (Conference Fund) is shown in a separate column on the basic fund statements.

Notes to the Financial Statements

The Notes provide additional information that is essential to a full understanding of the data provided in the agency-wide and the fund financial statements. The Notes to the Financial Statements can be found immediately following the statement of revenues, expenditures, and changes in fund balances.

Required Supplementary Information

The basic financial statements are followed by a section of required supplementary information. This section consists of: a budgetary comparison schedule, which includes reconciliations between budgetary inflows and outflows and GAAP revenues and expenditures, as presented in the governmental fund statement of revenues, expenditures, and changes in fund balances; a schedule of employer's share of net pension liability; and a schedule of employer contributions.

FINANCIAL ANALYSIS OF THE OFFICE AS A WHOLE

As noted previously, net position may serve over time as a useful indicator of an Office's financial position. The Office's net position totaled \$(3,379,993), \$(2,354,549), and \$(2,674,614) at the end of fiscal years 2017, 2016, and 2015, respectively.

Net Position			
	Governmental Activities		
	2017	2016	2015
Current and Other Assets	\$ 1,028,922	\$ 1,246,041	\$ 980,525
Capital Assets	5,124	7,583	10,043
Total Assets	\$ 1,034,046	\$ 1,253,624	\$ 990,568
Deferred Outflows of Resources	\$ 963,713	\$ 539,796	\$ 465,560
Long-Term Liabilities Outstanding	\$ 4,151,586	\$ 2,833,392	\$ 2,832,105
Other Liabilities	857,499	1,071,409	821,714
Total Liabilities	\$ 5,009,085	\$ 3,904,801	\$ 3,653,819
Deferred Inflows of Resources	\$ 368,667	\$ 243,168	\$ 476,923
Net Position			
Net Investment in Capital Assets	\$ (761)	\$ (717)	\$ (439)
Unrestricted	(3,379,232)	(2,353,832)	(2,674,175)
Total Net Position	\$ (3,379,993)	\$ (2,354,549)	\$ (2,674,614)

The Office's long-term liabilities increased significantly and unrestricted net position decreased significantly at June 30, 2017 compared to the prior two years primarily due to an increase in the net pension liability.

The following condensed financial information was derived from the agency-wide Statement of Activities and reflects how the Office's net position changed during each fiscal year:

Changes in Net Position			
	Governmental Activities		
	2017	2016	2015
Revenues:			
Program Revenues:			
Charges for Services	\$ 2,028,273	\$ 1,423,229	\$ 1,695,708
Operating Grants	589,485	561,249	640,336
Total Revenues	\$ 2,617,758	\$ 1,984,478	\$ 2,336,044
Expenses:			
Administration	\$ 311,302	\$ 215,412	\$ 213,793
State Agency Audits	5,031,352	4,039,900	4,032,685
NDUS Performance Audits	501,157	233,490	
Mineral Royalty Audits	685,514	531,292	633,726
Local Government Audits	958,709	750,569	707,992
Conferences		8,000	14,829
Interest on Long-term Debt	732	964	1,069
Total Expenses	\$ 7,488,766	\$ 5,779,627	\$ 5,604,094
Increase (Decrease) in Net Position Before Transfers	\$ (4,871,008)	\$ (3,795,149)	\$ (3,268,050)
Transfers	3,845,564	4,115,214	3,315,158
Increase (Decrease) in Net Position	\$ (1,025,444)	\$ 320,065	\$ 47,108
Net Position - Beginning	(2,354,549)	(2,674,614)	(2,721,722)
Net Position - Ending	<u><u>\$ (3,379,993)</u></u>	<u><u>\$ (2,354,549)</u></u>	<u><u>\$ (2,674,614)</u></u>

Revenues were higher in fiscal years 2017 and 2015 due to the majority of the Single Audit being performed in odd numbered fiscal years. The Single Audit work is billed at 100% whereas state agency audit billings are reduced if the agency being audited receives state general funds. Expenses increased significantly in fiscal year 2017 due primarily to an increase in pension expenses. In addition, the legislature authorized the creation of the NDUS Performance Audits division which began in fiscal year 2016.

FINANCIAL ANALYSIS OF THE OFFICE'S FUNDS

Governmental Funds

At June 30, 2017 and 2016, the Office reported combined fund balances of \$195,308 and \$194,537, respectively. The June 30, 2017 fund balance increased \$771 over the previous fiscal year-end. The June 30, 2016 fund balance increased \$15,586 over the previous fiscal year-end. These changes were not significant.

General Fund Budgetary Highlights

The Office has a biennial appropriated budget. The differences between the original budget and the final budget were either approved by the Construction Carryover Legislative Committee or were required budget allotment reductions mandated by the Governor. The decreases to the salaries and wages line (\$666,546) and the operating expenses line (\$18,704) were the two separate (4.05% and 2.5%) budget allotment reductions. The increase to the construction carryover line (\$80,000) was for office remodeling. The \$80,000 was not spent during the 2013-2015 biennium and was carried over to the 2015-2017 biennium.

There were no expenditures in excess of budgeted amounts in any of the appropriation line items.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets: at the end of the fiscal years 2017 and 2016, the capital assets consist of a copy machine with a depreciated value of \$5,124 and \$7,583, respectively.

Long-term Debt: at the end of fiscal years 2017 and 2016, the Office had \$4,151,586 and \$2,833,392, respectively, of long-term debt (due in more than one year), which consists of the liability for compensated absences, a capital lease, and net pension liability. The significant increase at June 30, 2017 is due primarily to an increase in the net pension liability. More detailed information regarding the Office's long-term obligations are presented in the notes to the financial statements.

CONTACTING THE OFFICE OF THE STATE AUDITOR

This financial report is designed to provide citizens and taxpayers with a general overview of the Office of the State Auditor's finances and to demonstrate the Office's accountability for the money it receives. Questions about this report or additional financial information should be addressed to the Office of the State Auditor, 600 E. Boulevard Ave. - Dept. 117, Bismarck, ND 58505.

OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota

STATEMENT OF NET POSITION
June 30, 2017 and 2016

	Governmental Activities	
	2017	2016
ASSETS		
Cash	\$ 108,898	\$ 100,619
Due from Local Governments	169,611	159,392
Due from Federal Government	152,543	145,258
Due from Other State Agencies	51,875	431,740
Due from State General Fund	545,995	409,032
Equipment - Net	5,124	7,583
Total Assets	<u>\$ 1,034,046</u>	<u>\$ 1,253,624</u>
DEFERRED OUTFLOWS OF RESOURCES		
Deferred Outflows - Pension	<u>\$ 963,713</u>	<u>\$ 539,796</u>
LIABILITIES		
Accrued Payroll	\$ 584,570	\$ 459,453
Accounts Payable	74,746	14,019
Due to Other State Agencies	18,901	43,135
Due to State General Fund	155,397	534,897
Capital Lease Payable:		
Due within one year	2,670	2,415
Due in more than one year	3,215	5,885
Compensated Absences:		
Due within one year	21,215	17,490
Due in more than one year	461,137	400,607
Net Pension Liability	3,687,234	2,426,900
Total Liabilities	<u>\$ 5,009,085</u>	<u>\$ 3,904,801</u>
DEFERRED INFLOWS OF RESOURCES		
Deferred Inflows - Pension	<u>\$ 368,667</u>	<u>\$ 243,168</u>
NET POSITION		
Net Investment in Capital Assets	\$ (761)	\$ (717)
Unrestricted	(3,379,232)	(2,353,832)
Total Net Position	<u><u>\$ (3,379,993)</u></u>	<u><u>\$ (2,354,549)</u></u>

OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota

STATEMENT OF ACTIVITIES
For the Fiscal Year Ended June 30, 2017

Functions/Programs	Expenses	Program Revenues		Net (Expense)
		Charges for	Operating	Revenue and
		Services	Grants	Change in Net
				Position
				Governmental
				Activities
Governmental Activities:				
Administration	\$ 311,302			\$ (311,302)
State Agency Audits	5,031,352	\$ 1,188,148		(3,843,204)
NDUS Performance Audits	501,157			(501,157)
Mineral Royalty Audits	685,514		\$ 589,485	(96,029)
Local Government Audits	958,709	840,125		(118,584)
Interest on Long-term Debt	732			(732)
Total	<u>\$ 7,488,766</u>	<u>\$ 2,028,273</u>	<u>\$ 589,485</u>	<u>\$ (4,871,008)</u>
General Revenues:				
Transfers				<u>\$ 3,845,564</u>
Change in Net Position				\$ (1,025,444)
Net Position, Beginning of Year				<u>(2,354,549)</u>
Net Position, End of Year				<u>\$ (3,379,993)</u>

**OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota**

**STATEMENT OF ACTIVITIES
For the Fiscal Year Ended June 30, 2016**

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Change in Net Position
		Charges for Services	Operating Grants	Governmental Activities
Governmental Activities:				
Administration	\$ 215,412			\$ (215,412)
State Agency Audits	4,039,900	\$ 613,926		(3,425,974)
NDUS Performance Audits	233,490			(233,490)
Mineral Royalty Audits	531,292		\$ 561,249	29,957
Local Government Audits	750,569	801,303		50,734
Conferences	8,000	8,000		
Interest on Long-term Debt	964			(964)
Total	<u>\$ 5,779,627</u>	<u>\$ 1,423,229</u>	<u>\$ 561,249</u>	<u>\$ (3,795,149)</u>
General Revenues:				
Transfers				<u>\$ 4,115,214</u>
Change in Net Position				\$ 320,065
Net Position, Beginning of Year				<u>(2,674,614)</u>
Net Position, End of Year				<u>\$ (2,354,549)</u>

OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota

BALANCE SHEET
Governmental Funds
June 30, 2017

	General	Federal	Operating Fund	Other Governmental Funds	Total
ASSETS					
Cash			\$ 108,898		\$ 108,898
Due from Local Governments			169,611		169,611
Due from Federal Government		\$ 152,543			152,543
Due from Other State Agencies	\$ 51,122		753		51,875
Due from State General Fund	545,995				545,995
Total Assets	\$ 597,117	\$ 152,543	\$ 279,262	\$ -	\$ 1,028,922
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accrued Payroll	\$ 462,275	\$ 45,250	\$ 77,045		\$ 584,570
Accounts Payable	68,189	1,974	4,583		74,746
Due to Other State Agencies	15,531	1,044	2,326		18,901
Due to State General Fund	51,122	104,275			155,397
Total Liabilities	\$ 597,117	\$ 152,543	\$ 83,954	\$ -	\$ 833,614
Fund Balances:					
Committed			\$ 195,308		\$ 195,308
Total Fund Balances	\$ -	\$ -	\$ 195,308	\$ -	\$ 195,308
Total Liabilities and Fund Balances	\$ 597,117	\$ 152,543	\$ 279,262	\$ -	\$ 1,028,922

Total Fund Balances - Governmental Funds \$ 195,308

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

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. The cost of the assets is \$12,297 and the accumulated depreciation is \$7,173. 5,124

Long-term liabilities are not due and payable in the current period and therefore are not reported as liabilities in the funds. Those liabilities consist of:

Compensated Absences	\$ (482,352)	
Capital Lease Payable	(5,885)	
Net pension liability	(3,687,234)	
Total long-term liabilities		(4,175,471)

Deferred outflows and inflows of resources are not reported in governmental funds:

Deferred outflows - pension	963,713
Deferred inflows - pension	(368,667)

Net Position of Governmental Activities \$ (3,379,993)

OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota

BALANCE SHEET
Governmental Funds
June 30, 2016

	General	Federal	Operating Fund	Other Governmental Funds	Total
ASSETS					
Cash			\$ 98,106	\$ 2,513	\$ 100,619
Due from Local Governments			159,392		159,392
Due from Federal Government		\$ 145,258			145,258
Due from Other State Agencies	\$ 430,987		753		431,740
Due from State General Fund	409,032				409,032
Total Assets	<u>\$ 840,019</u>	<u>\$ 145,258</u>	<u>\$ 258,251</u>	<u>\$ 2,513</u>	<u>\$ 1,246,041</u>
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accrued Payroll	\$ 359,932	\$ 40,234	\$ 59,287		\$ 459,453
Accounts Payable	9,663		1,843	\$ 2,513	14,019
Due to Other State Agencies	39,437	1,114	2,584		43,135
Due to State General Fund	430,987	103,910			534,897
Total Liabilities	<u>\$ 840,019</u>	<u>\$ 145,258</u>	<u>\$ 63,714</u>	<u>\$ 2,513</u>	<u>\$ 1,051,504</u>
Fund Balances:					
Committed			\$ 194,537		\$ 194,537
Total Fund Balances	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 194,537</u>	<u>\$ -</u>	<u>\$ 194,537</u>
Total Liabilities and Fund Balances	<u>\$ 840,019</u>	<u>\$ 145,258</u>	<u>\$ 258,251</u>	<u>\$ 2,513</u>	<u>\$ 1,246,041</u>

Total Fund Balances - Governmental Funds \$ 194,537

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

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. The cost of the assets is \$12,297 and the accumulated depreciation is \$4,714. 7,583

Long-term liabilities are not due and payable in the current period and therefore are not reported as liabilities in the funds. Those liabilities consist of:

Compensated Absences	\$ (418,097)	
Capital Lease Payable	(8,300)	
Net pension liability	<u>(2,426,900)</u>	
Total long-term liabilities		(2,853,297)

Deferred outflows and inflows of resources are not reported in governmental funds:

Deferred outflows - pension	539,796
Deferred inflows - pension	<u>(243,168)</u>

Net Position of Governmental Activities \$ (2,354,549)

**OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota**

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
Governmental Funds**

For the Year Ended June 30, 2017

	General	Federal	Operating Fund	Other Governmental Funds	Total
REVENUES					
Intergovernmental		\$ 589,485			\$ 589,485
Charges for Services	\$ 1,188,148		\$ 840,125		2,028,273
Total Revenues	\$ 1,188,148	\$ 589,485	\$ 840,125	\$ -	\$ 2,617,758
EXPENDITURES					
Current:					
Administration	\$ 267,458				\$ 267,458
State Audits	4,327,015				4,327,015
NDUS Performance Audits	436,093				436,093
Mineral Royalty Audits		\$ 589,485			589,485
Local Government Audits			\$ 839,354		839,354
Conference Expenses					-
Debt Service:					
Principal	2,414				2,414
Interest	732				732
Total Expenditures	\$ 5,033,712	\$ 589,485	\$ 839,354	\$ -	\$ 6,462,551
Revenues over (under) expenditures	\$ (3,845,564)		\$ 771		\$ (3,844,793)
OTHER FINANCING SOURCES (USES)					
Transfers In	\$ 5,033,712				\$ 5,033,712
Transfers Out	(1,188,148)				(1,188,148)
Total Other Financing Sources (Uses)	\$ 3,845,564				\$ 3,845,564
Net Change in Fund Balances			\$ 771		\$ 771
Fund Balances - Beginning of Year			194,537		194,537
Fund Balances - End of Year			\$ 195,308		\$ 195,308

Net Change in Fund Balances - Total Governmental Funds \$ 771

Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. These activities consist of:

Increase in compensated absences	(64,255)
Debt service principal expense which was capitalized	2,414
Depreciation expense	(2,458)
Increase in pension expense	(961,916)

Change in Net Position of Governmental Activities \$ (1,025,444)

**OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota**

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
Governmental Funds
For the Year Ended June 30, 2016**

	General	Federal	Operating Fund	Other Governmental Funds	Total
REVENUES					
Intergovernmental		\$ 561,249			\$ 561,249
Charges for Services	\$ 613,926		\$ 801,303		1,415,229
Conference Registration Fees				\$ 8,000	8,000
Total Revenues	\$ 613,926	\$ 561,249	\$ 801,303	\$ 8,000	\$ 1,984,478
EXPENDITURES					
Current:					
Administration	\$ 228,061				\$ 228,061
State Audits	4,255,189				4,255,189
NDUS Performance Audits	242,744				242,744
Mineral Royalty Audits		\$ 561,249			561,249
Local Government Audits			\$ 785,717		785,717
Conference Expenses				\$ 8,000	8,000
Debt Service:					
Principal	2,182				2,182
Interest	964				964
Total Expenditures	\$ 4,729,140	\$ 561,249	\$ 785,717	\$ 8,000	\$ 6,084,106
Revenues over (under) expenditures	\$ (4,115,214)		\$ 15,586		\$ (4,099,628)
OTHER FINANCING SOURCES (USES)					
Transfers In	\$ 4,729,140				\$ 4,729,140
Transfers Out	(613,926)				(613,926)
Total Other Financing Sources (Uses)	\$ 4,115,214				\$ 4,115,214
Net Change in Fund Balances			\$ 15,586		\$ 15,586
Fund Balances - Beginning of Year			178,951		178,951
Fund Balances - End of Year			\$ 194,537		\$ 194,537

Net Change in Fund Balances - Total Governmental Funds **\$ 15,586**

Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. These activities consist of:

Increase in compensated absences	(19,535)
Debt service principal expense which was capitalized	2,182
Depreciation expense	(2,460)
Decrease in pension expense	324,292

Change in Net Position of Governmental Activities **\$ 320,065**

**OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota**

**NOTES TO THE FINANCIAL STATEMENTS
June 30, 2017 and 2016**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. FINANCIAL STATEMENTS AND REPORTING ENTITY

The accompanying financial statements of the Office of the State Auditor have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

For financial reporting purposes, the Office of the State Auditor has included all funds and has considered all potential component units for which the Office of the State Auditor is financially accountable, and other organizations for which the nature and significance of their relationship with the Office of the State Auditor are such that exclusion would cause the Office of the State Auditor's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the Office of the State Auditor to impose its will on that organization; or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Office of the State Auditor.

Based upon these criteria, there are no component units to be included within the Office of the State Auditor as a reporting entity and the Office of the State Auditor is an agency within the State of North Dakota as a reporting entity.

B. AGENCY-WIDE AND FUND FINANCIAL STATEMENTS

AGENCY-WIDE FINANCIAL STATEMENTS

The Statement of Net Position and Statement of Activities report information on all activities of the Office of the State Auditor. Governmental activities generally are financed through intergovernmental revenues and other non-exchange revenues.

The Statement of Net Position presents the reporting entity's assets and liabilities, with the difference reported as net position. Net position is reported in three categories:

Net Investment in capital assets consists of a capital asset, net of accumulated depreciation.

Restricted net position results when constraints placed on net position use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation. Net position restricted by enabling legislation is subject to change by a majority vote of the Legislative Assembly.

Unrestricted net position consists of net position which does not meet the definition of the two preceding categories. Unrestricted net position often is designated to indicate management does not consider it to be available for general operations. Unrestricted net position often has constraints on resources which are imposed by management, but can be removed or modified.

The Statement of Activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function. Program revenues include: 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function; and 2) grants and contributions that are restricted to meeting the operational requirements of a particular function.

FUND FINANCIAL STATEMENTS

Major individual governmental funds are reported as separate columns in the fund financial statements, with non-major funds being combined into a single column.

C. MEASUREMENT FOCUS, BASIS OF ACCOUNTING, AND FINANCIAL STATEMENT PRESENTATION

MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

The agency-wide statements are reported using the economic resources management focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows.

The Office of the State Auditor follows the pronouncements of the Governmental Accounting Standards Board (GASB), which is the nationally accepted standard-setting body for establishing accounting principles generally accepted in the United States of America for governmental entities.

Governmental fund statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as they become susceptible to accrual; generally when they are both measurable and available. Revenues are considered to be available when they are collected within the current period or soon enough thereafter to pay liabilities of the current period.

Major revenues that are determined to be susceptible to accrual include federal grants and audit fees. All revenues are determined to be available if collected within one year of fiscal year-end. Revenues earned under the terms of reimbursement agreements with other governments are recorded at the time the related expenditures are made if other eligibility requirements have been met.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, expenditures related to debt service and compensated absences are recorded only when payment is due and payable.

FINANCIAL STATEMENT PRESENTATION

The Office of the State Auditor reports the following major governmental funds:

The general fund is the principal operating fund of the agency. It is used to account for all financial resources that are not accounted for in other funds. Included are transactions involving administration, state agency audits, and NDUS performance audits.

The federal fund accounts for all the financial resources from the federal government, which finances the Mineral Royalty Audit Division.

The operating fund accounts for all activities of the Local Government Audit Division.

D. GENERAL BUDGETARY POLICIES AND PROCEDURES

The Office of the State Auditor operates through a biennial appropriation provided by the State Legislature. The Office prepares a biennial budget, which is included in the Governor's budget presented to the Legislative Assembly at the beginning of each legislative session. The Legislative Assembly enacts the budgets of the various state departments through passage of specific appropriation bills. The Governor has line item veto powers over all legislation subject to legislative override.

Once passed and signed, the appropriation bill becomes the department's financial plan for the next two years. Changes to the appropriation are limited to Emergency Commission authorization, initiative, referendum, or allotment action. The Emergency Commission can authorize receipt of federal or other moneys not appropriated by the Assembly if the Assembly did not indicate an intent to reject the money. Unexpended appropriations lapse at the end of each biennium.

The biennial budget is prepared primarily on a cash basis. Encumbrance accounting is not used. The legal level of budgetary control is at the funding source and expenditure line item level. Revenues are not formally budgeted and expenditures are not budgeted by fund. The agency appropriation is defined through the use of specific expenditure line items.

E. CASH

Cash consists of money on deposit with the State Treasurer.

F. RECEIVABLES

Receivables include amounts "due from other state agencies" (state agency audits) and "due from local governments" (local government audits) for audits performed during the year.

G. DUE FROM STATE GENERAL FUND

"Due from state general fund" is the amount needed from the state general fund to liquidate accrued payroll and liabilities of the Office of the State Auditor general fund.

H. DUE FROM FEDERAL GOVERNMENT

The Office of the State Auditor has a contract with the United States Department of the Interior - Minerals Management Service for audit and related investigations of federal oil and gas leases located in the state of North Dakota. It is the Office of the State Auditor's policy to recognize federal revenue as allowable expenditures are incurred. Due from federal government represents amounts receivable for reimbursable expenditures incurred by June 30.

I. TRANSFERS

In the fund financial statements, transfers represent flows of assets without equivalent flows of assets in return or a requirement for repayment. "Transfers In" consists of transfers from the state's general fund and "Transfers Out" consists of transfers to the state's general fund.

J. CAPITAL ASSETS

Capital assets are valued at historical cost. Capital assets with an original cost of \$5,000 or more and an estimated useful life in excess of one year are capitalized and reported in the applicable governmental column in the agency-wide financial statements. Capital asset costs include the purchase price, plus the costs necessary to place the asset in its intended location and condition for use. Normal maintenance and repair costs that do not materially add to the value or extend the life of the asset are not capitalized.

Capital assets in governmental funds are recorded as expenditures in the funds used to acquire them in the governmental fund financial statements. Capital assets, along with accumulated depreciation and depreciation expense, are reported in the applicable governmental activities column in the agency-wide financial statements.

Capital assets are depreciated using the straight-line method over their estimated useful lives of 3-10 years.

K. LEASE COMMITMENTS

The Office of the State Auditor leases office space and a copy machine. Leases are classified according to GASB 62. The leases all have funding clauses; however, these clauses have no effect on classifying these leases for accounting purposes. Leases which represent acquisitions are classified as capital leases, and the related assets and liabilities recorded in the general purpose financial statements at the inception of the lease. Other leases are classified as operating leases with the lease payments recorded as expenditures or expenses during the life of the lease.

L. COMPENSATED ABSENCES

Annual Leave

State employees accrue vested annual leave at a variable rate based on years of service. In general, accrued annual leave cannot exceed 30 days at each year-end, as set by the agency.

The amount of annual leave earned ranges between one and two days per month, and is fixed by the employing unit per section 54-06-14 of the North Dakota Century Code. Employees are paid for unused annual leave upon termination or retirement.

The governmental fund financial statements recognize annual leave when the liability is incurred and payable from available expendable resources. The agency-wide financial statements present the cost of accumulated annual leave as a liability.

Sick Leave

The North Dakota Century Code, section 54-06-14, states employees accrue sick leave at the rate of one to a maximum of one and one-half working days per month of employment without limitation on the amount that can be accumulated. Employees of the Office accrue sick leave at a rate of one day per month. Employees vest at 10 years of creditable service at which time the state is liable for 10 percent of the employee's accumulated unused sick leave. The governmental fund financial statements recognize sick leave as it is incurred. The agency-wide financial statements present the estimated cost of sick leave as a liability after an employee has been employed by the state for six consecutive years.

M. REVENUES AND EXPENDITURES/EXPENSES

In the agency-wide Statement of Activities, revenues and expenses are segregated by activity, then further by function for governmental activities. Additionally, revenues are classified between program and general revenues. Program revenues include: 1) charges to customers for services; and 2) operating grants.

In the governmental fund financial statements, revenues are reported by source and expenditures are reported by character: "Current" and "Debt Service." Current expenditures are sub-classified by function. Debt service includes both principal and interest payments on a capital lease.

N. NET POSITION/FUND BALANCE

Net position represents the difference between (a) assets and deferred outflows of resources and (b) liabilities and deferred inflows of resources on the agency-wide statements. Fund balance represents the difference between assets and liabilities on the governmental fund statements. Fund balance classifications for governmental funds are reported in two general classifications, nonspendable and spendable. Nonspendable represents the portion of fund balance that is not in spendable form such as inventories and prepaids. Spendable fund balance is further categorized as restricted, committed, assigned, and unassigned.

The restricted fund balance category includes amounts that can be spent only for the specific purposes stipulated by the State constitution and external parties, such as the federal government, or through enabling legislation.

The committed fund balance classification includes amounts that can be used only for the specific purposes determined by a formal action of the government's highest level of decision-making authority, the state's legislature, through legislation, that is not considered as enabling legislation, passed into law.

Assigned fund balance classifications are used when the amounts are to be used for specific purposes but do not meet the criteria to be classified as restricted or committed. The assignment of fund balance is generally initiated by the executive branch and later appropriated by the Legislature for a specific purpose.

Unassigned fund balance is the residual classification for the government's general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification would only be used to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

The balance sheet amounts shown as committed fund balances in the operating fund can be used only for expenses relating to political subdivision audits in accordance with North Dakota Century Code. This commitment of fund balance can only be changed by an act of the State Legislature. The balance sheet amounts shown as assigned in the other governmental funds can only be used for conference activity.

O. PENSIONS

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the North Dakota Public Employees Retirement System (NDPERS) and additions to/deductions from NDPERS' fiduciary net position have been determined on the same basis as

they are reported by NDPERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

P. NEW ACCOUNTING PRONOUNCEMENTS

The following pronouncement was implemented for fiscal years 2017 and 2016:

GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, is to identify, in the context of the current governmental financial reporting environment, the hierarchy of generally accepted accounting principles (GAAP). The “GAAP hierarchy” consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP.

Issued but non-effective pronouncements will not have a significant impact on the Office of the State Auditor.

Q. DEFERRED OUTFLOWS/INFLOWS OF RESOURCES

In addition to assets, the statement of net position reports 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/ expenditure) until then.

In addition to liabilities, the statement of net position reports 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.

NOTE 2 – DETAILED NOTES ON ACCOUNT BALANCES

A. DEPOSITS

State law generally requires that all state funds be deposited in the Bank of North Dakota. NDCC 21-04-01 provides that public funds belonging to or in the custody of the state shall be deposited in the Bank of North Dakota. Also, NDCC 6-09-07 states, “all state funds . . . must be deposited in the Bank of North Dakota” or must be deposited in accordance with constitutional and statutory provisions.

At June 30, 2017 and 2016, the bank balances of the Office of the State Auditor’s deposits were \$108,898 and \$100,619, respectively. All deposits are exposed to custodial credit risk because they are not covered by depository insurance and the deposits are uncollateralized. All of the Office of the State Auditor’s deposits are at the Bank of North Dakota. Deposits with the Bank of North Dakota are considered uninsured; however, these deposits are guaranteed by the state of North Dakota (NDCC Chapter 6-09-10).

B. CAPITAL ASSETS

Capital assets consist of a copy machine that was acquired in fiscal year 2015 through a capital lease. The original cost was \$12,297 and accumulated depreciation at June 30, 2017 and 2016 was \$7,173 and \$4,714, respectively. The net value on June 30, 2017 and 2016 was \$5,124 and \$7,583 respectively.

C. OPERATING LEASES

The Office of the State Auditor leases office space under cancelable operating leases. Total expenditures for these leases for the years ended June 30, 2017 and 2016 were \$116,810 and \$104,432, respectively.

D. CAPITAL LEASE

The Office of the State Auditor is obligated under a capital lease for a copy machine. The five-year lease was entered into in August 2014 for a copy machine with a cost of \$12,297. In the agency-wide statements, a capital asset and a corresponding liability are recorded at the inception of the lease. The liability is reduced by payments of principal, with the payments of interest allocated to expense. For capital leases in governmental funds, other financing sources and capital outlay are recorded at lease inception. Lease payments are recorded as expenditures.

The schedule below lists the future minimum lease payments under the capital lease and the present value of the net minimum lease payments at June 30, 2017:

Year Ending June 30	Lease Payments
2018	3,146
2019	3,146
2020	262
Total Minimum Lease Payments	\$6,554
Less: Amount Representing Interest	(669)
Present Value of Future Minimum Lease Payments	<u>\$5,885</u>

E. LONG-TERM DEBT

A summary of changes in general long-term debt for the years ended June 30, 2017 and 2016 is as follows:

	Balance July 1, 2015	Additions	Reductions	Balance June 30, 2016	Amounts Due Within One Year
Compensated Absences	\$ 398,562	\$ 20,113	\$ 578	\$ 418,097	\$ 17,490
Capital Lease Payable	10,482		2,182	8,300	2,415
Total	<u>\$ 409,044</u>	<u>\$ 20,113</u>	<u>\$ 2,760</u>	<u>\$ 426,397</u>	<u>\$ 19,905</u>

	Balance July 1, 2016	Additions	Reductions	Balance June 30, 2017	Amounts Due Within One Year
Compensated Absences	\$ 418,097	95,240	\$ 30,985	\$ 482,352	\$ 21,215
Capital Lease Payable	8,300		2,415	5,885	2,670
Total	<u>\$ 426,397</u>	<u>\$ 95,240</u>	<u>\$ 33,400</u>	<u>\$ 488,237</u>	<u>\$ 23,885</u>

NOTE 3 - NORTH DAKOTA PUBLIC EMPLOYEES RETIREMENT SYSTEM (NDPERS)

The Office of the State Auditor participates in the North Dakota Public Employees Retirement System (NDPERS) - Main System. The following brief description of NDPERS is provided for general information purposes only. Participants should refer to NDCC Chapter 54-52 for more complete information.

A. DESCRIPTION OF PENSION PLAN

NDPERS is a cost-sharing multiple-employer defined benefit pension plan that covers substantially all employees of the State of North Dakota, its agencies and various participating political subdivisions. NDPERS provides for pension, death and disability benefits. The cost to administer the plan is financed through the contributions and investment earnings of the plan.

Responsibility for administration of the NDPERS defined benefit pension plan is assigned to a Board comprised of seven members. The Board consists of a Chairman, who is appointed by the Governor; one member appointed by the Attorney General; one member appointed by the State Health Officer; three members elected by the active membership of the NDPERS system; and one member elected by the retired public employees. Effective July 1, 2015, the board was expanded to include two members of the legislative assembly appointed by the chairman of the legislative management.

B. PENSION BENEFITS

Benefits are set by statute. NDPERS has no provision or policies with respect to automatic and ad hoc post-retirement benefit increases. Members of the Main System are entitled to unreduced monthly pension benefits beginning when the sum of age and years of credited service equal or exceed 85 (Rule of 85), or at normal retirement age (65). For members hired on or after January 1, 2016 the Rule of 85 will be replaced with the Rule of 90 with a minimum age of 60. The monthly pension benefit is equal to 2.00% of their average monthly salary, using the highest 36 months out of the last 180 months of service, for each year of service. The plan permits early retirement at ages 55-64 with three or more years of service.

Members may elect to receive the pension benefits in the form of a single life, joint and survivor, term-certain annuity, or partial lump sum with ongoing annuity. Members may elect to receive the value of their accumulated contributions, plus interest, as a lump sum distribution upon retirement or termination, or they may elect to receive their benefits in the form of an annuity. For each member electing an annuity, total payment will not be less than the members' accumulated contributions plus interest.

C. DEATH AND DISABILITY BENEFITS

Death and disability benefits are set by statute. If an active member dies with less than three years of service for the Main System, a death benefit equal to the value of the member's accumulated contributions, plus interest, is paid to the member's beneficiary. If the member has earned more than three years of credited service for the Main System, the surviving spouse will be entitled to a single payment refund, life-time monthly payments in an amount equal to 50% of the member's accrued normal retirement benefit, or monthly payments in an amount equal to the member's accrued 100% Joint and Survivor retirement benefit if the member had reached normal retirement age prior to date of death. If the surviving spouse dies before the member's accumulated pension benefits are paid, the balance will be payable to the surviving spouse's designated beneficiary.

Eligible members who become totally disabled after a minimum of 180 days of service, receive monthly disability benefits equal to 25% of their final average salary with a minimum benefit of \$100. To qualify under this section, the member has to become disabled during the period of eligible employment and apply for benefits within one year of termination. The definition of disabled is set by the NDPERS in the North Dakota Administrative Code.

D. REFUNDS OF MEMBER ACCOUNT BALANCE

Upon termination, if a member of the Main System is not vested (is not 65 or does not have three years of service), they will receive the accumulated member contributions and vested employer contributions, plus interest, or may elect to receive this amount at a later date. If the member has vested, they have the option of applying for a refund or can remain as a terminated vested participant. If a member terminated and withdrew their accumulated member contribution and is subsequently reemployed, they have the option of repurchasing their previous service.

E. MEMBER AND EMPLOYER CONTRIBUTIONS

Member and employer contributions paid to NDPERS are set by statute and are established as a percent of salaries and wages. Member contribution rates are 7% and employer contribution rates are 7.12% of covered compensation.

The member's account balance includes the vested employer contributions equal to the member's contributions to an eligible deferred compensation plan. The minimum member contribution is \$25 and the maximum may not exceed the following:

- 1 to 12 months of service – Greater of one percent of monthly salary or \$25
- 13 to 24 months of service – Greater of two percent of monthly salary or \$25
- 25 to 36 months of service – Greater of three percent of monthly salary or \$25
- Longer than 36 months of service – Greater of four percent of monthly salary or \$25

F. PENSION LIABILITIES, PENSION EXPENSE, AND DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES RELATED TO PENSIONS

At June 30, 2017 and June 30, 2016, the Office of the State Auditor (Office) reported a liability of \$3,687,234 and \$2,426,900, respectively for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2016 and June 30, 2015, respectively and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of those dates. The Office's proportion of the net pension liability was based on the Office's share of covered payroll in the Main System pension plan relative to the covered payroll of all participating Main System employers. At June 30, 2016 and June 30, 2015, the Office's proportion was 0.378334 percent and 0.356906 percent, respectively, reflecting an increase of 0.021428 and a decrease of 0.028019, respectively.

For the year ended June 30, 2017, the Office recognized pension expense of \$480,486. At June 30, 2017, the Office reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual experience	\$ 55,390	\$ 34,141
Changes of assumptions	339,916	183,182
Net difference between projected and actual earnings on pension plan investments	514,422	0
Changes in proportion and differences between employer contributions and proportionate share of contributions	120,461	134,101
Employer contributions subsequent to the measurement date	<u>963,713</u>	<u>0</u>
Total	<u>\$ 1,993,902</u>	<u>\$ 351,424</u>

\$963,713 reported as deferred outflows of resources related to pensions resulting from Employer contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2018.

For the year ended June 30, 2016, the Office recognized pension expense of \$197,652. At June 30, 2016, the Office reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual experience	\$ 70,407	\$ 0
Changes of assumptions	0	216,225
Net difference between projected and actual earnings on pension plan investments	280,424	331,655
Changes in proportion and differences between employer contributions and proportionate share of contributions	4,418	172,211
Employer contributions subsequent to the measurement date	<u>539,796</u>	<u>0</u>
Total	<u>\$ 895,045</u>	<u>\$ 720,091</u>

\$539,796 reported as deferred outflows of resources related to pensions resulting from Employer contributions subsequent to the measurement date was recognized as a reduction of the net pension liability in the year ended June 30, 2017.

Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended June 30:

2018	\$ 115,877
2019	115,877
2020	228,097
2021	143,724
2022	75,190
Thereafter	0

Actuarial assumptions. The total pension liability in the July 1, 2016 and July 1, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.50%
Salary increases	4.50% per annum
Investment rate of return	8.00%, net of investment expenses
Cost-of-living adjustments	None

For active members, inactive members and healthy retirees, mortality rates were based on the RP-2000 Combined Healthy Mortality Table set back two years for males and three years for females, projected generationally using the SSA 2014 Intermediate Cost scale from 2014. For disabled retirees, mortality rates were based on the RP-2000 Disabled Mortality Table set back one year for males (no setback for females) multiplied by 125%.

The actuarial assumptions used were based on the results of an actuarial experience study completed in 2015. They are the same as the assumptions used in the July 1, 2016, funding actuarial valuation for NDPERS.

As a result of the 2015 actuarial experience study, the NDPERS Board adopted several changes to the actuarial assumptions effective July 1, 2015. This includes changes to the mortality tables, disability incidence rates, retirement rates, administrative expenses, salary scale, and percent married assumption.

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

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Domestic Equity	31%	6.90%
International Equity	21%	7.55%
Private Equity	5%	11.30%
Domestic Fixed Income	17%	1.52%
International Fixed Income	5%	0.45%
Global Real Assets	20%	5.38%
Cash Equivalents	1%	0.00%

Discount rate. The discount rate used to measure the total pension liability was 8 percent as of June 30, 2016 and June 30, 2015. The projection of cash flows used to determine the discount rate assumes that member and employer contributions will be made at rates equal to those based on the July 1, 2016 and July 1, 2015, Actuarial Valuation Reports. For this purpose, only employer contributions that are intended to fund benefits of current plan members and their beneficiaries are included. Projected employer contributions that are intended to fund the service costs of future plan members and their beneficiaries, as well as projected contributions from future plan members, are not included. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments for current plan members as of June 30, 2016 and June 30, 2015. 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 as of June 30, 2016 and June 30, 2015.

Sensitivity of the Employer's proportionate share of the net pension liability to changes in the discount rate. The following presents the Employer's proportionate share of the net pension liability calculated using the discount rate of 8 percent, as well as what the Employer's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (7 percent) or 1-percentage-point higher (9 percent) than the current rate:

	1% Decrease (7%)	Current Discount Rate (8%)	1% Increase (9%)
6/30/2017 Employer's proportionate share of the net pension liability	\$5,230,270	\$3,687,234	\$2,387,146
6/30/2016 Employer's proportionate share of the net pension liability	\$3,721,529	\$2,426,900	\$1,367,659

Pension plan fiduciary net position. Detailed information about the pension plan's fiduciary net position is available in the separately issued NDPERS financial report.

NOTE 4 - RISK MANAGEMENT

The Office of the State Auditor is exposed to various risks of loss related to torts; theft of; damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The following are funds/pools established by the state for risk management issues:

The 1995 Legislative Session established the Risk Management Fund (RMF), an internal service fund, to provide a self-insurance vehicle for funding the liability exposures of state agencies resulting from the elimination of the state's sovereign immunity. The RMF manages the tort liability of the state and its agencies' employees, and the university system. All state agencies participate in the RMF and their fund contribution is determined using a projected cost allocation approach. The statutory liability of the state is limited to a total of \$250,000 per person and \$1,000,000 per occurrence.

The Office of the State Auditor also participates in the North Dakota Fire and Tornado Fund and the State Bonding Fund. The agency pays an annual premium to the Fire and Tornado Fund to cover property damage to building and personal property. Replacement cost coverage is provided by estimating replacement cost in consultation with the Fire and Tornado Fund. The Fire and Tornado Fund is reinsured by a third party insurance carrier for losses in excess of \$1,000,000 per occurrence. The State Bonding Fund currently provides the Office with blanket fidelity bond coverage in the amount of \$1,107,000 per employee. The State Bonding Fund does not currently charge any premium for this coverage.

The Office participates in the North Dakota Worker's Compensation Bureau, an enterprise fund of the state of North Dakota. The Bureau is a state insurance fund and a "no fault" insurance system covering the state's employers and employees financed by premiums assessed to employers. The premiums are available for the payment of claims to employees injured in the course of employment.

There have been no significant reductions in insurance coverage from the prior years and settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

NOTE 5 - RELATED PARTIES

As noted in "Note 1" of these financial statements, the Office of the State Auditor is an agency of the state of North Dakota; therefore other agencies of the state are related parties.

**OFFICE OF THE STATE AUDITOR
Bismarck, North Dakota**

**Required Supplementary Information
BUDGETARY COMPARISON SCHEDULE - GENERAL AND SPECIAL REVENUE FUNDS
For The Biennium Ended June 30, 2017**

	Original Appropriation	Adjustments	Final Appropriation	Actual	Variance Positive (Negative)
Resources:					
General Fund Transfer	\$ 10,461,832	\$ (605,250)	\$ 9,856,582	\$ 9,762,852	\$ (93,730)
Federal Fund Revenue	1,497,451		1,497,451	1,159,342	(338,109)
Special Fund Revenue	2,008,419		2,008,419	1,629,955	(378,464)
Amounts Available for Appropriation	<u>\$ 13,967,702</u>	<u>\$ (605,250)</u>	<u>\$ 13,362,452</u>	<u>\$ 12,552,149</u>	<u>\$ (810,303)</u>
Charges to Appropriations:					
Salaries and Wages	\$ 12,322,192	\$ (666,546)	\$ 11,655,646	\$ 11,080,197	\$ 575,449
Operating Expenses	1,195,510	(18,704)	1,176,806	1,151,349	25,457
Construction Carryover		80,000	80,000	73,904	6,096
Information Tech Consultants	450,000		450,000	431,991	18,009
Total Charges to Appropriations	<u>\$ 13,967,702</u>	<u>\$ (605,250)</u>	<u>\$ 13,362,452</u>	<u>\$ 12,737,441</u>	<u>\$ 625,011</u>

Explanation of Differences Between Budgetary Inflows and GAAP Revenues and Expenditures

Sources/Inflows of Resources

Actual Amounts (budgetary basis) "total revenue inflows" \$ 12,552,149

The period of availability for revenue recognition for budget purposes differs from the GAAP basis. 2,865

General fund revenue is not budgeted 1,802,074

Conference revenue is not budgeted 8,000

Total revenues/transfers in as reported on the statement of revenues, expenditures, and changes in fund balance - governmental funds \$ 14,365,088

Uses/Outflows of Resources

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule \$ 12,737,441

Differences - budget to GAAP:

Expenditures from the conference fund are not appropriated 8,000
Reimbursement not reflected in financial statements (198,784)

Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balance - governmental funds \$ 12,546,657

Schedules of Required Supplementary Information

Schedule of Employer's Share of Net Pension Liability ND Public Employees Retirement System Last 10 Fiscal Years*

	2017	2016	2015
Employer's proportion of the net pension liability (asset)	0.378334%	0.356906%	.0384925%
Employer's proportionate share of the net pension liability (asset)	\$3,687,234	\$2,426,900	\$2,443,201
Employer's covered-employee payroll	\$3,812,718	\$3,179,602	\$3,242,528
Employer's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll	96.71%	76.33%	75.35%
Plan fiduciary net position as a percentage of the total pension liability	70.46%	77.15%	77.70%

*Complete data for this schedule is not available prior to 2015.

The amounts presented for each fiscal year have a measurement date of the previous fiscal year end.

Schedule of Employer Contributions ND Public Employees Retirement System Last 10 Fiscal Years*

	2017	2016	2015
Statutorily required contribution	\$288,773	\$276,034	\$241,516
Contributions in relation to the statutorily required contribution	(\$288,733)	(\$263,759)	(\$246,821)
Contribution deficiency (excess)	\$0	\$12,275	(\$5,305)
Employer's covered-employee payroll	\$3,948,380	\$3,812,718	\$3,179,602
Contributions as a percentage of covered-employee payroll	7.31%	6.92%	7.76%

*Complete data for this schedule is not available prior to 2015.

Changes of assumptions.

Amounts reported in 2017 reflect actuarial assumption changes effective July 1, 2016 based on the results of an actuarial experience study completed in 2015. This includes changes to the mortality tables, disability incidence rates, retirement rates, administrative expenses, salary scale, and percent married assumption.



Independent Auditor's Comments Requested by the North Dakota Legislative Audit and Fiscal Review Committee

Governor of North Dakota
The Legislative Assembly

Office of the State Auditor
Bismarck, North Dakota

The Legislative Audit and Fiscal Review Committee requires that certain items be addressed by independent certified public accountants performing audits of state agencies. The items and our responses regarding the June 30, 2017 and 2016, audits of the Office of the State Auditor are as follows:

Audit Report Communications

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

Unmodified

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?

No – see current year finding 2017-A.

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

No.

5. Was action taken on prior audit findings and recommendations?

There were no prior year findings or recommendations.

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

No.

Audit Committee Communications

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

None.

- 2. 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 most sensitive estimates affecting the financial statements were the valuation of the work-in-process receivables and net pension liability. The estimate of the WIP receivables is based on the percentage of the audit completed divided by the total budgeted hours for the audit. The auditor's conclusion regarding the reasonableness of this estimate is based on accuracy of the estimates based on these factors. Management's estimate of the net pension liability is based on an actuary's calculation in accordance with the employment contracts. We evaluated the key factors and assumptions used to develop the net pension liability in determining that it is reasonable in relation to the financial statements taken as a whole.

- 3. Identify any significant audit adjustments?**

Yes – See finding 2017-A

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

None

- 5. Identify any serious difficulties encountered in performing the audit.**

None

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

None

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

None

- 8. 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 assessed by auditors are directly related to the operations of an information technology system.**

None

This report is intended solely for the information and use of the Legislative Audit and Fiscal Review Committee, management, and other state officials, and is not intended to be and should not be used by anyone other than these specified parties.

Eide Bailly LLP

Bismarck, North Dakota
January 5, 2018



**Independent Auditor's 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***

Governor of North Dakota
The Legislative Assembly

Office of the State Auditor
Bismarck, North Dakota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Office of the State Auditor as of and for the years ended June 30, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the Office of the State Auditor's basic financial statements, and have issued our report thereon dated January 5, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Office of the State Auditor'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 Office of the State Auditor's internal control. Accordingly, we do not express an opinion on the effectiveness of the Office of the State Auditor's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described in the accompanying schedule of findings and responses, we identified a certain deficiency in internal control that we consider to be a material weakness.

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

We consider the deficiency described in the accompanying schedule of findings and responses as item 2017-A to be a material weaknesses.

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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Office of the State Auditor'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*.

Office of the State Auditor's Response to Findings

Office of the State Auditor's response to the findings identified in our audit are described in the accompanying schedule of findings and responses. Office of the State Auditor's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

A handwritten signature in black ink that reads "Eide Bailly LLP". The signature is written in a cursive, flowing style.

Bismarck, North Dakota
January 5, 2018

2017-A Audit Adjustments

Criteria: The work in process balance should not include a job that is also included in the accounts receivable balance.

Condition: The work in process balance did not appropriately reflect the amount earned by the Office of the State Auditor at the end of each fiscal year.

Cause: The discrepancy was caused in part by a formula error in the work in process worksheet and in part due to jobs not being taken out of the work in process balance before being reported in the accounts receivable balance and going undetected by someone within the entity.

Effect: The financial statements needed to be adjusted by \$23,950 for the year ended June 30, 2017, and \$9,200 for the year ended June 30, 2016.

Recommendation: We recommend the work in process and accounts receivable worksheets be appropriately reviewed to ensure correct formulas and to prevent job balances from being duplicated.

Views of Responsible Officials: The Office of the State Auditor concurs with this recommendation and will put procedures in place to ensure accounts receivables and work in progress are properly computed and reported.