

**NORTH DAKOTA DEPARTMENT OF TRUST LANDS
BISMARCK, NORTH DAKOTA**

AUDITED FINANCIAL STATEMENTS

FOR THE YEAR ENDED JUNE 30, 2017

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CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To the Governor of North Dakota
The Legislative Assembly
North Dakota Department of Trust Lands
Bismarck, North Dakota

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the North Dakota Department of Trust Lands, a department of the State of North Dakota, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the North Dakota Department of Trust Lands' 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 these 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit 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 North Dakota Department of Trust Lands, as of June 30, 2017, and the respective changes in financial position and the statement of appropriations for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1 to the financial statements, the financial statements of North Dakota Department of Trust Lands are intended to present the net position, revenues and expenses of only that portion of the financial statement of the State of North Dakota that is attributable to the transactions of the North Dakota Department of Trust Lands. They do not purport to, and do not, present fairly the financial position or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 27 of the financial statements, the North Dakota Department of Trust Lands reclassified one of the funds from a special revenue fund to a fiduciary fund. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 - 9, the schedule of contributions and schedule of employer's proportionate share of net pension liability on pages 52 and 53 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the North Dakota Department of Trust Lands' basic financial statements. The combining and individual nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining and individual nonmajor fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining and individual nonmajor fund financial statements are fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 23, 2017 on our consideration of North Dakota Department of Trust Lands' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Agency's internal control over financial reporting and compliance.



**BRADY, MARTZ & ASSOCIATES, P.C.
BISMARCK, NORTH DAKOTA**

October 23, 2017

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2017

As management of the North Dakota Department of Trust Lands (the Department), our discussion and analysis of the Department's financial performance provides an overview of the financial activities for the fiscal years ended June 30, 2017 and 2016. Please read it in conjunction with the basic financial statements, which follow this discussion.

Financial Highlights

- The assets and deferred outflows of the Department exceeded its liabilities and deferred inflows as of June 30, 2017 and 2016 by \$4,682,355,712 and \$4,346,135,622, respectively.
- The Department's net position increased by \$337,360,195 for the year ending June 30, 2017, and decreased by \$294,569,389 for the year ending June 30, 2016. The net position increase for fiscal year 2017 is due to an increase in gross production and oil extraction taxes, and investment returns.
- Royalty revenues totaled \$192,039,448 in fiscal year 2017, an increase of \$12,952,915 over the amount earned in fiscal year 2016. Royalty revenues totaled \$179,086,533 in fiscal year 2016. The increase in fiscal year 2017 was due to stable oil prices.
- Mineral lease bonus revenues totaled \$8,722,669 in fiscal year 2017, a decrease of \$3,694,721 when compared to fiscal year 2016. Bonus revenues totaled \$12,417,390 in fiscal year 2016. This decrease occurred because mineral acres in prime Bakken areas are leased and new acreage being nominated for lease auction is now outside prime Bakken areas.
- Gross production tax revenues in fiscal year 2017 totaled \$104,345,426, an increase of \$76,761,720 over the \$27,583,706 in fiscal year 2016.
 - Gross production tax revenues received by the Strategic Investment and Improvements fund (SIIF) totaled \$58,124,279 in fiscal year 2017. During fiscal year 2016, the SIIF did not receive any gross production tax revenues. The changes in deposits from fiscal year 2016 to fiscal year 2017 is a result of the distribution formula, which results in higher distributions to the SIIF during the second year of each biennium versus the first year.
 - Gross production tax revenues received by the oil and gas impact grant fund total \$46,221,147 in fiscal year 2017, compared to \$27,583,706 in fiscal year 2016. The revenue changes from year to year are a result of a change in the gross production tax formula as directed by the legislature for the biennium.
- Oil extraction tax revenues received in fiscal year 2017 total \$135,549,207, an increase of \$75,911,018 over the \$59,638,189 earned in fiscal year 2016.
 - Oil extraction tax revenues received by the Common School Trust fund totaled \$57,132,278 in fiscal year 2017, compared to \$59,638,189 in fiscal year 2016. These tax revenue changes are due to lower crude oil prices over the past two years.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
JUNE 30, 2017

- Oil extraction tax revenues received by the Strategic Investment and Improvements fund (SIIF) totaled \$78,416,929 in fiscal year 2017. During fiscal year 2016 the SIIF did not receive any oil extraction tax revenues. Oil extraction tax revenues are deposited into the SIIF in accordance with NDCC 57-51.1-07.5. The increase in deposits is a result of the distribution formula, which results in higher distributions to the SIIF during the second year of each biennia versus the first year.
- Investment income, including interest income, loan income and securities lending income, totaled \$102,397,155 in fiscal year 2017, an increase of \$17,384,085 over fiscal year 2016. Investment income totaled \$85,013,070 in fiscal year 2016. Although loan income was down substantially, due to the transfer of the school construction loan assistance fund to BND, permanent investment income grew by more than 19%, driven by combination of trust growth, higher interest rates, and the full funding of the trusts' real estate portfolio.
- The change in fair value of investments, otherwise known as capital gains/loss, reflects a gain of \$270,374,270 in fiscal year 2017, an increase of \$358,686,676 over the \$88,312,406 losses experienced in fiscal year 2016. Losses of more than 9% in the permanent trusts' diversified inflation strategies and international equities portfolios drove negative results in fiscal year 2016. Equity returns of near 20%, and returns of nearly 10% for the trusts' absolute return and real estate portfolios were the primary drivers of fiscal year 2017 gains.

Overview of the Financial Statements

This report consists of four parts – management's discussion and analysis (this section), the basic financial statements, required supplementary information, and a section that presents combining statements for non-major government funds. The basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements.

Government-Wide Financial Statements. The *government-wide financial statements* provide broad information about the Department's financial condition.

The *statement of net position* presents information on all assets and deferred inflows of resources and liabilities and deferred inflows of resources managed by the Department with the difference between these reported as *net position*. Changes in net position may at times, serve as a useful indicator of whether the financial position of the Department is improving or deteriorating.

The *statement of activities* presents information showing how the net position managed by the Department changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows.

Fund Financial Statements. A *fund* is a grouping of related accounts used to maintain control of resources that have been segregated for specific objectives. The Department uses fund accounting to provide a relevant financial statement format for users and to demonstrate compliance with constitutional and legislative requirements. All of the funds of the Department are governmental funds.

Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the Common Schools

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
JUNE 30, 2017

Trust fund, Coal Development Trust fund, Department of Trust Lands General fund, Oil and Gas Impact Grant fund, School Construction Assistance Loan fund, and the Strategic Investment and Improvements fund. Data from the other thirteen governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these is provided in the *combining statements* immediately following the notes to the financial statements.

The Department is appropriated a biennial budget from the North Dakota Legislature for its General fund. A statement of appropriation statement has been provided to demonstrate compliance with this budget.

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

Government-Wide Financial Analysis

As noted earlier, changes in net position may, at times, serve as a useful indicator of the Department's financial position. As of June 30, 2017, the Department's total net position was \$4,682,355,712. As of June 30, 2016, the Department's total net position was \$4,346,135,622. The largest portion of the Department's net position is represented by investments in financial securities. The Department uses this net position to provide distributions to educational entities and general government.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
JUNE 30, 2017

The following is a comparative statement of net position:

Condensed Statement of Net Position

	2017	2016
Current and other assets	\$ 4,896,805,154	\$ 4,512,952,452
Capital assets	7,755,857	7,762,092
Total assets	4,904,561,011	4,520,714,544
Deferred pension outflows	710,051	164,533
Long-term liabilities	2,109,611	1,402,461
Other liabilities	220,693,335	173,206,557
Total liabilities	222,802,946	174,609,018
Deferred pension inflows	112,404	134,437
Net Position:		
Net position invested in capital assets	7,755,857	7,762,092
Restricted net position		
Nonexpendable	68,887,821	67,997,836
Expendable	4,183,723,624	3,739,964,835
Unrestricted net position	421,988,410	530,410,859
Total net position	\$ 4,682,355,712	\$ 4,346,135,622

During fiscal year 2017, the Department's net position increased by \$337,360,195. The main change relates to gains in fair value of investments and oil extraction taxes deposited into the Common Schools Trust fund during the year.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
JUNE 30, 2017

The following provides a comparative statement of the Department's operations:

	2017	2016
<u>Revenues</u>		
<i>General Revenues:</i>		
Interest on investments	\$ 5,596,574	\$ 3,381,320
Change in fair value of investments	(536,525)	1,644,442
Interest income	75,317	96,166
Royalties	67,956,040	65,932,309
Bonuses	5,229,065	6,483,598
Rents	269,240	314,934
Interest on loans	1,774,078	2,930,054
Contributions to perpetual funds	11,895,026	15,637,987
Taxes	243,036,900	90,353,041
Gain on Sale of Capital Asset - Land	306	4,632,556
Total General Revenue	335,296,021	191,406,407
 <i>Program Revenues:</i>		
Interest on loans	633,805	848,916
Interest on investments	94,317,381	77,756,614
Change in fair value of investments	270,910,795	(89,956,848)
Royalties	124,083,408	113,154,224
Bonuses	3,493,604	5,933,792
Rents	12,859,385	12,497,923
Fees to Maintenance fund	5,532,792	4,476,326
Total Program Revenue	511,831,170	124,710,947
Total Revenues	847,127,191	316,117,354
 <u>Expenses</u>		
<i>Governmental Activities:</i>		
General government	1,430,446	1,244,485
Intergovernmental	26,674,859	114,001,692
Education	19,274,511	17,051,017
Total Expenses	47,379,816	132,297,194
 Excess before transfer	 799,747,375	 183,820,160
Transfers	(462,387,180)	(478,389,549)
Increase(decrease) in net position	337,360,195	(294,569,389)
 Net position - beginning	 4,346,135,622	 4,640,705,011
Change in statement presentation	(1,140,105)	
Net position - beginning of year restated	4,344,995,517	4,640,705,011
Net position - ending	\$ 4,682,355,712	\$ 4,346,135,622

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
JUNE 30, 2017

During the fiscal year ending June 30, 2017, the Department's revenues increased by a total of \$535,642,087. Royalty revenues increased by \$12,952,915 as commodity prices were higher. Mineral lease bonus revenue declined by \$3,694,721 as most mineral acreage in the area of the Bakken formation are leased. Oil extraction and gross production tax revenues increased by \$75,911,018 and \$76,761,720, respectively, due primarily to the tax distribution formula, which resulted in higher distributions to the SIIF during the second year of each biennia versus the first year. The change in fair value of investments for fiscal year 2017 was a gain of \$358,686,676 from the previous year as capital markets produced stronger gains.

Financial Analysis of the Government's Funds

As noted earlier, the Department uses fund accounting to ensure and demonstrate compliance with finance-related constitutional and legislative requirements.

Governmental funds. The focus of the Department's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the Department's financing requirements.

Capital Asset

The Department's capital assets for its governmental funds as of June 30, 2017 are \$7,755,857 (net of accumulated depreciation for equipment), respectively. These capital assets include land and equipment. See Note 16 to Financials Statements for additional details on capital assets.

Economic Factors

During fiscal year 2017, trust assets experienced an increase primarily as a result of gross production and oil extraction taxes allocated to the SIIF and higher investment returns as compared to prior fiscal years. While crude production remained relatively stable, lower crude oil pricing also remained stable affecting oil and royalties, mineral leasing and bonuses. During the Sixty-fifth Legislative assembly, several bills with emergency clauses transferred a total of \$20 million from SIIF to various State agencies as part of their appropriations or special project needs.

Requests for Information

This financial report is designed to provide a general overview of the Department's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the ND Department of Trust Lands, 1707 N 9th St., PO Box 5523, Bismarck, ND, 58506-5523.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
STATEMENT OF NET POSITION
JUNE 30, 2017

<u>Assets</u>	Governmental Activities
Cash	\$ 216,708,012
Investments	4,324,726,551
Interest receivable	14,289,804
Accounts receivable	23,333,895
Invested securities lending collateral	207,497,316
Loans	
Farm loans	7,626,699
Energy construction loans	1,216,168
School loans	48,247,859
Energy impact loans	12,659,515
Capital asset - land	7,740,063
Due from other state agencies	34,605,547
Equipment (net of accumulated depreciation)	15,794
Restricted assets:	
Cash and cash equivalents	5,893,788
Total Assets	4,904,561,011
<u>Deferred Outflows of Resources</u>	
Deferred pension outflows	710,051
<u>Liabilities</u>	
Accrued payroll	253,479
Accounts payable	1,661,118
Securities lending collateral	207,497,316
Due to other state agencies	405,442
Claimant liability	10,875,980
Long-term liabilities:	
Compensated absences due within one year	11,763
Compensated absences due in more than one year	208,484
Pension liability	1,889,364
Total Liabilities	222,802,946
<u>Deferred Inflows of Resources</u>	
Deferred pension inflows	112,404
<u>Net Position</u>	
Net investment in capital assets	7,755,857
Restricted	
Nonexpendable	68,887,821
Expendable	4,183,723,624
Unrestricted	421,988,410
Total Net Position	\$ 4,682,355,712

See Notes to the Financial Statements

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2017

Functions/Programs of Governmental activities:	Program Revenues			Net (Expense) Revenue
	Expenses	Charges for Services	Operating Grants and Contributions	
General government	\$ 1,430,446			\$ (1,430,446)
Intergovernmental	26,674,859			(26,674,859)
Education	19,274,511	\$ 5,532,792	\$ 506,298,378	492,556,659
Total	\$ 47,379,816	\$ 5,532,792	\$ 506,298,378	464,451,354
Net revenue				464,451,354
General revenues:				
Taxes:				
Coal severance				3,142,267
Oil extraction				135,549,207
Gross production				104,345,426
Contributions to special revenue fund				11,895,026
Unrestricted investment earnings				5,596,574
Net increase (decrease) in fair value of investments				(536,525)
Royalties				67,956,040
Bonuses				5,229,065
Rents				269,240
Loan income				1,774,078
Interest Income				75,317
Gain on sale of capital asset – land				306
Transfers:				
To/from other state agencies				(352,840,180)
Educational institutions				(109,547,000)
Total general revenues and transfers				(127,091,159)
Total change in net position				337,360,195
Net position - beginning of year as previously stated				4,346,135,622
Change in financial presentation				(1,140,105)
Net position - beginning of year, restated				4,344,995,517
Net position - ending				\$ 4,682,355,712

See Notes to the Financial Statements

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2017

Assets:	General Fund	Common Schools Trust Fund	Coal Development Trust Fund	Oil and Gas & Flood Impact Grant Funds	Strategic Investment & Improvements Fund	School Construction Assistance Loan Fund	Other Governmental Funds	Total
Cash	\$ 3,468,764	\$ 16,313,100	\$ 144,810	\$ 56,576,800	\$ 139,366,637	\$	\$ 837,901	\$ 216,708,012
Investments		3,889,084,286	7,803,244		194,081,810		233,757,211	4,324,726,551
Interest receivable		12,843,762	74,880		530,786		840,376	14,289,804
Accounts receivable		14,683,108			6,965,515		1,685,272	23,333,895
Invested securities lending collateral		160,471,349	1,457,495		35,367,942		10,200,530	207,497,316
Loans								
Farm		7,025,144					601,555	7,626,699
Energy construction		1,216,168						1,216,168
School			48,247,859					48,247,859
Energy impact			12,659,515					12,659,515
Due from other state agencies		9,519,872	509,727		24,575,948			34,605,547
Due from other funds		1,800,881			1,302,434		82,685	3,186,000
Restricted assets:								
Cash and cash equivalents					5,893,788			5,893,788
Total Assets	\$ 3,468,764	\$ 4,112,957,670	\$ 70,897,530	\$ 56,576,800	\$ 408,084,860	\$	\$ 248,005,530	\$ 4,899,991,154
Liabilities:								
Accrued payroll	\$ 244,269	\$	\$	\$ 9,210	\$	\$	\$	\$ 253,479
Accounts payable	36,830	1,477,988	2,279		55,355		88,666	1,661,118
Securities lending collateral		160,471,349	1,457,495		35,367,942		10,200,530	207,497,316
Due to other state agencies	28,572	17,365	356,809	1,210			1,486	405,442
Due to other funds	3,186,000							3,186,000
Claimant liability		10,875,980						10,875,980
Total Liabilities	3,495,671	172,842,682	1,816,583	10,420	35,423,297	\$	10,290,682	223,879,335
Fund Balance:								
Fund Balance:								
Permanent funds								
Nonspendable			68,887,821					68,887,821
Committed			193,126					193,126
Special revenue funds								
Restricted		3,940,114,988			5,893,788		237,714,848	4,183,723,624
Committed				56,566,380	193,803,354			250,369,734
Assigned					229,325,049			229,325,049
Unassigned	(26,907)				(56,360,628)			(56,387,535)
Total Fund Balance	(26,907)	3,940,114,988	69,080,947	56,566,380	372,661,563	\$	237,714,848	4,676,111,819
Total Liabilities and Fund Balances	\$ 3,468,764	\$ 4,112,957,670	\$ 70,897,530	\$ 56,576,800	\$ 408,084,860	\$	\$ 248,005,530	\$ 4,899,991,154

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

Total fund balances - governmental funds	\$ 4,676,111,819
Capital asset - land	7,740,063
Net book value of equipment	15,794
Liability for compensated absences	(220,247)
Net pension liability	(1,889,364)
Deferred pension outflows	710,051
Deferred pension inflows	(112,404)
Net position of governmental activities	<u>\$ 4,682,355,712</u>

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2017

Revenues:	General Fund	Common Schools Trust Fund	Coal Development Trust Fund	Oil and Gas & Flood Impact Grant Funds	Strategic Investment & Improvements Fund	School Construction Assistance Loan Fund	Other Governmental Funds	Total
Investment income		\$ 88,363,607	\$ 144,605		\$ 4,728,592	\$ 12,101	\$ 5,894,412	\$ 99,143,317
Interest income					75,317			75,317
Loan income								
Farm loans		533,265					45,610	578,875
Energy construction		54,930						54,930
School loans-Coal			704,393					704,393
School construction loans-SCALF						1,069,685		1,069,685
Net increase (decrease) in fair value of investments		255,695,851	(18,123)		(506,057)		15,202,599	270,374,270
Securities lending income		600,720	5,218		126,626		38,074	770,638
Royalties		114,182,591			67,052,863		10,803,994	192,039,448
Bonuses		3,373,437			5,226,025		123,207	8,722,669
Rental income		11,846,054			100,598		1,181,973	13,128,625
Coal severance tax			3,142,267					3,142,267
Gross production tax				\$ 46,221,147	58,124,279			104,345,426
Oil extraction tax		57,132,278			78,416,929			135,549,207
Unclaimed property collections		7,817,110						7,817,110
Indirect recovery costs	\$ 5,532,792							5,532,792
Tobacco settlement		4,077,916						4,077,916
Total revenues	<u>5,532,792</u>	<u>543,677,759</u>	<u>3,978,360</u>	<u>46,221,147</u>	<u>213,345,172</u>	<u>1,081,786</u>	<u>33,289,869</u>	<u>847,126,885</u>
Expenditures:								
Current								
General government			19,943		1,239,432		36,613	1,295,988
Intergovernmental				26,674,859				26,674,859
Education	5,505,390	12,851,353				500	917,268	19,274,511
Total expenditures	<u>5,505,390</u>	<u>12,851,353</u>	<u>19,943</u>	<u>26,674,859</u>	<u>1,239,432</u>	<u>500</u>	<u>953,881</u>	<u>47,245,358</u>
Excess of revenue over (under) expenditures	<u>27,402</u>	<u>530,826,406</u>	<u>3,958,417</u>	<u>19,546,288</u>	<u>212,105,740</u>	<u>1,081,286</u>	<u>32,335,988</u>	<u>799,881,527</u>
Other Financing Sources (Uses):								
Transfer to Public Instruction		(103,067,000)						(103,067,000)
Transfer to Educational Institutions							(6,480,000)	(6,480,000)
Transfer to Lignite Research Fund			(2,199,587)					(2,199,587)
Transfer to State General Fund			(882,064)		(155,000,000)			(155,882,064)
Transfer to Facilities Management							(2,735,000)	(2,735,000)
Transfer to NDSU					(16,634,854)			(16,634,854)
Transfer to Bank of North Dakota						(153,220,175)		(153,220,175)
Transfer to Department of Transportation					(3,500,000)			(3,500,000)
Transfer to Department of Human Services					(9,000,000)			(9,000,000)
Transfer to Department of State Treasurer					(8,100,000)			(8,100,000)
Transfer to Legal Counsel for Indigents					(389,000)			(389,000)
Transfer to Adjutant General					(79,500)			(79,500)
Transfer to State Historical Society					(50,000)			(50,000)
Transfer to Department of Health					(250,000)			(250,000)
Transfer to ND Oil & Gas Division					(800,000)			(800,000)
Total other financing sources (uses)		<u>(103,067,000)</u>	<u>(3,081,651)</u>		<u>(193,803,354)</u>	<u>(153,220,175)</u>	<u>(9,215,000)</u>	<u>(462,387,180)</u>
Net Change in Fund Balance	<u>27,402</u>	<u>427,759,406</u>	<u>876,766</u>	<u>19,546,288</u>	<u>18,302,386</u>	<u>(152,138,889)</u>	<u>23,120,988</u>	<u>337,494,347</u>
Fund balance - beginning as previously stated	(54,309)	3,512,355,582	68,204,181	37,020,092	354,359,177	152,138,889	215,733,965	4,339,757,577
Change in financial presentation							(1,140,105)	(1,140,105)
Fund balance - beginning as restated	(54,309)	3,512,355,582	68,204,181	37,020,092	354,359,177	152,138,889	214,593,860	4,338,617,472
Fund balance - ending	<u>\$ (26,907)</u>	<u>\$ 3,940,114,988</u>	<u>\$ 69,080,947</u>	<u>\$ 56,566,380</u>	<u>\$ 372,661,563</u>	<u>\$ 152,138,889</u>	<u>\$ 237,714,848</u>	<u>\$ 4,676,111,819</u>

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

Net change in fund balance	\$ 337,494,347
Net value of capital asset - acquired land	306
Depreciation expense on equipment	(6,541)
Increase in compensated absences liability	(1,507)
Decrease in net pension liability	(693,961)
Changes in deferred outflows and inflow resources related to net pension liability	567,551
Change in net position of governmental activities	<u>\$ 337,360,195</u>

See Notes to the Financial Statements

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
STATEMENT OF FIDUCIARY NET POSITION
JUNE 30, 2017

<u>Assets</u>	<u>Indian Cultural Education Trust</u>
Cash	\$ 3,278
Investments	1,218,152
Interest receivable	2,864
Invested securities lending collateral	50,248
Total Assets	<u>1,274,542</u>
<u>Liabilities</u>	
Accounts payable	463
Securities lending collateral	50,248
Total Liabilities	<u>50,711</u>
<u>Net Position</u>	
Net position retracted for Indian Cultural Education	<u>1,223,831</u>
Total Net Position	<u>\$ 1,223,831</u>

See Notes to the Financial Statements

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
STATEMENT OF CHANGES IN FIDUCIARY NET POSITION
FOR THE YEAR ENDED JUNE 30, 2017

	Indian Cultural Education Trust
Additions	
Contributions:	
Donations	\$
Total Contributions	
Investment income:	
Net change in fair value of investments	82,357
Interest	28,397
Less investment expense	3,170
Net Investment Income	107,584
Securities Lending Activity:	
Securities lending income	188
Net Securities Lending Income	188
Miscellaneous Income	2,900
Total Additions	110,672
Deductions	
Payments in accordance with Trust agreement	26,547
Administrative expenses	399
Total Deductions	26,946
Change in net position held in Trust for:	
Private-Purpose	83,726
Total Change in Net Position	83,726
Net Position - Beginning of Year	1,140,105
Net Position - End of Year	\$ 1,223,831

See Notes to the Financial Statements

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
STATEMENT OF APPROPRIATIONS
FOR THE BIENNIUM ENDED JUNE 30, 2017

	Approved 2015-17 Biennial Appropriation	Final Adjusted Appropriation	2016 Expenditures	2017 Expenditures	Unexpended Appropriation
General Fund Appropriated Expenditures:					
Salaries and Wages	\$ 6,123,516	\$ 6,131,344	\$ 2,544,743	\$ 2,746,809	\$ 839,792
Operating Expenses	2,019,637	2,019,637	573,851	952,982	492,804
Contingencies	100,000	100,000	-	-	100,000
	<u>\$ 8,243,153</u>	<u>\$ 8,250,981</u>	<u>\$ 3,118,594</u>	<u>\$ 3,699,791</u>	<u>\$ 1,432,596</u>
Continuing Appropriations:					
Investments			\$ 16,768,498	\$ 21,497,686	
Land Management - Grant and Non-Grant			247,953	197,976	
County Services - Roads & Bridges			119,061	121,610	
In Lieu of Property Taxes			113,624	122,039	
Strategic Investment and Improvements fund			265,920	105,633	
Uniform Unclaimed Property			299,329	361,759	
Total*			<u>\$ 17,814,385</u>	<u>\$ 22,406,703</u>	

*This total represents the Department's expenditures through the State Treasurer's Office using the State's PeopleSoft system with the exception of investments. Investment manager fees are generally paid through the Payden & Rygel cash account on a quarterly basis, although some managers withhold fees directly from the mutual or commingled fund investments.

	Approved 2015-17 Biennial Appropriation	Final Adjusted Appropriation	2016 Expenditures	2017 Expenditures	Unexpended Appropriation
Oil and Gas Impact Grant Fund:					
Energy Infrastructure and Impact Grants	\$ 139,300,000	\$ 139,300,000	\$ 27,403,058	\$ 16,294,975	\$ 95,601,967
Energy Infrastructure and Impact Operating	700,000	700,000	319,313	253,929	126,758
Flood Infrastructure Development Grants		5,981,231	3,301,991		2,679,240
	<u>\$ 140,000,000</u>	<u>\$ 145,981,231</u>	<u>\$ 31,024,362</u>	<u>\$ 16,548,904</u>	<u>\$ 98,407,965</u>

	Approved 2015-17 Biennial Appropriation	2016 Expenditures (including 2016 Emergency Clause)	19 Biennial with Emergency Clause	2017 Expenditures	Unexpended Appropriation
Strategic Investment and Improvements Fund:					
ND Department of Transportation (HB 1012)	\$ 7,000,000	3,500,000	\$ -	3,500,000	\$ -
ND Industrial Commission (HB 1014)	13,625,322	\$ 13,625,322	-	-	-
ND Commerce Department (HB 1018)	7,500,000	7,500,000	-	-	-
Main Research Center (HB 1020)	18,000,000	3,000,000	-	15,000,000	-
Commission on Legal Counsel for Indigents (HB 1024)	200,000	-	-	200,000	-
ND Commerce Department (HB 1285)	650,000	650,000	-	-	-
Bank of North Dakota (HB 1443)	50,000,000	50,000,000	-	-	-
Bank of North Dakota (SB 2012)	49,891,582	49,891,582	-	-	-
Bank of North Dakota (SB 2039)	150,000,000	150,000,000	-	-	-
ND State Treasurer & ND Department of Transportation (SB 2013)	1,100,000,000	1,100,000,000	-	-	-
Legal Counsel of Indigents (HB 1024)			189,000	189,000	-
ND Department of Health (HB 1024)			250,000	250,000	-
ND Department of Human Services (HB 1024)			9,000,000	9,000,000	-
Adjutant General (HB 1024)			79,500	79,500	-
ND State Historical Society (HB 1024)			50,000	50,000	-
ND State Treasurer (HB 1024)			8,100,000	8,100,000	-
ND Attorney General (HB 1024)			15,872,000	-	15,872,000
ND Department of Mineral Resources (SB 2134)			800,000	800,000	-
ND State University (HB 1015)			1,634,854	1,634,854	-
Office of Management & Budget (HB 1024)			155,000,000	155,000,000	-
	<u>\$ 1,396,866,904</u>	<u>\$ 1,378,166,904</u>	<u>\$ 190,975,354</u>	<u>\$ 193,803,354</u>	<u>\$ 15,872,000</u>

See Note 22 to Financial Statements on the Department's continuing appropriation authority of funding.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Statements and Reporting Entity

The North Dakota Department of Trust Lands (Department) is an agency of the State of North Dakota. The Board of University and School Lands (Board) was created under Article IX, Section 3 of the North Dakota State Constitution, and operates through the legislative authority of the N.D.C.C. Title 15, Chapters 47-30.1 and 57-62. The Board is the governing authority of the Department. As a state agency, the Department is considered to be a department of the State of North Dakota and is included in the State's Comprehensive Annual Financial Report.

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (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 Department has included all funds and has considered all potential component units for which the Department is financially accountable, and other organizations for which the nature and significance of their relationship with the Department are such that exclusion would cause the Department's financial statements to be misleading or incomplete.

The GASB has set forth criteria to be considered in determining financial accountability. This criteria includes appointing a voting majority of an organization's governing body and (1) the ability of the Board 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 Board. Based upon these criteria, there are no component units to be included within the Department's statements and the Department is a reporting entity within the State of North Dakota as a reporting entity.

Fund Accounting Structure

The Department uses funds to report its financial position and the results of its operations. Fund accounting is designed to demonstrate constitutional and legislative compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts. The accounting and reporting treatment applied to a fund is determined by its measurement focus.

Governmental fund balance is classified on a hierarchy that shows, from the highest to the lowest, the level or form of constraints on fund balance and accordingly, the extent to which the Department is bound to honor them: nonspendable, restricted, committed, assigned and unassigned.

The following fund types and funds are used to account for the Department's activities.

General Fund – include operating fund activities financed by the trusts that are legislatively assigned for specified purposes.

The Department maintenance fund is used to pay operating expenses of the department. The Department maintenance fund is the general fund.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

Permanent Fund – report resources that are constitutionally committed for distribution purposes as described in Article X of the State Constitution and N.D.C.C. Chapter 57-61.

The Coal Development Trust fund receives a portion of the coal severance tax. The Trust transfers a portion of the coal severance tax to the lignite research fund for lignite research and clean coal projects as enacted by the legislative assembly for future distribution. As described in N.D.C.C. Chapters 15.1-36 and 57-62, the Trust also makes loans to coal development impacted counties, cities and school districts and low interest loans to school districts for new construction. Interest earned on moneys from the Trust is distributed to the State general fund.

Special Revenue Funds - include fund activities financed by specific revenue sources that are constitutionally and legislatively restricted, committed or assigned to expenditures for specified purposes.

The Common Schools Trust funds account for all assets and proceeds as described in Section 11 through 19 of the Enabling Act of 1889, Article IX of the State Constitution and N.D.C.C. Chapter 15-01-02. The beneficiaries of the Common Schools Trust are publicly funded schools, grades K-12. Other beneficiaries of the Educational Trust funds are the North Dakota State University, School for the Blind, School for the Deaf, State Hospital, Valley City State University, Mayville State University, Youth Correctional Center, State School of Science, Veterans Home, and the University of North Dakota. Income from the assets held by the Ellendale Trust are allocated equally among Dickinson State University, Minot State University, Dakota College at Bottineau, School for the Blind, Veterans Home, State Hospital, and State College of Science. The benefits of the original grant to the School of Mines are distributed to the University of North Dakota. The Trusts own assets in the form of rangeland, producing and non-producing mineral interests, investment securities, farm and energy construction loans and an office building. The Common Schools Trust fund is also used to account for unclaimed property collected under the authority of N.D.C.C. Chapter 47-30.1-23.

The Strategic Investment and Improvements (SIIF) fund accounts for producing and non-producing mineral interests formerly owned by the Bank of North Dakota (BND) and State Treasurer, and acres located under navigable streams, rivers, and lakes, which are owned by North Dakota as a sovereign state. The Trust receives revenues from mineral bonuses, mineral royalties and a portion of the State's share of gross production and oil extraction taxes once certain thresholds are met. In accordance with NDCC 15-08.1-08, the SIIF may be expended as the legislature provide for one-time expenditures related to improving state infrastructure or for initiatives to improve the efficiency and effectiveness of state government.

The Oil, Gas and Flood Impact Grant fund provides grant assistance to counties, cities, school districts and other political subdivisions impacted by oil or gas development through the oil and gas impact grant fund. The program is funded with a percentage of the oil and gas gross production tax as enacted by the legislative assembly. In addition, the Energy Infrastructure and Impact Office administers the Flood-Impacted Political Subdivision Infrastructure Development Grants program by providing infrastructure development grants to flood-impacted political subdivisions. The program is funded with one-time State general fund moneys and expires June 30, 2019.

The School Construction Assistance Loan fund is a special revolving loan fund in the State Treasury for the purpose of providing low-interest school construction loans in accordance with NDCC 15.1-36. All interest or other earnings of the fund, and all repayments of loans collected by

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

the fund will remain in the fund. In January 2017, the North Dakota legislature approved the transfer of this fund from the Department to the Bank of North Dakota, whom will manage this fund as a revolving loan fund.

The Department reports the Common Schools Trust fund, Coal Development Trust fund, Department's General fund, Oil and Gas Impact Grant fund, School Construction Assistance Loan fund, and Strategic Investment and Improvements Trust fund as major governmental funds.

Private Purpose Trust Fund – accounts for resources of trust arrangements in which principal and income benefit individuals, private organizations, or other governments.

The Indian Cultural Educational Trust "is established for the purpose of generating income to benefit Indian culture." The beneficiary of the Indian Cultural Educational Trust is the Mandan, Hidatsa and Arikara Nation Cultural Education Foundation. The Trust receives revenues from surface rental income.

Basis for Accounting

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. For this purpose, the State generally considers tax revenues to be available if they are collected within one year of the end of the fiscal period.

All revenues in the perpetual funds except for taxes, tobacco settlement money and unclaimed property revenue are presented as program revenues.

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

Budgetary Policies and Procedures

The Department operates through a biennial appropriation provided by the State Legislature and other continuing appropriations. The Department prepares a biennial budget which is included in the Governor's budget that is presented to the General Assembly at the beginning of each legislative session. The General Assembly enacts the budgets of the various state departments through passage of specific appropriation bills. Before signing the appropriation bills, the Governor may veto any specific appropriation, subject to legislative override. Changes to the appropriation are limited to Emergency Commission authorization, initiative, or referendum action. Unexpended appropriations lapse at the end of the biennium.

Due to the lack of a formal revenue budget, a Combined Statement of Revenues, Expenditures, and Changes in Fund Balances - Budget and Actual statement cannot be prepared as required by GAAP. In its place, a Statement of Appropriations has been presented. The Statement of Appropriations has been prepared using the modified accrual basis and encumbrance accounting is not used.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

Cash Deposits and Investments

Cash includes all funds deposited with the BND as well as certain funds deposited in The Northern Trust (TNT) Cash Pool at Northern Trust.

Investments are reported at fair value. All investment income, including changes in the fair value, is recognized in the statements of revenues, expenditures and changes in fund balance.

Cash for all funds is pooled and invested to the extent possible. Income earned from pooled investments is allocated to each of the funds based on the fund's total contribution to the pool.

Accounts Receivable

Accounts receivable represents accrued amounts on royalty revenue and interest on investments not available on June 30, 2017 for funding of current operations. A majority of the accrued royalty revenue is expected to be collected within the first 90 days following June 30, 2017. All receivables are considered collectible.

Claimant Liability

Claimant liability represents the value of property escheated to the Department and expected to be repaid to the rightful owners or their heirs. Escheated property can be reclaimed into perpetuity thus is a liability for the amounts expected to be reclaimed and paid.

Capital Assets

Capital assets includes original grant, pre-1980 acquired properties and cancelled contract lands valued at \$10.00 per acre, and post-1980 acquired properties valued at historical cost or fair value, and equipment valued at historical cost or at estimated historical cost if actual cost is not available. Donated capital assets are valued at their estimated fair value on the date of donation.

All other capital assets with an original cost of \$5,000 or more per unit and an estimated useful life in excess of one year are capitalized and reported in the applicable governmental activities columns in the government-wide financial statements in accordance with N.D.C.C. Chapter 54-27-21. 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 or construct them in the governmental fund financial statements. Capital assets, along with equipment, accumulated depreciation and depreciation expense, are reported in the applicable governmental activities columns in the government-wide financial statements.

Land is not depreciated. Other capital assets are depreciated using the straight-line method over 3 to 10 years for all furniture and equipment.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

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.

Deferred Outflows / Inflows of Resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and will not be recognized as an outflow of resources (expense/ expenditure) until then. The Department has one item reported on the statement of net position as cost sharing defined benefit pension plan, which represents actuarial differences within the NDPERS pension plans. See Note 24 to financial statements for additional details on Department's Pension Plan.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and will not be recognized as an inflow of resources (revenue) until that time. The Department has one type of item, which arises only under a modified accrual basis of accounting that qualifies for reporting in this category. See Note 24 to financial statements for additional details on Department's Pension Plan.

Compensated Absences Payable

N.D.C.C. Chapter 54-06-14 allows employees to accrue annual leave at a varying rate between one and two days per month based on years of service. In general, accrued annual leave cannot exceed thirty days at each calendar year end. Employees are paid for unused annual leave upon termination or retirement.

Sick leave is accrued at the rate of one day per month without limitation on the amount that can be accumulated. Employees vest in sick leave at ten years of service at which time the State is liable for ten percent of the employee's accumulated unused sick leave.

Assets of the maintenance fund are used to pay off these liabilities.

NOTE 2 – ORGANIZATION AND RELATED PARTY TRANSACTIONS

As stated in Note 1, the Department is an entity of the state of North Dakota and as such, other state agencies of the state and political subdivisions are related parties.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

NOTE 3 – CASH

Custodial Credit Risk

State law generally requires that all state funds be deposited in the BND. N.D.C.C. Chapter 21-04-01 provides that public funds belonging to or in the custody of the state shall be deposited in the BND. Also, N.D.C.C. Chapter 6-09-07 states, “[a]ll state funds ... must be deposited in the Bank of North Dakota” or must be deposited in accordance with constitutional and statutory provision.

The carrying amount of deposits with the BND was \$86,051,026 while Northern Trust was \$136,550,774 as of June 30, 2017, and the bank balances were \$149,095,518. These differences result from timing differences of deposits processed by the Bank at year-end. These deposits are exposed to custodial credit risk as uninsured and uncollateralized. However, deposits held at the BND are guaranteed by the State of North Dakota through N.D.C.C. Chapter 6-09-10. The Department does not have a formal policy regarding deposits.

NOTE 4 – FUND BALANCE CLASSIFICATION

The following fund balance classifications describe the spending constraints placed on the purpose for which resources can be used:

Nonspendable: this classification includes amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact as directed by legislation or the state constitution.

The Coal Development Trust fund was established by Article X of the State Constitution. This fund is held in trust and administered by the Board for loans to coal impacted counties, cities and school districts and for loans to school districts throughout the state. The Coal Development Trust fund balance includes the corpus (or principal) of this fund and the long-term portion of loans receivable, therefore is not in spendable form.

Restricted: this classification includes amounts for which constraints have been placed on the use of the resources either (a) imposed by the beneficiary of the assets or (b) imposed by law through constitutional provisions or enabling legislation.

The Common School and other Perpetual Education trust funds were created under the State Constitution to support school and public institutions. All revenue resources are restricted for the purpose of distributions to the beneficiaries.

The Capitol Building fund was created under the State Constitution for the construction and maintenance of public buildings at the capital. The entire balance of the trust is subject to legislative appropriation each biennium.

The Strategic Investment and Improvements fund has restricted funds to cover the possible default of loans for the Fuel Production Facilities program that is administered by the Bank of North Dakota.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

Committed: this classification includes amounts that can be used only for the specific purpose imposed by formal action of the legislative assembly or the Board.

The Coal Development Trust fund was established by Article X of the State Constitution. Any changes to the fund balance commitment would require a referendum and vote of the people of the State of North Dakota. Interest earned on the moneys held in this trust will first replace uncollectable loans made from this trust, and any remaining balance will be transferred to the State general fund.

The Oil and Gas Impact Grant fund holds funds appropriated by the state legislature to assist local political subdivisions in dealing with problems arising from oil and gas development. Any changes to the fund balance commitment would require an appropriation bill action of the legislative assembly.

The Flood-Impacted Political Subdivision Infrastructure Development Grant program is administered by the Energy Infrastructure and Impact Office and allocates funds appropriated by the state legislature to provide infrastructure development grants to flood-impacted political subdivisions. This funding is considered a one-time funding item from the State general fund and expired June 30, 2017. Any changes to the fund balance commitment would require appropriation bill action of the legislative assembly.

The Strategic Investment and Improvements fund was established by legislation and consists of mineral acres formerly owned by the BND and State Treasurer, minerals located under navigable streams, rivers, and lakes, which are owned by North Dakota as a sovereign state, and various financial assets. The balance of this fund is subject to appropriation by the legislature. Any changes to the fund balance commitment would require action of the legislative assembly to change the North Dakota century code.

Assigned: this classification includes amounts that can be used only for the specific purpose imposed by formal action of the legislative assembly or the Board, but do not meet the criteria to be classified as restricted or committed.

The Strategic Investment and Improvements fund has assigned funds by the Board to indicate that these funds should not be transferred out of this fund until potential title disputes related to riverbed leases have been resolved.

Unassigned: the residual classification for the general fund and also reflects negative residual amounts in other funds.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

Fund Balances	General Fund	Common Schools Trust Fund	Coal Development Trust Fund	Oil and Gas & Flood Impact Grant Fund	Strategic Investment & Improvements Fund	Other Governmental Funds	Total
Permanent Funds:							
<i>Nonspendable</i>							
Permanent fund principal			\$ 68,887,821				\$ 68,887,821
<i>Committed</i>							
Designated for transfer to State general fund			193,126				193,126
Special Revenue Funds:							
<i>Restricted</i>							
Distribution to educational beneficiaries		\$ 3,940,114,988				\$ 232,624,972	4,172,739,960
Capitol building maintenance						5,089,876	5,089,876
Fuel production facility - BND					\$ 5,893,788		5,893,788
<i>Committed</i>							
Grants				\$ 56,566,380			56,566,380
Designated for transfer to(from):							
Adjutant General					79,500		79,500
General Fund of North Dakota					155,000,000		155,000,000
Legal Counsel of Indigents					389,000		389,000
ND Department of Health					250,000		250,000
ND Department of Human Services					9,000,000		9,000,000
ND Department of Transportation					3,500,000		3,500,000
ND Oil and Gas Division					800,000		800,000
ND State Historical Society					50,000		50,000
ND State University					16,634,854		16,634,854
Office of ND State Treasurer					8,100,000		8,100,000
<i>Assigned</i>							
Potential mineral title disputes					229,325,049		229,325,049
<i>Unassigned</i>							
Operating Expenses	\$ (26,907)				(56,360,628)		(56,387,535)
Total Fund Balances:	\$ (26,907)	\$ 3,940,114,988	\$ 69,080,947	\$ 56,566,380	\$ 372,661,563	\$ 237,714,848	\$ 4,676,111,819

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

NOTE 5 – INVESTMENTS

The Board's investment policy is to invest trust assets in a manner that balances the growth of the portfolio with the need to meet constitutionally required distributions. This is accomplished by investing in a widely diversified portfolio.

N.D.C.C. Chapter 15-03-04 requires that the Board apply the prudent investor rule in investing the funds under its control. Application of the prudent investor rule dictates that investments of the Board should be made using the same judgment and care that an institutional investor of ordinary prudence, discretion, and intelligence exercises in the management of large investments entrusted to it.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of investments. The Board manages its interest rate risk by maintaining a diversified portfolio that contains a wide variety of maturity dates for the debt securities held. The Board has adopted an asset allocation schedule and approves the hiring of all managers within the various asset classes. The Board does not have a formal policy regarding the maturities of its investments.

The following table shows the investments by investment type, amount and maturity as of June 30, 2017. When callable, maturity is calculated with the first call date.

Investment Type	Maturity Amount	Weighted Average Maturity (Years)
Asset Backed Securities	\$ 14,799,636	9.74
Bank Deposits	940,537	
Commercial Mortgage-Backed	6,252,723	19.49
Commerical Paper	2,000,100	0.45
Corporate Bonds	410,818,605	6.67
TIPS Fund	79,556,299	8.49
Government Agencies	121,171,128	1.85
Brandywine Fund	95,423,365	12.03
Low Duration Fund	194,302	2.17
Fixed Income ETF	110	
Government Bonds	284,444,335	6.56
Government Mortgage Backed Securities	86,731,614	21.94
Gov't-issued Commerical Mortgage-Backed	12,930,721	5.52
Index Linked Government Bonds	1,267,630	
Municipal/Provincial Bonds	13,901,862	7.73
Non-Government Backed CMOs	16,829,078	19.46
Other ETF	18	
Other Fixed Income	120,202,243	5.40
Short Term Bills and Notes	106,505,215	0.35
Short Term Investment Funds	78,776,704	0.11
Sukuk	959,500	4.74
Total	<u>\$ 1,453,705,725</u>	
Weighted Average Maturity		<u>6.90</u>

The table above includes the fair value of inflation indexed bonds. The principal balances of these bonds are adjusted every six months based on the inflation index for the period.

Other investments included above, such as variable rate collateralized mortgage obligations (CMOs), have a high degree of sensitivity to interest rate changes. As of June 30, 2017, the Board held \$60,657,628 in variable rate CMOs.

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NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Board maintains a diversified portfolio of debt securities encompassing a wide range of credit ratings, including securities identified as U.S. Government in the tables below, which are U.S. Treasury and Agency debt securities that are either explicitly or implicitly guaranteed by the U.S. government and thus are considered to have no credit risk. Each fixed income securities manager is given a specific set of guidelines to invest within based on the mandate for which it was hired. The guidelines specify in which range of credit, and to what extent within the ranges, the manager may invest. The Board does not have a formal policy regarding credit risk. The following table presents the Board's ratings as of June 30, 2017.

	AAA	AA	A	BBB	BB	B	Not Rated	Government	Total
Asset Backed Securities	\$ 6,038,304	\$ 329,725	\$ -	\$ -	\$ -	\$ -	\$ 8,431,607	\$ -	\$ 14,799,636
Bank Deposits	-	-	-	-	-	-	940,537	-	940,537
Commercial Mortgage-Backed	-	-	-	-	-	-	6,252,723	-	6,252,723
Commercial Paper	-	-	-	-	-	-	2,000,100	-	2,000,100
Corporate Bonds	10,948,577	32,661,915	111,255,635	144,312,761	76,879,935	28,666,776	6,093,006	-	410,818,605
TIPS	-	-	-	-	-	-	-	79,556,299	79,556,299
Government Agencies	16,324,580	104,363,718	-	-	-	-	-	482,830	121,171,128
Brandywine Fund	-	-	-	-	-	-	-	95,423,365	95,423,365
Low Duration Fund	-	-	-	-	-	-	-	194,302	194,302
Fixed Income ETF	-	-	-	-	-	-	110	-	110
Government Bonds	9,280,879	7,106,468	18,053,763	17,454,702	3,638,948	-	38,473,308	190,436,267	284,444,335
Gov't Mortgage Backed Securities	-	4,715,483	-	-	-	-	317,435	81,698,696	86,731,614
Gov't-issued Commercial Mortgage-Backed	-	-	-	-	-	-	1,867,566	11,063,155	12,930,721
Index Linked Government Bond	-	-	-	-	-	-	-	1,267,630	1,267,630
Municipal/ Provincial Bonds	2,609,206	6,888,211	3,297,941	-	-	-	1,106,504	-	13,901,862
Non-Government Backed C.M.O.s	2,972,452	1,298,519	294,457	-	-	-	12,263,650	-	16,829,078
Other ETF	-	-	-	-	-	-	18	-	18
Other Fixed Income	-	-	-	-	-	-	120,202,243	-	120,202,243
Short Term Bills and Notes	-	-	-	-	-	-	-	106,505,215	106,505,215
Short Term Investment Funds	-	-	-	-	-	-	78,776,704	-	78,776,704
Sukuk	-	-	-	-	-	-	959,500	-	959,500
	<u>\$ 48,173,998</u>	<u>\$ 157,364,039</u>	<u>\$ 132,901,796</u>	<u>\$ 161,767,463</u>	<u>\$ 80,518,883</u>	<u>\$ 28,666,776</u>	<u>\$ 277,685,011</u>	<u>\$ 566,627,759</u>	<u>\$ 1,453,705,725</u>

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The Board treats currency exposure in two different ways, depending on the type of investment. For the Board's international equity portfolio, the currency exposure is not hedged as currency exposure is one of the items that add diversity to the overall portfolio. In the case of foreign bonds, the Board fully hedges the currency exposure as the purpose of this portfolio is to generate more consistent returns. The Board does not have a formal policy regarding foreign currency risk. The Board's exposure to foreign currency risk is presented in the following table:

Currency	Debt	Equity	Total
Australian Dollar	\$ 7,234,871	\$ 36,071,682	\$ 43,306,553
Brazilian Real	5,108,510	5,729,579	10,838,089
British Pound Sterling	20,034,586	98,792,733	118,827,319
Canadian Dollar	5,592,646	-	5,592,646
Chilean Peso	-	811,891	811,891
Chinese Renminbi	-	566,051	566,051
Columbian Peso	(187,280)	256,058	68,778
Czech Koruna	-	815,215	815,215
Danish Krone	(86,762)	9,724,965	9,638,203
Egyptian Pounds	-	43,717	43,717
Euro Members	841,494	147,246,403	148,087,897
Hong Kong Dollar	-	36,738,481	36,738,481
Hungarian Forint	35,276	1,182,839	1,218,115
Indian Rupee	4,446,729	12,280,295	16,727,024
Indonesian Rupiah	4,408,559	3,776,945	8,185,504
Israel Shekel	-	3,721,288	3,721,288
Japanese Yen	-	115,707,238	115,707,238
Kenyan Shilling	-	572,272	572,272
Malaysian Ringgit	5,123,615	2,098,426	7,222,041
Mexican Peso	13,651,513	3,567,726	17,219,239
New Romanian Leu	14,611	-	14,611
New Taiwan Dollar	-	16,411,625	16,411,625
New Zealand Dollar	(151,188)	843,492	692,304
Norwegian Krone	6,432,397	3,125,882	9,558,279
Peruvian Nuevo Sol	-	6,245	6,245
Philippines Peso	-	1,110,617	1,110,617
Polish Zloty	5,785,007	1,826,806	7,611,813
Russian Rubles	-	743,193	743,193
Singapore Dollar	44,379	6,648,701	6,693,080
South African Rand	4,589,083	7,469,252	12,058,335
South Korean Won	-	14,231,931	14,231,931
Swedish Krona	6,212,061	13,694,339	19,906,400
Swiss Franc	-	46,094,350	46,094,350
Thai Baht	81,866	2,869,149	2,951,015
Turkish Lira	276,728	1,969,649	2,246,377
	<u>\$ 89,488,701</u>	<u>\$ 596,749,035</u>	<u>\$ 686,237,736</u>

Derivative Securities

Derivatives are financial arrangements between two parties whose payments are based on, or "derived" from, the performance of some agreed upon benchmark. The investment policies of the Board allow the use of derivative securities to hedge or replicate underlying exposures but not for speculation. All derivatives are considered investment derivative instruments. The fair value of all

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NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

derivative securities is reported in the Statement of Net Position. At June 30, 2017, the Board had one type of derivative security: currency forwards.

Currency Forwards

Currency forwards represent forward exchange contracts that are obtained to manage the exposure to changes in currency exchange rates on the currency denominated portfolio holdings. A forward exchange contract is a commitment to purchase or sell a currency at a future date at a negotiated forward rate. The gain or loss arising from the difference between the original contracts and the closing of such contracts is included in the net change in fair value of investments in the Statement of Changes in Net Position with a loss of \$1,462,092 for fiscal year 2017. At June 30, 2017, the Board's investment portfolio included the currency forwards balances shown below.

<u>Currency</u>	<u>Cost</u>	<u>Purchases</u>	<u>Sales</u>	<u>Fair Value June 30, 2017</u>
Australian Dollar	\$(20,891,475)	\$ -	\$ (21,092,407)	\$ (21,092,407)
Brazilian Real	(3,575,153)	-	(3,578,334)	(3,578,334)
Canadian Dollar	(6,072,073)	-	(6,320,557)	(6,320,557)
Columbian Peso	(4,099,083)	-	(3,928,813)	(3,928,813)
Danish Krone	(9,298,348)	3,572,919	(13,013,434)	(9,440,515)
Euro Members	(11,611,715)	-	(11,800,055)	(11,800,055)
Hungary Forint	(3,465,654)	-	(3,549,441)	(3,549,441)
Malaysian Ringgit	(6,694,282)	-	(6,679,285)	(6,679,285)
Mexico Peso	(6,699,419)	-	(7,078,983)	(7,078,983)
New Romanian Leu	(1,364,583)	-	(1,428,218)	(1,428,218)
New Zealand Dollar	(7,219,177)	-	(7,257,656)	(7,257,656)
Norwegian Krone	(6,816,641)	-	(6,887,842)	(6,887,842)
Polish Zloty	(6,456,543)	-	(6,901,714)	(6,901,714)
Singapore Dollar	(6,641,671)	-	(6,755,989)	(6,755,989)
South Africa Rand	(4,251,157)	-	(4,269,344)	(4,269,344)
Thai Baht	(3,852,235)	-	(3,944,678)	(3,944,678)
United Kingdom Pound	(2,531,235)	3,775,138	(6,248,504)	(2,473,366)
United States Dollar	111,750,443	118,982,152	(7,231,709)	<u>111,750,443</u>
Total forwards subject to currency risk				<u>\$ (1,636,754)</u>

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NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

NOTE 6 – SECURITIES LENDING

GASB Statement No. 28, *Accounting and Financial Reporting for Securities Lending Transactions* establishes accounting and financial reporting standards for securities lending transactions. The standard requires governmental entities to report securities lent as assets in their balance sheets. Cash received as collateral and investments made with that cash must also be reported as both an asset and a liability. The statement also requires the costs of the securities lending transactions to be reported as expenses separately from income received. In addition, the statement requires disclosures about the transactions and collateral related to them.

Securities are loaned versus collateral that may include cash, U.S. government securities and irrevocable letters of credit. U.S. securities are loaned versus collateral valued at 102% of the fair value of the securities plus any accrued interest. In all cases the borrower provides more collateral than the value of securities lent. Therefore, there is no credit risk related to security lending transactions. Non-U.S. securities are loaned versus collateral valued at 105% of the market value of the securities plus any accrued interest.

Non-cash collateral cannot be pledged or sold unless the borrower defaults.

All securities loans can be terminated on demand by either the lender or the borrower, although the average term of North Dakota Board of University & School Lands loans was approximately 79 days as of June 30, 2017.

Cash open collateral is invested in a short-term investment pool, the NDLAN Custom fund, which had an interest sensitivity of 29 days as of this statement date.

There were no violations of legal or contractual provisions, no borrower or lending agent default losses known to the securities lending agent.

There are no dividends or coupon payments owing on the securities lent. Securities lending earnings are credited to participating clients on approximately the fifteenth day of the following month.

Indemnification deals with the situation in which a client's securities are not returned due to the insolvency of a borrower and Northern Trust has failed to live up to its contractual responsibilities relating to the lending of those securities. Northern Trust's responsibilities include performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable Department of Labor and Federal Financial Institutions Examination Council regulations concerning securities lending.

Securities lending collateral is invested in investment pools and is not exposed to custodial credit risk.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

The following represents the Board's balances related to securities lending transactions at June 30, 2017.

	Underlying Securities on Loan for Cash	Cash Collateral	Underlying Securities on Loan for Non- Cash Collateral	Non-Cash Collateral
GLOBAL Agencies	\$ 4,483,718	\$ 4,715,750	\$	\$
GLOBAL Equities			907,561	954,525
US Agencies	21,613,008	22,113,048		
US Corporate Fixed	52,379,482	53,666,829		
US Equities	48,650,990	49,804,419	4,836,244	4,936,497
US Government Fixed	75,540,700	77,247,518	23,973,843	24,516,369
	\$ 202,667,898	\$ 207,547,564	\$ 29,717,648	\$ 30,407,391
Market Value of Securities on Loan against Cash Collateral				\$ 202,667,898
Market Value of Securities on Loan against Non Cash Collateral				29,717,648
Total Market Value of Securities on Loan				\$ 232,385,546

NOTE 7 - FAIR VALUE OF FINANCIAL INSTRUMENTS

The following investments are reported at fair value, which represents stated market prices. Actual gains and losses realized by the Department will be determined at the time of the sale and will be based on market conditions on that date.

Fair Value Hierarchy

In accordance with GASB Statement No. 72, assets and liabilities are grouped at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

- Level 1 – Valuation is based upon quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- Level 2 – Valuation is based upon quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

Determination of Fair Value

In accordance with GASB Statement No. 72, fair values are based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It is the Department's policy to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements, in accordance with the fair value hierarchy.

The equity, fixed income and other investment assets classified as Level 1 of the fair value hierarchy are either individual securities, mutual funds or ETFs that are valued using prices quoted in active markets for those securities or funds. The short-term bills and notes, equity, fixed income and other investment assets classified as Level 2 of the fair value hierarchy are primarily debt instruments and funds whose pricing is determined by pricing vendors using quoted prices for similar assets in active markets. Level two assets also include some low traded equities in the unclaimed property account, as well as currencies and forward foreign currency exchange contracts held in the portfolio that are used to hedge certain portions of the fixed income portfolio.

Assets classified as being measured by NAV include certain investments in six different equity common trust funds that have either daily or monthly liquidity, investments in two different bond funds, both of which have daily liquidity, and investments in five different open ended real estate funds/partnerships that are priced quarterly by the general partner and which have redemption notice requirements of 90 days. Items classified as being valued at other than FV include cash held in money markets accounts at Northern Trust as well as adjustments to cash for pending sales and purchases.

The table below presents the balances of assets and liabilities measured at fair value on a recurring basis at June 30, 2017.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

	Fair Value at 6/30/17	Fair Value Measures Using		
		Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Investments, at fair value				
Short Term Securities				
Short Term Bills and Notes	\$ 106,505,215		\$ 106,505,215	
Total Short Term Securities	<u>106,505,215</u>		<u>106,505,215</u>	
Equity Investments				
Common Stock	258,629,803	\$ 258,629,447	52	\$ 304
Equity Funds/EFTs	124,658,270	124,658,270	-	-
Convertible Equity	2,380,490	2,380,490	-	-
Preferred Stock	32,335,274	32,335,274	-	-
Total Equity Investments	<u>418,003,837</u>	<u>418,003,481</u>	<u>52</u>	<u>304</u>
Fixed Income Investments				
Asset Backed Securities	14,799,636	-	14,799,636	-
Bond Funds/EFTs	120,381,959	120,381,959	-	-
Collateralized Mortgage	21,861,996	-	21,861,996	-
Commercial Mortgage Backed	19,183,443	-	19,183,443	-
Commercial Paper	2,000,100	-	2,000,100	-
Corporate Bonds	411,792,801	-	411,792,801	-
Government Agencies	34,035,598	-	34,035,598	-
Government Bonds	298,346,196	-	298,346,196	-
Government Mortgage Backed	168,834,226	-	168,834,226	-
Index Linked Government Bonds	1,267,630	-	1,267,630	-
Total Fixed Income Investments	<u>1,092,503,585</u>	<u>120,381,959</u>	<u>972,121,626</u>	<u>-</u>
Other Investment Assets				
Currency	24,959,979	-	24,959,979	-
Currency ETF	18	18	-	-
FX Contracts	(1,638,066)	-	(1,638,066)	-
Global Tactical Asset Allocation MF	550,238,037	550,238,037	-	-
Master Limited Partnership	132,640,890	132,640,890	-	-
REITs	17,543,479	17,543,479	-	-
Rights/Warrants	314	316	-	-
Total Other Investment Assets	<u>723,744,651</u>	<u>700,422,740</u>	<u>23,321,913</u>	<u>-</u>
Total Investments at Fair Value	<u>\$ 2,340,757,288</u>	<u>\$ 1,238,808,180</u>	<u>\$ 1,101,948,806</u>	<u>\$ 304</u>
		Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Investments measured at NAV:				
Commingled Funds - Equities	\$ 1,129,147,675		Daily, Monthly	< 5 days
Commingled Funds - Fixed Income	174,979,664		Daily	< 5 days
Real Estate Funds	632,915,027		Quarterly	90 days
Total Investments measured at NAV	<u>\$ 1,937,042,366</u>			
Investments at other than fair value				
Cash and adjustments to cash	\$ 47,096,023			
Total Investments at other than fair value	<u>\$ 47,096,023</u>			
Total Investments	<u>\$ 4,324,895,677</u>			

In addition, the Department holds unclaimed mutual funds and other securities for owners. Actual gains and losses realized will be determined at the time of the sale and will be based on market conditions at that date. As of June 30, 2017, the Board held \$504,429 in unclaimed mutual funds.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

The Common Schools Trust Fund owns the building occupied by the Department. For the period ending June 30, 2017, the book value of the building was \$544,597. The book value of the building is included in the investments line of the balance sheet

NOTE 8 – INVESTMENT EXPENSES

The following is a summary of investment expenses as of June 30, 2017.

Investment managers' fees:	
Large cap equity	\$ 63,673
Mid cap equity	1,784
Small cap equity	886,536
International equity	121,178
Emerging markets equity	1,016,120
US investment grade fixed income	1,327,941
High yield fixed income	345,650
International fixed income	669,431
Core real estate	3,438,246
Non-core real estate	4,783,604
Inflation protected	2,141,332
Global tactical	<u>6,055,217</u>
Total investment managers' fees	<u>20,850,712</u>
Custody fees	169,356
Investment consultant fees	145,000
Miscellaneous expenses	<u>332,618</u>
Total investment expenses	<u><u>\$21,497,686</u></u>

The following is a reconciliation of investment expense to the financial statements.

Investments expenses as reflected in the financial statements	\$ 10,797,209
Plus investment management fees included in investment income	
Large cap equity	6,479
International equity	6,848
Emerging markets equity	1,016,120
US investment grade fixed income	296,064
Core real estate	(58,678)
Non-core real estate	4,783,604
Global tactical	<u>4,650,040</u>
Investment expenses per schedule	<u><u>\$21,497,686</u></u>
 BND loan pool management expenses	
Expenses as reflected in the financial statements	\$ 40,356
Plus expenses as reflected in interest income	3,106
Total loan pool expenses	<u><u>\$ 43,462</u></u>

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

NOTE 9 – FARM LOAN POOL AND FARM REAL ESTATE

N.D.C.C. Chapter 15-03 authorizes the Board to invest in first mortgage farm loans. All purchased loans are credited to the pool and the investments, repayments, interest and income are credited to the various trusts in proportion to their participation. The pool is administered by the BND in accordance with standard banking practices, including executing all instruments on behalf of the Board and handling foreclosures.

As of June 30, 2017, the non-current and current portions of the loans were \$6,867,242 and \$759,457, respectively.

As of June 30, 2017, the pool had a net position of \$8,140,363. For the same period, the pool earned net income of \$538,520.

NOTE 10 – ENERGY CONSTRUCTION LOAN PROGRAM

The Board approved participation in an energy construction loan program with the BND for the purpose of new construction loans in areas of North Dakota impacted by oil development. The primary focus of the loan program is for multi-family housing and commercial loans. The Board will participate in up to 50% of a first mortgage at market rates; loans must be amortized over 20 years or less. The Board authorized the Commissioner to allocate up to \$20,000,000 to this program. The Common School Trust fund is the only trust participating in this program.

The loan program meets the “exclusive benefit” rule, whereby any investment decision made must be for the sole benefit of the Common School Trust fund. The loan program is administered by the BND who charges an annual fee of one-quarter percent on all outstanding loans.

As of June 30, 2017, the non-current and current portions of the loans were \$1,183,704 and \$32,464, respectively.

As of June 30, 2017, the program had a net position of \$1,248,356. For the same period, the program earned net income of \$54,930.

NOTE 11 - COAL WARRANTS

The Board is authorized to make loans to coal development impacted counties, cities and school districts from the Coal Development Trust fund. A warrant is executed by the governing body as evidence of the loan. The loans bear interest at 3, 3.2 or 3.75 percent annually, depending on the loan date. The coal warrants are payable only from the borrowing entities share of coal severance tax payments and do not constitute a general obligation of the entity. No losses are anticipated on the warrants and an allowance has not been provided.

As of June 30, 2017, the non-current and current portions of the loans were \$11,977,360 and \$682,155, respectively.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

NOTE 12 - SCHOOL CONSTRUCTION LOAN PROGRAM

The school construction loan program, fund by the Coal Development Trust Fund, is governed by N.D.C.C. Chapter 15.1-36-02, authorizing the Board to fund low-interest school construction loans; of which the outstanding principal balance of loans made from this fund may not exceed fifty million dollars.

A proposed construction project must be submitted and approved by the superintendent of public instruction. The application may be submitted before or after authorization of a bond issue in accordance with N.D.C.C. Chapter 21-03. The superintendent determines the loan amount, the term of the loan, and the interest rate to be paid. To be eligible for a loan, the school district must have an existing indebtedness equal to at least fifteen percent of the school district's taxable valuation. The interest rate discount on a loan must be at least one percent, but cannot exceed four percent of the interest rate charged on comparable tax-exempt bond rates.

For all regular school construction loans the BND processes and services all loans. BND receives payments of principal and interest from the school districts and remits these payments to the Department for deposit in the Coal Development Trust fund.

In 2013, the legislature changed the program to allow certain school districts in oil producing areas to use a portion of the gross production tax due to the district under N.D.C.C. Chapter 57-51 to repay school loans. For gross production tax backed school loans, the amount of the loan does not count as debt for the borrowing entity and repayment of the loan will be accomplished by the State Treasurer capturing a school district's gross production tax payments each month and remitting those funds to appropriate trust fund until such time that year's scheduled loan payment has been captured. As of June 30, 2017, there was one gross production tax backed school construction loan processed with Coal Development Trust funding.

As of June 30, 2017, the non-current and current portions of loans from the Coal Development Trust Fund were \$45,035,465 and \$3,212,394, respectively.

NOTE 13 - SCHOOL CONSTRUCTION ASSISTANCE LOAN FUND

In 2015, the legislature amended N.D.C.C. Chapter 15.1-36 to end the loan making authority from SIIF and created the School Construction Assistance revolving loan fund (SCALF) in the State Treasury. The legislative assembly provided for the transfer of one hundred and fifty million dollars of loans from the SIIF for school construction loans. All interest or other earnings of the fund, and all repayments of loans collected by the fund will remain in the fund. The money in this fund is appropriated on a continuing basis for the purpose of providing low-interest school construction loans.

With passage of Senate Concurrent Resolution No. 4003 by the Sixty-Fourth Legislative Assembly and approval of the State voters on November 2, 2016, the Department transferred the administration of the SCALF to the BND on January 17, 2017.

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NOTE 14 – FUEL PRODUCTION FACILITIES LOAN GUARANTEE PROGRAM

The Fuel Production Facility Loan Guarantee Program is governed under N.D.C.C. Chapter 6-09.7. Under this program, the BND may use up to \$25 million of the SIIF to guarantee loans to facilities that use biomass for agriculturally derived fuel production. The guarantee is limited to 30% of the debt needed to build the project.

On March 6, 2014, \$18,000,000 was transferred from SIIF to the BND to guarantee \$60 million of loans to Dakota Spirit AgEnergy. The loan guarantee closed on May 12, 2014. The guaranteed funds will be held at BND, on behalf of the SIIF, in an income earning account. Any net income earned and fees collected under the guarantee program will be transferred back into the SIIF periodically.

As of June 30, 2017, restricted investments held by the BND for the Fuel Production Facility Loan Guarantee Program totaled \$5,893,788. These investments are recorded as restricted on the SIIF's financial statements.

NOTE 15 - OFFICE LEASE COMMITMENT

The Board's administrative agent, the Department rents office space owned by the Common Schools Trust Fund. The Department's commitment to rent its office space from the Common Schools Trust is continuous, with periodic adjustments made in accordance with acceptable accounting practices and market conditions.

For the period ending June 30, 2017, rent of \$52,735, was paid by the non-Common Schools Trusts funds.

NOTE 16 - CAPITAL ASSETS

Governmental Activities:	7/1/2016	Additions	Retirements	Balance 6/30/17
Land	\$ 7,739,757	\$ 306	\$ -	\$ 7,740,063
Equipment	43,132			43,132
Less accumulated depreciation:				
Equipment	(20,797)	(6,541)		(27,338)
Net capital assets	\$ 7,762,092	\$ (6,235)	\$ -	\$ 7,755,857

Under the provisions of the Enabling Act, land was granted to the State for the support of the common schools and other institutions. Under Constitutional authority, no grant land may be sold for less than ten dollars an acre which is the value per acre used for balance sheet purposes. In fiscal year 2017, 30.60 acres were acquired and no acres were sold.

All lands held by the Department are considered capital assets, except lands acquired through foreclosure that the Board intends to sell. Land is not depreciable according to GASB 34.

A total of \$6,541 in equipment depreciation for fiscal years ending June 30, 2017 was charged to education expenses.

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NOTE 17 - DUE FROM (TO) OTHERS

The following detail shows amounts that are due from and to other trust funds managed by the Department at June 30, 2017:

Fund	Due from other funds	Due to other funds
General fund		\$ 3,186,000
Strategic Investment and Improvements fund	\$ 1,302,434	
Non-major perpetual funds	82,685	
Common Schools Trust fund	1,800,881	
	<u>\$ 3,186,000</u>	<u>\$ 3,186,000</u>

As stated in Note 1 of these financial statements, the Department is a state agency of North Dakota, as such, the other state agencies of the State and political subdivision are related parties. The following is detail of amounts due from and to other state agencies as of June 30, 2017.

Fund	Due from other state agencies	Due to other state agencies
Coal Development Trust fund:		
State Treasurer	\$ 509,727	\$ 356,809
	<u>509,727</u>	<u>356,809</u>
General fund		
Attorney General		10,114
Dept. of Transportation		6,009
Information Technology Department		11,796
Central Services		653
		<u>28,572</u>
Common School Trust Fund:		
State Treasurer	9,519,872	
Bank of North Dakota		17,365
	<u>9,519,872</u>	<u>17,365</u>
Perpetual funds:		
Bank of North Dakota		1,486
		<u>1,486</u>
Strategic Investment & Improvements fund:		
State Treasurer	24,575,948	
	<u>24,575,948</u>	
Oil and Gas Impact fund:		
Information Technology Department		650
Attorney General		50
Dept. of Transportation		510
		<u>1,210</u>
Total Due From/Due To	<u>\$ 34,605,547</u>	<u>\$ 405,442</u>

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NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
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NOTE 18 – PERPETUAL FUND DISTRIBUTION POLICY

According to Section 2 of Article IX of the North Dakota State Constitution, biennial distributions from the perpetual trust funds must be ten percent of the five-year average value of trust assets, excluding the value of lands and minerals. The average value of trust assets is determined by using the ending net value of each trusts' financial assets for the fiscal year that ends one year before the beginning of the biennium and the assets' ending value for the four preceding fiscal years. Equal amounts must be distributed during each year of the biennium.

NOTE 19 – TRANSFERS FROM (TO) OTHER AGENCIES

The following detail represents amounts transferred to beneficiaries and other state agencies as of June 30, 2017.

Fund	Transfers from other agencies	Transfers to other agencies
Perpetual Funds:		
Department of Public Instruction		\$ 103,067,000
Ellendale		273,000
Industrial School		686,000
Mayville State University		191,000
ND State University		1,684,000
School of Mines		567,000
School of Science		494,000
School of the Blind		228,000
School of the Deaf		590,000
State Hospital		500,000
University of ND		804,000
Valley City State University		285,000
Veterans Home		178,000
		<u>109,547,000</u>
Coal Development Trust:		
Lignite Research Fund		2,199,587
General Fund of ND		882,064
		<u>3,081,651</u>
Strategic Investment and Improvements:		
Adjutant General		79,500
General Fund of North Dakota		155,000,000
Legal Counsel of Indigents		389,000
ND Department of Health		250,000
ND Department of Human Services		9,000,000
ND Department of Transportation		3,500,000
ND Oil and Gas Division		800,000
ND State Historical Society		50,000
ND State University		16,634,854
Office of ND State Treasurer		8,100,000
		<u>193,803,354</u>
School Construction Assistance Loan Fund:		
Bank of North Dakota		153,220,175
		<u>153,220,175</u>
Capitol Building Trust:		
Facilities Management		2,735,000
		<u>2,735,000</u>
Total Transfers	\$ -	<u>\$ 462,387,180</u>

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NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
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NOTE 20 – ASSIGNED FUND BALANCE

On August 21, 2017 the Board of University and School Lands classified \$229,325,049 of the Strategic Investment and Improvements fund as an assigned fund balance for fiscal year 2017 financial statement purposes. This commitment was made by the Board to indicate that these funds should not be transferred out of this fund until potential title disputes related to certain riverbed leases have been resolved.

NOTE 21 – LITIGATION

The Board of University and School Lands (Board) is currently involved in litigation relating to mineral title ownership along the Missouri River. Riparian owners are challenging the State's determination of the ordinary high watermark. The Board has set aside funds to cover the potential title disputes related to certain riverbed leases until they are resolved.

The Board is also involved in litigation relating to ownership of minerals under the railroad rights-of-way in a section of land in Mountrail County. At issue are rights-of-way that the railroad acquired through rights-of-way deeds.

The Board is also party to a lawsuit before the United States Supreme Court to determine where proceeds of certain unclaimed property must be paid.

Wilkinson Family v. State of North Dakota

On January 10, 2012, the Wilkinson family filed a suit in state court asserting that they own shore zone minerals in about 200 acres west of Williston. In July 2014, the plaintiffs filed an amended complaint and added claims of unconstitutional takings, conversion, constructive trust and unjust enrichment, civil conspiracy and deprivation of rights under 42 U.S.C. § 1983. The plaintiffs allege that the Board should be issuing leases on the west side of the Highway 85 Bridge pursuant to the Phase II delineation study which determined the location of the historic Missouri River channel, prior to the Garrison Dam project. The district court granted a summary judgment motion brought by the State and found in the State's favor determining that the minerals under the property in question are owned by the State of North Dakota and dismissing the remaining counts in the complaint. The plaintiffs and two of the defendants appealed to the North Dakota Supreme Court. During the 2017 Legislative Assembly and following the district court's decision, the North Dakota Legislature passed S. B. 2134 which attempts to define the historic ordinary high watermark for certain areas of the Missouri River which are inundated by Lake Sakakawea. On September 28, 2017, the North Dakota Supreme Court reversed and remanded the case back to the district court for further proceedings and consideration of S.B. 2134.

Whitetail Wave LLC v. XTO Energy, Inc., Board of University and School Lands, and the State of North Dakota

This case is also challenging the State's determination of the ordinary high watermark but the tract is located on the east side of the Highway 85 Bridge where the Department has currently leased only the historic channel of the Missouri River. The Plaintiffs are requesting that title to the minerals be quieted and have alleged claims of unconstitutional takings, trespass, slander of title and constructive trust/unjust enrichment against the State. The complaint also makes a number of claims against XTO individually. The district court issued an order dated August 21, 2017 staying these proceedings until such time as final review findings under N.D.C.C. § 61-33.1-03 are adopted by the North Dakota Industrial Commission.

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Mary K. Starin, as Personal Representative of the Estate of Bruno Herman Weyrauch v. Kelly Schmidt, State Treasurer, et. al.

This is a quiet title action. A deed previously issued by the Department of Trust Lands was lost without being recorded, the plaintiff is seeking a judgment to cure the defect in the chain of title. The tract, however, is located under Lake Sakakawea. The Board has filed an answer claiming any interest in any minerals located below the ordinary high watermark. The district court issued an order dated July 10, 2017 staying these proceedings until such time as final review findings under N.D.C.C. § 61-33.1-03 are adopted by the North Dakota Industrial Commission with the exception that the plaintiff may submit a motion for summary judgment on issues other than the location of the ordinary high watermark.

Whiting Oil and Gas Corporation v. Arlen A. Dean, et. al.

Whiting filed an interpleader for the lands underlying a spacing unit located near the Montana border for which the Yellowstone River runs through. Whiting is requesting the Court determine the property interests for the spacing unit so that Whiting can correctly distribute the proceeds from the well located in the unit. A scheduling order was issued on September 8, 2017 setting the matter for a five day court trial beginning on August 6, 2018.

Continental Resources, Inc. v. North Dakota Board of University and School Lands, United States

This is an interpleader action filed by Continental Resources, Inc. for certain lands underlying Continental operated wells located in McKenzie, Mountrail, and Williams Counties which are being claimed by both the state of North Dakota and the United States. Continental is requesting the Court determine the property interests for the lands so that Continental can correctly distribute the proceeds from the wells. Continental Resources filed an amended complaint on September 14, 2017. The Board filed an answer to the amended complaint on October 18, 2017. The United States filed a motion to dismiss on October 18, 2017.

North Dakota Office of the State Engineer and North Dakota Board of University & School Lands v. Bureau of Land Management (Office of Hearings and Appeals, Board of Land Appeals)

In 2014, the Bureau of Land Management (BLM) resurveyed land along the Missouri River to locate the boundary between public domain land owned by the United States and the riverbed owned by the State of North Dakota. In identifying the boundary, the BLM applied federal law rather than state law. The BLM uses these surveys as the basis for leasing minerals. In certain areas, the new surveys overlap with minerals currently leased by the Board. The Board of University and School Lands and State Engineer challenged the BLM's resurvey but the BLM's Montana Office rejected the challenge. The Board and State Engineer then appealed that decision to the Office of Hearings and Appeals.

Engineer challenged the BLM's resurvey but the BLM's Montana Office rejected the challenge. The Board and State Engineer then appealed that decision to the Office of Hearings and Appeals, Board of Land Appeals (IBLA). The Board and State Engineer and BLM have both filed briefs with the IBLA regarding their respective positions and are awaiting a decision from the IBLA.

State of Arkansas, et al. v. State of Delaware (United States Supreme Court)

This case is an attempt to have the United States Supreme Court assume jurisdiction over a lawsuit involving unclaimed property brought by 30 states, including the state of North Dakota, against the state of Delaware. The substantive issue involved is whether sums payable on unclaimed and abandoned checks sold by Moneygram Payments Systems, Inc. should be

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remitted to the Plaintiff States, as the states of purchase, or to Defendant Delaware, as Moneygram's state of incorporation. The Special Master has accepted the Case Management Order agreed to by the parties.

EOG Resources, Inc. v. Soo Line Railroad Co., et. al.

This case concerns ownership of the minerals underlying the railroad rights-of-way in a section of land in Mountrail County. The railroad acquired an interest in a strip of land through the property in question through a "Right of Way Deed." At issue is whether the deed granted an easement or fee title to the strip of land. The North Dakota Supreme Court heard this case in November of 2014 and found that the deed in question is ambiguous and remanded the case to the district court for further proceedings. The parties are currently attempting to negotiate a settlement agreement.

The State's estimated loss contingency on the above litigation cases cannot be made at this time.

NOTE 22 – CONTINUING APPROPRIATIONS

The following information discloses the Department's continuing appropriation authority.

NDCC 15-03-16 Investments. To pay costs related to investments controlled by the Board, including investment management fees, trustee fees, consulting fees, custodial fees, and the cost of capitalized building repairs and renovations.

NDCC 15-04-23 County Services. This statute requires the Board to pay a fee to counties in which the state retains original grant lands for roads and bridges.

NDCC 15-04-24 Grant Land. To pay expenses for trust lands controlled by the Board, including appraisal fees, survey costs, surface lease refunds, weed and insect control costs, clean-up costs, capital improvement rent credits, and expenses necessary to manage, preserve, and enhance the value of the trust asset.

NDCC 15-05-19 Mineral Leases. To pay expenses for minerals controlled by the Board, including appraisal fees, consulting fees, refunds, and expenses necessary to manage, preserve, and enhance the value of the trust asset.

NDCC 15-06-22 Grant Land. This statute allows the Board to pay expenses relating to the sale of original grant land including appraisal fees.

NDCC 15-07-22 Non-Grant Land. To pay expenses for trust lands controlled by the Board, including appraisal fees, survey costs, clean-up or demolition costs, weed and insect control costs, rural fire district reimbursements for fire protection, and expenses necessary to manage, preserve, and enhance the value of the trust asset.

NDCC 15-08-04 Land Surveys. To pay all expenses to ascertain the true boundaries of any tract of land, or to describe or dispose of the same in suitable and convenient lots.

NDCC 15-68-06 Indian Cultural Education Trust. To pay expenses for lands donated under this chapter including survey costs, surface lease refunds, weed and insect control, cleanup costs, capital improvement rent credits, in lieu of tax payments, or expenses necessary to manage,

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preserve, and enhance the value of the trust asset. NDCC 57-02.3-07 In Lieu Property Taxes. This statute requires the Board to pay counties in which State property is located in lieu of property taxes.

NDCC 47-30.1-23 Uniform Unclaimed Property Act. To pay all expense deductions under this section.

NOTE 23 – LONG TERM LIABILITIES

Compensated Absences Payable

The Department employees can earn annual leave at a varying rate based on years of service. The amount of annual leave earned ranges from one to two days per month, and accrued annual leave cannot exceed 30 days as of April 30th of each year. The Department employees earn sick leave at the rate of one working day per month of employment without limitation on the amount that can be accumulated. At 10 years of continuous service, the State is liable for 10 percent of the employee’s accumulated unused sick leave.

	<u>Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Amounts</u> <u>Due Within</u> <u>One Year</u>	<u>Amounts</u> <u>Due</u> <u>Thereafter</u>	<u>Balance</u> <u>6/30/2017</u>
Governmental Activities-	7/1/2016					
Other long-term liabilities:						
Compensated absences	\$218,741	\$142,490	\$140,983	\$11,763	\$208,484	\$220,247

NOTE 24 – PENSION PLAN

North Dakota Public Employees Retirement System (Main System)

The following brief description of NDPERS is provided for general information purposes only. Participants should refer to N.D.C.C. Chapter 54-52 for more complete information.

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.

Pension Benefits

Benefits are set by statute. NDPERS has no provisions 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

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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.

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 for disabled is set by the NDPERS in the North Dakota Administrative Code.

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.

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

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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

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

At June 30, 2017, the Department reported a liability of \$1,889,364 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2016, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Department's proportion of the net pension liability was based on the Department'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, the Department's proportion was 0.193861 percent which was an increase of 0.018062 from its proportion measured as of June 30, 2015.

For the year ended June 30, 2017, the Department recognized pension expense of \$270,709. At June 30, 2017, the Department reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
	<u> </u>	<u> </u>
Differences between expected and actual experience	\$ 28,382	\$ (17,494)
Changes in actuarial assumptions	174,175	(93,864)
Difference between projected and actual investment earnings	263,594	-
Changes in proportion and differences between employer contributions and proportionate share of contributions	98,164	(1,046)
Contributions paid to PERS subsequent to the measurement date	145,736	-
Total	<u>\$ 710,051</u>	<u>\$ (112,404)</u>

The \$145,736 reported as deferred outflows of resources related to pensions resulting from Department contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2018.

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

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Year ended June 30:	Pension Expense Amount
2018	\$ 83,880
2019	83,880
2020	141,383
2021	97,812
2022	44,956

Actuarial assumptions. The total pension liability in the July 1, 2016 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%

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Discount rate. The discount rate used to measure the total pension liability was 8 percent as of June 30, 2016. 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, Actuarial Valuation Report. 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. 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.

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 in Discount Rate (7%)	Discount Rate (8%)	1% Increase in Discount Rate (9%)
Employer's proportionate share of the net pension liability:	<u>\$ 2,680,027</u>	<u>\$ 1,889,364</u>	<u>\$ 1,223,190</u>

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 25 – POSTRETIREMENT BENEFITS

Former employees receiving retirement benefits under the Retirement Plan of the Department are eligible to participate in the Retiree Health Benefits Fund, a cost-sharing multiple-employer plan, administered by the Public Employees Retirement Board. The retired employee is provided a credit toward their monthly health insurance premium under the state health plan based upon their years of credited service. In accordance with N.D.C.C 54-52.1-03.2, the Department reimburses the Retiree Health Benefits Fund monthly for credit received by members of the retirement plan.

The benefits, fully paid by the Department, are equal to \$5.00 for each of the employee's or deceased employee's years of credited service, not to exceed the premium in effect for selected coverage. For this pay-as-you-go plan, total Department expenditures for the period ending June 30, 2017 was \$23,334.

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NOTE 26 – RISK MANAGEMENT

The Department is exposed to various risks of loss related to torts, theft, damage, destruction of assets, errors and omissions, injuries to employees, and natural disasters. The Department participates in the following funds or pools:

The Risk Management Fund (RMF) was created in 1995 and is an internal service fund to provide a self-insurance vehicle for the liability exposure of state agencies resulting from the elimination of the state's sovereign immunity. The RMF manages the tort liability of the state, its agencies' employees, and the University System. All state agencies participate in the RMF and their fund contribution was 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 Department pays an annual premium to the Fire and Tornado Fund (FTF) to cover property damage to personal property. Replacement cost coverage is provided by estimating replacement cost in consultation with the FTF. The FTF is reinsured by a third party insurance carrier for losses in excess of one million dollars per occurrence during a twelve month period.

The State Bonding Fund currently provides the Department with blanket fidelity bond coverage in the amount of \$3,000,000 for its employees. The State Bonding Fund does not currently charge any premium for this coverage.

North Dakota Workforce Safety and Insurance is an enterprise fund of the State of North Dakota; it 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 year and settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

NOTE 27 – CHANGE IN FINANCIAL PRESENTATION

The Department restated one of its special revenue funds, Indian Cultural Education, to a fiduciary fund to be consistent with how the State of North Dakota reports the fund. Consequently, an adjustment was made to reduce the beginning net position on the Combining Statement of Revenues, Expenditures, and Changes in Fund Balances and Statement of Activities by \$1,140,105 to remove the Indian Cultural Education fund from these statements so these balances can be reported as a fiduciary fund in the current year.

NOTE 28 – ISSUED BUT NON-EFFECTIVE PRONOUNCEMENTS

GASB Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions, is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement is effective for fiscal years beginning after June 15, 2017. Earlier application is encouraged.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, provides recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. This Statement requires that a government that receives resources pursuant to an irrevocable split-interest agreement recognize assets, liabilities, and deferred inflows of resources at the inception of the agreement. Furthermore, this Statement requires that a government recognize assets representing its beneficial interests in irrevocable split-interest agreements that are administered by a third party, if the government controls the present service capacity of the beneficial interests. This Statement requires that a government recognize revenue when the resources become applicable to the reporting period. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2016, and should be applied retroactively. Earlier application is encouraged.

GASB Statement No. 82, *Pension Issues – an amendment of GASB Statements No. 67 and No. 73*, provides further guidance regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. This Statement amends GASB Statements No. 67 and No. 68 to require the presentation of covered payroll to be defined as the payroll on which contributions to a pension plan are based, rather than the payroll of employees that are provided with pensions through the pension plan. The requirements of this Statement are effective for reporting periods beginning after June 15, 2016, except for the requirements of this Statement for the selection of assumptions in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. Earlier application is encouraged.

GASB Statement No. 83, *Certain Asset Retirement Obligations*, addresses accounting and financial reporting for certain asset retirement obligations (AROs). This Statement establishes criteria for determining the timing and pattern of recognition of a liability and corresponding deferred outflow of resources for AROs. It also establishes disclosure of information about the nature of a government's AROs, the methods and assumptions used for the estimates of the liabilities, and the estimated remaining useful life of the associated tangible capital assets. The requirements of this Statement are effective for reporting periods beginning after June 15, 2018. Earlier application is encouraged.

GASB Statement No. 84, *Fiduciary Activities*, provides guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018. Earlier application is encouraged.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2017

GASB Statement No. 85, *Omnibus 2017*, addresses practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). The requirements of this Statement are effective for reporting periods beginning after June 15, 2017. Earlier application is encouraged.

GASB Statement No. 86, *Certain Debt Extinguishment Issues*, provides guidance for derecognizing debt that is defeased in substance, regardless of how cash and other monetary assets placed in an irrevocable trust for the purpose of extinguishing that debt were acquired. This Statement requires that any remaining prepaid insurance related to the extinguished debt be included in the net carrying amount of that debt for the purpose of calculating the difference between the reacquisition price and the net carrying amount of the debt. In addition, this Statement will enhance the decision-usefulness of information in notes to financial statements regarding debt that has been defeased in substance. This Statement is effective for reporting periods beginning after June 15, 2017. Earlier application is encouraged.

GASB Statement No. 87, *Leases*, establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. This Statement requires recognition of certain lease assets and liabilities for leases that were previously classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. This Statement is effective for reporting periods beginning after December 15, 2019. Earlier application is encouraged.

Management has not yet determined the effect these Statements will have on the Agency's financial statements.

NOTE 29 – SUBSEQUENT EVENTS

No significant events occurred subsequent to Department's year end. Subsequent events have been evaluated through October 23, 2017, which is the date these financial statements were available to be issued

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
COMBINING BALANCE SHEET
NON-MAJOR GOVERNMENTAL FUNDS
JUNE 30, 2017

Assets:	Special Revenue Funds												Special Revenue	Total	
	N.D.S.U.	School for the Blind	School for the Deaf	State Hospital	Ellendale	Valley City State U.	Mayville State U.	Industrial School	School of Science	School of Mines	Veterans Home	U.N.D.	Total	Capitol Building	Non-major Govern- mental Funds
Cash	\$ 237,911	\$ 76,915	\$ 19,330	\$ 25,909	\$ 84,081	\$ 52,549	\$ 17,834	\$ 59,023	\$ 28,017	\$ 87,395	\$ 6,551	\$ 71,388	\$ 766,903	\$ 70,998	\$ 837,901
Investments	62,350,578	9,940,396	19,673,400	13,531,521	18,264,781	10,988,293	6,955,517	19,803,603	15,543,194	18,145,956	4,986,754	28,633,856	228,817,849	4,939,362	233,757,211
Interest receivable	215,718	36,288	63,850	64,148	46,047	41,839	28,156	77,533	61,989	67,663	30,266	99,942	833,439	6,937	840,376
Accounts receivable	259,358	79,631	55,067	84,432	93,514	51,862	37,491	701,932	40,463	119,485	6,475	81,905	1,611,615	73,657	1,685,272
Invested securities lending collateral	2,590,397	412,602	818,487	564,223	756,012	456,549	289,184	824,599	646,858	754,816	208,130	1,190,034	9,511,891	688,639	10,200,530
Loans															
Farm loans	151,639	29,271	41,563	42,586	27,294	34,547	24,866	58,847	43,334	43,731	34,295	69,582	601,555		601,555
Due from other funds	50,631	1,141	-	3,511	2,251	556	770	14,693	273	-	4,531	4,328	82,685		82,685
Total Assets	\$ 65,856,232	\$ 10,576,244	\$ 20,671,697	\$ 14,316,330	\$ 19,273,980	\$ 11,626,195	\$ 7,353,818	\$ 21,540,230	\$ 16,364,128	\$ 19,219,046	\$ 5,277,002	\$ 30,151,035	\$ 242,225,937	\$ 5,779,593	\$ 248,005,530
Liabilities:															
Accounts payable	\$ 23,854	\$ 3,800	\$ 7,536	\$ 5,195	\$ 6,962	\$ 4,204	\$ 2,663	\$ 7,593	\$ 5,956	\$ 6,951	\$ 1,916	\$ 10,958	\$ 87,588	\$ 1,078	\$ 88,666
Securities lending collateral	2,590,397	412,602	818,487	564,223	756,012	456,549	289,184	824,599	646,858	754,816	208,130	1,190,034	9,511,891	688,639	10,200,530
Due to other state agencies	374	73	102	105	67	86	61	145	107	108	85	173	1,486		1,486
Total Liabilities	2,614,625	416,475	826,125	569,523	763,041	460,839	291,908	832,337	652,921	761,875	210,131	1,201,165	9,600,965	689,717	10,290,682
Fund Balance:															
Fund Balance:															
Special revenue funds															
Restricted	63,241,607	10,159,769	19,845,572	13,746,807	18,510,939	11,165,356	7,061,910	20,707,893	15,711,207	18,457,171	5,066,871	28,949,870	232,624,972	5,089,876	237,714,848
Total Fund Balance	63,241,607	10,159,769	19,845,572	13,746,807	18,510,939	11,165,356	7,061,910	20,707,893	15,711,207	18,457,171	5,066,871	28,949,870	232,624,972	5,089,876	237,714,848
Total Liabilities and Fund Balances	\$ 65,856,232	\$ 10,576,244	\$ 20,671,697	\$ 14,316,330	\$ 19,273,980	\$ 11,626,195	\$ 7,353,818	\$ 21,540,230	\$ 16,364,128	\$ 19,219,046	\$ 5,277,002	\$ 30,151,035	\$ 242,225,937	\$ 5,779,593	\$ 248,005,530

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
NON-MAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2017

Revenues:	Special Revenue Funds												Special Revenue Funds	Total	
	N.D.S.U.	School for the Blind	School for the Deaf	State Hospital	Ellendale	Valley City State U.	Mayville State U.	Industrial School	School of Science	School of Mines	Veterans Home	U.N.D.	Total	Capitol Building	Non-major Governmental Funds
Investment income	\$ 1,366,050	\$ 289,773	\$ 459,114	\$ 317,556	\$ 418,578	\$ 252,923	\$ 162,026	\$ 490,688	\$ 362,429	\$ 417,733	\$ 116,779	\$ 663,797	\$ 5,317,446	\$ 576,966	\$ 5,894,412
Loan income															
Farm loans	11,498	2,219	3,151	3,229	2,069	2,619	1,885	4,462	3,286	3,316	2,600	5,276	45,610		45,610
Change in fair value of investments	4,136,794	631,551	1,326,350	914,347	1,198,756	726,976	464,610	1,320,904	1,045,019	1,200,039	337,539	1,912,059	15,214,944	(12,345)	15,202,599
Securities lending income	9,697	1,545	3,064	2,112	2,830	1,709	1,083	3,087	2,421	2,826	779	4,455	35,608	2,466	38,074
Royalties	2,715,139	1,620,226	346,825	380,425	793,308	508,641	222,342	935,676	377,030	1,036,869	89,825	874,511	9,900,817	903,177	10,803,994
Bonuses	5,042	29,233	160	(13,288)	78,281	80	780	2,559	560	1,720	-	15,040	120,167	3,040	123,207
Rental income	251,318	62,535	78,860	28,368	70,323	69,933	49,536	72,147	73,984	58,442	38,110	159,775	1,013,331	168,642	1,181,973
Donations															-
Total Revenues	8,495,538	2,637,082	2,217,524	1,632,749	2,564,145	1,562,881	902,262	2,829,523	1,864,729	2,720,945	585,632	3,634,913	31,647,923	1,641,946	33,289,869
Expenditures:															
Current															
General government														36,613	36,613
Education	241,088	42,648	75,152	47,991	73,401	49,488	33,747	80,280	60,867	68,962	24,172	119,472	917,268		917,268
Total Expenditures	241,088	42,648	75,152	47,991	73,401	49,488	33,747	80,280	60,867	68,962	24,172	119,472	917,268	36,613	953,881
Excess of revenue over expenditures	8,254,450	2,594,434	2,142,372	1,584,758	2,490,744	1,513,393	868,515	2,749,243	1,803,862	2,651,983	561,460	3,515,441	30,730,655	1,605,333	32,335,988
Other Financing Uses:															
Transfer to Educational Institutions	(1,684,000)	(228,000)	(590,000)	(500,000)	(273,000)	(285,000)	(191,000)	(686,000)	(494,000)	(567,000)	(178,000)	(804,000)	(6,480,000)		(6,480,000)
Transfer to Facilities Management														(2,735,000)	(2,735,000)
Total Other Financing Uses	(1,684,000)	(228,000)	(590,000)	(500,000)	(273,000)	(285,000)	(191,000)	(686,000)	(494,000)	(567,000)	(178,000)	(804,000)	(6,480,000)	(2,735,000)	(9,215,000)
Increase (decrease) in net position	6,570,450	2,366,434	1,552,372	1,084,758	2,217,744	1,228,393	677,515	2,063,243	1,309,862	2,084,983	383,460	2,711,441	24,250,655	(1,129,667)	23,120,988
Net position - beginning as restated*	56,671,157	7,793,335	18,293,200	12,662,049	16,293,195	9,936,963	6,384,395	18,644,650	14,401,345	16,372,188	4,683,411	26,238,429	208,374,317	6,219,543	214,593,860
Net position - ending	\$ 63,241,607	\$ 10,159,769	\$ 19,845,572	\$ 13,746,807	\$ 18,510,939	\$ 11,165,356	\$ 7,061,910	\$ 20,707,893	\$ 15,711,207	\$ 18,457,171	\$ 5,066,871	\$ 28,949,870	\$ 232,624,972	\$ 5,089,876	\$ 237,714,848

*The beginning balance was restated due to reclassification of a fund to a fiduciary fund. See Note 27.

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
SCHEDULE OF CONTRIBUTIONS
LAST 10 FISCAL YEARS*
JUNE 30, 2017

Fiscal Year Ending	Pension Plan	Statutorily Required Contribution	Contributions in Relation to the Statutorily Required Contributions	Contribution Deficiency (Excess)	Trust Land's Covered- Employee Payroll	Contributions as a Percentage of Covered- Employee Payroll
June 30						
2015	PERS	\$ 118,962	\$ (120,360)	(1,398)	\$ 1,566,160	7.60%
2016	PERS	141,442	(127,027)	14,415	1,953,665	7.25%
2017	PERS	145,736	(147,738)	(2,002)	2,046,857	7.12%

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

NORTH DAKOTA DEPARTMENT OF TRUST LANDS
SCHEDULE OF EMPLOYER'S PROPORTIONATE
SHARE OF NET PENSION LIABILITY
LAST TEN FISCAL YEARS*
JUNE 30, 2017

For the Fiscal Year Ended June 30	Trust Land's Proportion of the Net Pension Liability (Asset)	Trust Land's Proportionate Share of the Net Pension Liability (Asset) (a)	Trust Land's Covered- Employee Payroll	Proportionate Share of the Net Pension Liability (Asset) as a Percentage of its Covered-employee Payroll	Plan Fiduciary Net Postion as a Percentage of the Total Pension Liability
2015 PERS	0.176238%	\$ 1,118,320	\$ 1,484,586	75.33%	77.70%
2016 PERS	0.175799%	1,195,403	1,566,160	76.33%	77.15%
2017 PERS	0.193861%	1,889,364	1,953,665	96.71%	70.46%

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

Notes to the Required Supplementary Information:

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, administrative expenses, salary scale, and percent married assumption.



CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

To the Governor of North Dakota
Legislative Audit and Fiscal Review Committee
North Dakota Department of Trust Lands
Bismarck, North Dakota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of North Dakota Department of Trust Lands, a department of the State of North Dakota, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise North Dakota Department of Trust Lands' basic financial statements, and have issued our report thereon dated October 23, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered North Dakota Department of Trust Lands' 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 North Dakota Department of Trust Lands' internal control. Accordingly, we do not express an opinion on the effectiveness of North Dakota Department of Trust Lands' internal control.

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

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

Compliance and Other Matters

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

Purpose of this Report

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



**BRADY, MARTZ & ASSOCIATES, P.C.
BISMARCK, NORTH DAKOTA**

October 23, 2017



CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

**INDEPENDENT AUDITOR'S COMMENTS REQUESTED BY
THE LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE**

To the Governor of North Dakota
Legislative Audit and Fiscal Review Committee
State of North Dakota
Bismarck, North Dakota

The Legislative Audit and Fiscal Review Committee require that certain items be addressed by independent certified public accountants performing audits of state agencies. These items and our responses are as follows:

Audit Report Communications:

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

Unmodified opinion.

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

Yes-a review was made of the pertinent chapters of the North Dakota Century Code and we felt the Department operated within the statutes, laws, rules and regulations under which it was created.

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. Was action taken on prior audit findings and recommendations?

No prior year audit finding.

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

No.

Audit Committee Communications:

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

None.

- 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 these estimates.**

Management's estimate of the fair value of investments is based on quoted market prices, estimates of fair value from investment managers, cash flow analysis, and yield currently available on comparable securities. We evaluated the key factors and assumptions used to develop the fair value estimate in determining that it is reasonable in relation to the financial statements taken as a whole.

Management's estimate of the unclaimed property liability is based on the historical average payout percentage per subsequent year to determine the current year liability. The historical average is based on a ten year rolling average percentage of the total unclaimed property amounts collected during a specific fiscal year paid out in subsequent fiscal years. We evaluated the key factors and assumptions and checked the clerical accuracy of the spreadsheet used to determine the liability and determined that it is reasonable in relation to the financial statements taken as a whole.

- 9. Identify any significant audit adjustments.**

There were no material audit adjustments detected during the audit. There were passed (immaterial) audit adjustments which are identified in the audit committee letter on page 60.

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

None.

- 11. Identify any significant difficulties encountered in performing the audit.**

None.

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

None.

- 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 addressed above are directly related to the operations of an information technology system.**

The State Lands Information Management System (SLIMS) is a database application that supports the Department's business process over management of state lands, mineral and surface leases, royalties, investments, grants management, and general ledger accounting. There were no exceptions identified that were directly related to the SLIMS data base application.

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



**BRADY, MARTZ & ASSOCIATES, P.C.
BISMARCK, NORTH DAKOTA**

October 23, 2017



CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

October 23, 2017

To Governor Burgum
The Legislative Assembly
North Dakota Department of Trust Lands
Bismarck, North Dakota

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of North Dakota Department of Trust Lands, a department of the State of North Dakota, for the year ended June 30, 2017. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated August 3, 2017. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by North Dakota Department of Trust Lands are described in Note 1 to the financial statements. No new accounting policies were adopted during 2017. The Department did change the accounting and financial presentation of the Indian Cultural Education Trust as noted in Note 27 of the financial statements. We noted no transactions entered into by the department during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

Management's estimate of the fair value of investments is based on quoted market prices, estimates of fair value from investment managers, cash flow analysis, and yields currently available on comparable securities. We evaluated the key factors and assumptions used to develop the fair value estimate in determining that it is reasonable in relation to the financial statements taken as a whole.

Management's estimate of the unclaimed property liability is based on the historical average payout percentage per subsequent year to determine the current year liability. The historical average is based on a ten year rolling average percentage of the total unclaimed property amounts collected during a specific fiscal year paid out in subsequent fiscal years. We evaluated the key factors and assumptions and checked the clerical accuracy of the spreadsheet used to determine the liability and determined that it is reasonable in relation to the financial statements taken as a whole.

The financial statement disclosures are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. The schedule below summarizes uncorrected misstatements of the financial statements. Management has determined their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

	<u>Debit</u>	<u>Credit</u>
<u>Non Major Funds</u>		
Revenues	\$48,353	
Expenditures		\$48,353
To correct overstatement of revenues and expenditures due to entry being recorded twice.		
<u>Common Schools Fund</u>		
Investments	\$103,670	
Fund Balance		\$103,670
<u>Non-Major Funds</u>		
Fund Balance	\$103,670	
Investments		\$103,670
<u>Permanent Trusts</u>		
Investment		\$105,165
Fund Balance	\$105,165	
To correct investment allocation.		
<u>Common Schools Fund</u>		
Capital Assets	\$544,597	
Investments		\$544,597
To recode capital asset recorded as an investment.		
<u>Non-Major</u>		
Revenues	\$260,519	
Fund Balance		\$260,519
To correct incorrectly allocated income for tract allocations.		

<u>Common Schools</u>		
Fund Balance	\$260,519	
Revenues		\$260,519
To correct incorrectly allocated income for tract allocations		
 <u>Common Schools</u>		
Unclaimed Property Liability		\$3,986,456
Fund Balance	\$3,986,456	
To record understatement of unclaimed property liability.		
 <u>Common Schools</u>		
Revenues		\$880,198
Expenses	\$880,198	
 <u>SIIF</u>		
Revenues		\$345,001
Expenses	\$345,001	
 <u>Coal Development Trust Fund</u>		
Revenues		\$14,218
Expenses	\$14,218	
 <u>Non-Major</u>		
Revenues		\$59,354
Expenses	\$59,354	
To record securities lending at gross amounts in accordance with GASB 28.		

Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated October 23, 2017.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year. However, these discussions occurred in the normal course of our professional relationship.

Other Matters

We applied certain limited procedures to management's discussion and analysis, Schedule of Contributions and Schedule of Employer's Proportionate Share of Net Pension Liability, which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding 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 did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the combining fund statements, which accompany the financial statements but are not RSI. With respect to this supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

Restrictions on Use

This information is intended solely for the use of the Governor, the Legislative Assembly, and management of North Dakota Department of Trust Lands, and is not intended to be, and should not be, used by anyone other than these specified parties.

Sincerely,



**BRADY, MARTZ & ASSOCIATES, P.C.
BISMARCK, NORTH DAKOTA**

October 23, 2017