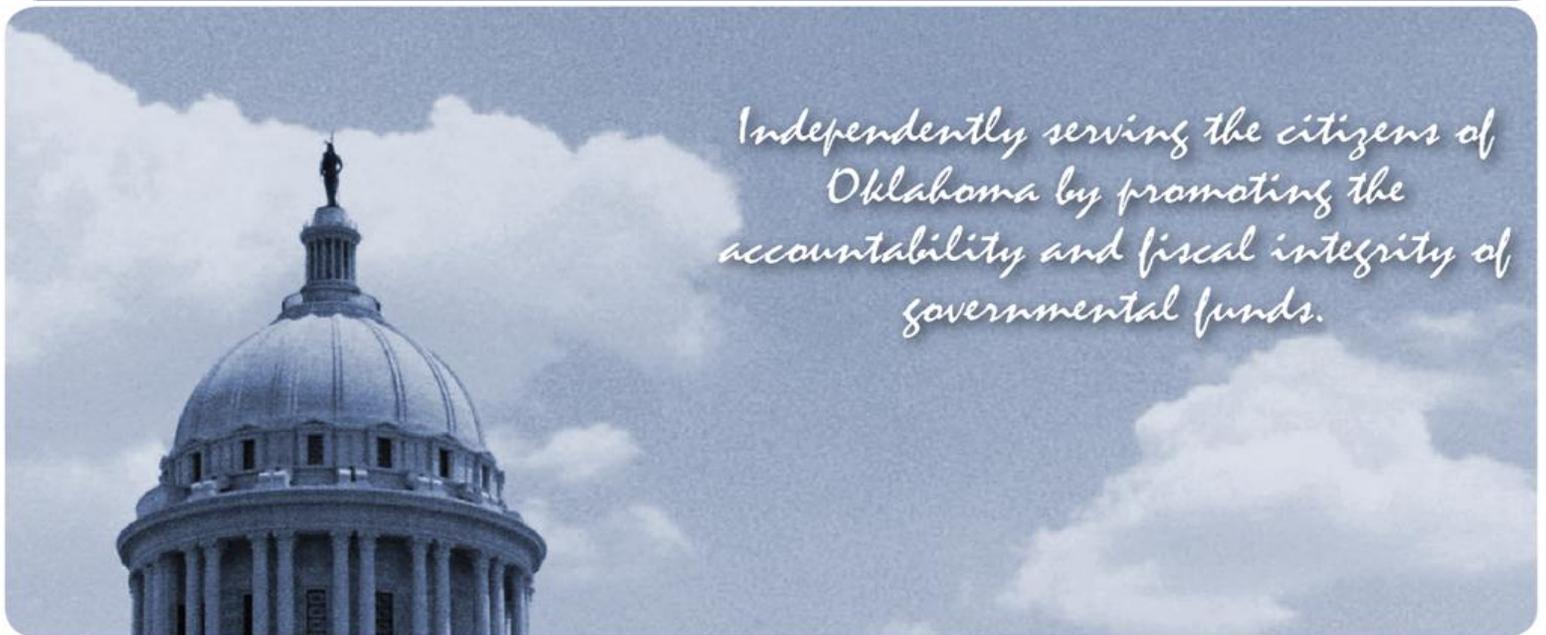


FINANCIAL AUDIT

OFFICE OF THE STATE TREASURER

For the fiscal year ended June 30, 2016



*Independently serving the citizens of
Oklahoma by promoting the
accountability and fiscal integrity of
governmental funds.*



Oklahoma State
Auditor & Inspector
Gary A. Jones, CPA, CFE

**OFFICE OF THE STATE TREASURER OF OKLAHOMA
FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2016**

This publication, issued by the Oklahoma State Auditor and Inspector's office as authorized by 74 O.S. § 212, has not been printed, but is available on the agency's website (www.sai.ok.gov) and the Oklahoma Department of Libraries Publications Clearinghouse Digital Collection, pursuant to 65 O.S. § 3-114.



Oklahoma State Auditor & Inspector

2300 N. Lincoln Blvd. • State Capitol, Room 100 • Oklahoma City, OK 73105 • Phone: 405.521.3495 • Fax: 405.521.3426

January 9, 2017

**TO THE HONORABLE MARY FALLIN
GOVERNOR OF THE STATE OF OKLAHOMA**

This is the audit report and the financial statements of the Office of the State Treasurer for the year ended June 30, 2016. The goal of the State Auditor and Inspector is to promote accountability and fiscal integrity in state and local government. Maintaining our independence as we provide this service to the taxpayers of Oklahoma is of utmost importance.

This report is a public document pursuant to the Open Records Act (51 O.S. § 24A.1 et seq.), and shall be open to any person for inspection and copying,

We wish to take this opportunity to express our appreciation for the assistance and cooperation extended to our office during our engagement.

Sincerely,

A handwritten signature in blue ink that reads "Gary A. Jones". The signature is fluid and cursive, with a long horizontal stroke at the end.

GARY A. JONES, CPA, CFE
OKLAHOMA STATE AUDITOR AND INSPECTOR

**OFFICE OF THE STATE TREASURER OF OKLAHOMA
FINANCIAL STATEMENTS AND INDEPENDENT
AUDITOR'S REPORTS
FOR THE YEAR ENDED JUNE 30, 2016**

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INDEPENDENT AUDITOR'S REPORT

**TO THE HONORABLE KEN MILLER
STATE TREASURER OF OKLAHOMA**

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and each major fund of the Office of the State Treasurer (OST), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Office of the State Treasurer's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

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

Emphasis of Matters

As discussed in Note 1, the financial statements of the Office of the State Treasurer are intended to present the financial position and the changes in financial position of only that portion of the general fund of the State of Oklahoma that is attributable to the transactions of Office of the State Treasurer. They do not purport to, and do not, present fairly the financial position of the State of Oklahoma as of June 30, 2016, the changes in its 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.

Also as discussed in Note 1 to the financial statements, in FY 2016 the Office of the State Treasurer adopted new accounting guidance, GASB Statement No. 68, *Accounting and Financial Reporting for Pensions— An Amendment of GASB Statement No. 27* and GASB Statement No. 71, *Government Pension Transition for Contributions Made Subsequent to the Measurement Date—An Amendment to GASB Statement 68*.

Our opinion is not modified with respect to these matters.

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 4-8 and the pension schedules on pages 37 and 38 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 Office of the State Treasurer's basic financial statements. The Expenditures by Object Code schedule is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The Expenditures by Object Code schedule has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 5, 2017, on our consideration of the Office of the State Treasurer's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Office of the State Treasurer's internal control over financial reporting and compliance.

A handwritten signature in blue ink that reads "Gary A. Jones". The signature is fluid and cursive, with the first name "Gary" being the most prominent.

GARY A. JONES, CPA, CFE
OKLAHOMA STATE AUDITOR AND INSPECTOR

January 5, 2017

MANAGEMENT'S DISCUSSION & ANALYSIS

Office of the State Treasurer of Oklahoma
Management's Discussion and Analysis
June 30, 2016

Management of the Office of the State Treasurer of Oklahoma provides this Management's Discussion and Analysis (MD&A) as an overview and overall review of the Office of the State Treasurer's financial activities for the fiscal year ended June 30, 2016. The intent of the MD&A is to look at the Office of the State Treasurer's financial performance as a whole. It should, therefore, be read in conjunction with the financial statements and accompanying notes.

FINANCIAL HIGHLIGHTS

Statement of Net Position

The Statement of Net Position provides an indication of the Office of the State Treasurer's financial condition at the end of the 2016 fiscal year; the statement reports all assets and liabilities using the accrual basis of accounting. The Statement of Activities reports all of the revenues and expenses during the time periods indicated.

OFFICE OF THE STATE TREASURER
NET POSITION

	2016	2015*
Current Assets	\$ 10,948,103	\$ 8,940,265
Capital assets	216,787	299,133
Capital assets - Development in Progress	1,525,515	1,525,515
Total Assets	12,690,405	10,764,913
Deferred Outflows – Pensions	810,557	411,235
Current Liabilities	898,684	693,559
Noncurrent Liabilities	565,969	299,982
Total Liabilities	1,464,653	993,541
Deferred Inflows - Pensions	681,975	864,443
Invested in capital assets	1,742,302	1,824,648
Unrestricted	9,612,032	7,493,516
Total Net Position	\$ 11,354,334	\$ 9,318,164

*Amounts for the 2015 Statement of Net Position have been restated to reflect the implementation of GASB 68 and GASB 71. See Note 12 for more information.

As of June 30, 2016, the Office of the State Treasurer's increase in current assets was primarily attributable to net revenues received for the administration of the unclaimed property program, the continued use of compensating balances to offset banking fees and recognition of a receivable for unclaimed property program expenses that were accrued at year end and are reimbursable.

No funds were expended on systems development projects to replace COBOL based disbursement and cash management applications. These projects remained on hold during the period and resources were redirected to upgrade other statewide applications to support Higher Education payroll and compliance with Affordable Care Act requirements. Information technology services were consolidated statewide into the Office of Management and Enterprise Services Information Services Division (OMES ISD). The Office continues to work with OMES ISD to re-engage projects to upgrade certain disbursement applications during FY2017.

Accounts payable vendors increased due to unclaimed property program expenses that were accrued at year end. Noncurrent liabilities increased due to the increase in the net pension liability during the period.

Unrestricted net position primarily includes funds received for the administration of the Unclaimed Property Program in excess of program expenses and funds received from securities lending for the payment of bank fees pursuant to state statute. It also includes other funding internally designated for capital projects like systems development and hardware replacement. The unrestricted net position increase of 17% during the year is attributable to net revenues from the administration of the Unclaimed Property Program in excess of program expenditures, increased use of compensating balances to offset certain banking fees, and steps taken by the Office to reduce expenditures pursuant to budget failures during the period.

Statement of Activities - Revenues and Expenses

Four percent (4%) of all property relinquished to the state under the Uniform Unclaimed Property Act is recognized as revenue by the Office of the State Treasurer and used to finance certain Unclaimed Property Program expenses. Program revenues also include transfers from the Unclaimed Property Fund to pay for Personnel Services charges associated with property recovery and advertising services. Gross receipts to the Oklahoma Uniform Unclaimed Property Fund declined approximately \$6.3 million from FY15 to FY16 resulting in a \$250,000 decline in agency revenues for program administration. Personnel Services charges for the recovery of unclaimed property declined by \$650,000 from FY15 to FY16.

Except for revenues received for the administration of the Unclaimed Property Program, operating revenues of the Office of the State Treasurer are largely dependent upon state General Revenue appropriation. The Office of the State Treasurer received a 9% decrease in the FY2016 General Revenue appropriation.

Amounts paid for banking fees decreased in FY 2016 as the fees offset by earnings credits increased from \$275,000 in FY 2015 to \$390,000 in FY 2016.

The significance of the statewide budget deficit for FY 2018 may have an impact on the Office of the State Treasurer’s net assets as further discussed below.

OFFICE OF THE STATE TREASURER
 STATEMENT OF ACTIVITIES

	2016	2015*
General Revenues		
Appropriations	\$ 3,050,060	\$ 3,354,437
Unclaimed Property	5,440,842	5,990,200
Service Charges	44,808	55,348
Administrative Charges	498,080	457,360
Securities Lending	211,739	152,847
Total General Revenues	9,245,529	10,010,192

Office of the State Treasurer of Oklahoma
 Financial Statement Report
 For the Year Ended June 30, 2016

Expenses

Personnel Services	5,776,891	6,320,063
Travel	34,734	49,589
Administrative Expenses	142,321	145,420
Contracted Services	280,146	259,243
Equipment	1,902	10,411
Other	1,317	1,328
Bank Service Charges	278,540	412,492
Bank Service Charges Securities Lending	31,761	22,927
Payments to Counties	95,000	100,000
Depreciation	82,346	73,339
Total Expenses	6,724,958	7,394,812
 Excess Before Transfers	 2,473,663	 2,615,380
 Transfers	 (484,401)	 (1,020,511)
Increase (Decrease) in Net Position	2,036,170	1,594,869
 Net Position Beginning Balance, as restated	 9,318,164	 7,723,295
 Net Position Ending Balance	 \$ 11,354,334	 \$ 9,318,164

*Amounts for the 2015 Statement of Activities have been restated to reflect the implementation of GASB 68 and GASB 71.

Fund Highlights:

Governmental Fund - Fund Balance

In anticipation of a state budget deficit for FY 2017, the Governor of the State of Oklahoma issued a moratorium on non-essential out-of-state travel and has directed each agency to reduce non-mission-critical agency expenses by 10% for FY 2016 and FY 2017. The Office of the State Treasurer identified and transferred \$1,000,000 in excess funds after June 30, 2016 from the unclaimed property administration fund to the State's General Fund to help address the State's FY 2017 budget deficit. The ongoing contraction in Gross Receipts to the Treasury driven by low oil and gas prices has now lasted longer than the downturn experienced from the Great Recession. The significance of the statewide budget deficit for FY 2018 may have an impact on the availability of assigned fund balances to fund long-term projects.

USING THIS ANNUAL REPORT

The basic financial statements presented in the annual report include both government-wide and fund financial statements.

Government-wide statements:

Government-wide statements include a Statement of Net Position and a Statement of Activities. These statements display information about the Office of the State Treasurer as a whole. The government-wide financial statements of the Office of the State Treasurer are presented on an economic resources measurement focus and a full accrual basis of accounting which includes all assets and liabilities whether current or non-current. These statements provide both short-term and long-term information about the Office of the State Treasurer's overall financial status.

Fund statements:

The fund financial statements include the Governmental Fund Balance Sheet and Statement of Revenue, Expenditures, and Changes in Fund Balance. In the fund financial statements, the revenues and expenditures of the Office of the State Treasurer are presented using the current financial resources measurement focus and the modified accrual basis of accounting. Under these accounting methods, revenues and assets are recognized when they become both measurable and available, and expenditures and liabilities are recognized when obligations are incurred as a result of the receipt of goods or services.

The Office of the State Treasurer provides banking and investment services for state agencies and administers the Oklahoma Unclaimed Property Program. The deposits and investments held by the Office of the State Treasurer on behalf of the State are reported in the Fiduciary Fund.

This financial report is designed to provide a general overview of the Office of the State Treasurer's finances for all of Oklahoma's citizens, taxpayers, customers, and investors and creditors. This financial report seeks to demonstrate the Treasurer's accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to:

Susan Nicewander, Chief Deputy State Treasurer
2300 N. Lincoln Blvd. Room 217
Oklahoma City, OK 73105

Sherian Kerlin, Director of Portfolio Accounting & Reporting
2300 N. Lincoln Blvd. Room 217
Oklahoma City, OK 73105

BASIC FINANCIAL STATEMENTS

OFFICE OF THE STATE TREASURER
STATEMENT OF NET POSITION
June 30, 2016

ASSETS

Cash	\$	9,830,904
Due from the Fiduciary Fund		1,117,199
Capital Assets, net of Accumulated Depreciation		
Furniture, Fixtures, and Equipment		216,787
Capital Assets - Development in Progress		<u>1,525,515</u>
Total Assets		<u>12,690,405</u>

Deferred Outflows - Pensions		<u>810,557</u>
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LIABILITIES

Accounts Payable Vendors	676,024
Accrued Payroll Expenses	62,452
Net Pension Liability - Noncurrent	490,501
Compensated Absences:	
Payable Within One Year	160,208
Payable After One Year	<u>75,468</u>
Total Liabilities	<u>1,464,653</u>

Deferred Inflows - Pensions	<u>681,975</u>
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NET POSITION

Invested in Capital Assets	1,742,302
Unrestricted	<u>9,612,032</u>
Total Net Position	<u>\$ 11,354,334</u>

The notes to the financial statements are an integral part of this statement.

**OFFICE OF THE STATE TREASURER
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2016**

Expenses

Governmental Activities - General Government:

Personnel Services	\$ 5,776,891
Travel	34,734
Administrative Expenses	142,321
Contracted Services	280,146
Equipment	1,902
Other	1,317
Bank Service Charges	278,540
Bank Service Charges Securities Lending	31,761
Payments to Counties	95,000
Depreciation	<u>82,346</u>
Total Expenses	<u>6,724,958</u>

General Revenues

Appropriations	3,050,060
Unclaimed Property	5,440,842
Service Charges	44,808
Administrative Charges	498,080
Securities Lending	<u>211,739</u>
Total General Revenues	<u>9,245,529</u>

Transfers (484,401)

Change in Net Position 2,036,170

Net Position, July 1, 2015 (as restated) 9,318,164

Net Position, June 30, 2016 \$ 11,354,334

The notes to the financial statements are an integral part of this statement.

**OFFICE OF THE STATE TREASURER
BALANCE SHEET
GOVERNMENTAL FUND
June 30, 2016**

		<u>GENERAL FUND</u>
ASSETS		
Cash	\$	9,830,904
Due from the Fiduciary Fund		1,117,199
Total Assets	\$	<u><u>10,948,103</u></u>
 LIABILITIES AND FUND BALANCE		
Liabilities		
Accounts Payable Vendors	\$	676,024
Accrued Payroll Expenses		62,452
Total Liabilities		<u><u>738,476</u></u>
 Fund Balance		
Committed to:		
Unclaimed Property Program Administration		5,243,782
Banking Fees		887,396
Assigned to:		
Compensated Absences and Succession Planning		400,000
Hardware Replacement and Systems Development		3,678,449
Total Fund Balance		<u><u>10,209,627</u></u>
Total Liabilities and Fund Balance	\$	<u><u>10,948,103</u></u>

The notes to the financial statements are an integral part of this statement.

**OFFICE OF THE STATE TREASURER
RECONCILIATION OF THE GOVERNMENTAL FUND
BALANCE SHEET TO THE STATEMENT OF NET POSITION
June 30, 2016**

Total Fund Balance - Governmental Fund	\$ 10,209,627
Capital Assets used in governmental activities are not financial resources and therefore are not reported in the fund.	
Furniture, Fixtures, and Equipment	216,787
Development in Progress	1,525,515
Deferred outflows related to the pension are not financial resources and therefore are not reported in the fund.	
	810,557
Long term liabilities are not due and payable in the current period and therefore are not reported in the fund.	
Compensated Absences	(235,676)
Net Pension Liability	(490,501)
Deferred inflows related to the pension are not due and payable in the current period and therefore are not reported in the fund.	
	<u>(681,975)</u>
Net Position of Governmental Activities	<u>\$ 11,354,334</u>

The notes to the financial statements are an integral part of this statement.

**OFFICE OF THE STATE TREASURER
STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCE
GOVERNMENTAL FUND
FOR THE YEAR ENDED JUNE 30, 2016**

	GENERAL FUND
Revenues	
Unclaimed Property	\$ 5,440,842
Service Charges	44,808
Administrative Charges	498,080
Securities Lending	211,739
Total Revenues	6,195,469
Expenditures	
Personnel Services	6,098,744
Travel	34,734
Administrative Expenses	142,321
Contracted Services	280,146
Equipment	1,902
Other	1,317
Bank Service Charges	278,540
Bank Service Charges Securities Lending	31,761
Payments to Counties	95,000
Total Expenditures	6,964,465
Revenues Over (Under) Expenditures	(768,996)
Other Financing Sources (Uses)	
Appropriations	3,050,060
Transfers	(484,401)
Total Other Financing Sources (Uses)	2,565,659
Net Change In Fund Balance	1,796,663
Fund Balance, July 1, 2015	8,412,964
Fund Balance, June 30, 2016	\$ 10,209,627

The notes to the financial statements are an integral part of this statement.

**OFFICE OF THE STATE TREASURER
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCE OF THE
GOVERNMENTAL FUND TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR END JUNE 30, 2016**

Net Change in Fund Balance - Governmental Fund	\$ 1,796,663
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Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which depreciation exceeded capital outlays in the current period.	(82,346)
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Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.

This amount represents the increase in unused compensated absences during the current period.	(4,785)
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This amount represents the increase in the net pension liability (\$255,152), the increase in deferred outflows (\$399,322), and the decrease in deferred inflows (\$182,468) during the current period.	326,638
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Change in net position of governmental activities	\$ <u><u>2,036,170</u></u>
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The notes to the financial statements are an integral part of this statement.

**OFFICE OF THE STATE TREASURER
STATEMENT OF FIDUCIARY ASSETS AND LIABILITIES
FIDUCIARY FUND
June 30, 2016**

	<u>Agency Fund</u>
ASSETS	
Cash	
Cash and Cash Equivalents	\$ 682,384,968
Investments	
Treasurer's Portfolio	
OKinvest	5,171,898,247
General Revenue	49,400,000
State Agency Portfolio	2,152,481
Total Investments	<u>5,223,450,728</u>
Interest Receivable	
OKinvest Portfolio	18,650,482
General Revenue Portfolio	175,392
Total Interest Receivable	<u>18,825,874</u>
 Total Assets	 <u>\$ 5,924,661,570</u>
 LIABILITIES	
Balance Due Depositors	
State Government Entities	\$ 5,921,391,891
State Government Entities Investments	2,152,480
Total Due Depositors	<u>5,923,544,371</u>
Due to the General Fund	<u>1,117,199</u>
 Total Liabilities	 <u>\$ 5,924,661,570</u>

The notes to the financial statements are an integral part of this statement.

FOOTNOTES TO THE FINANCIAL STATEMENTS

**OFFICE OF THE STATE TREASURER
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

1. Summary of Significant Accounting Policies

In June 2012 the Governmental Accounting Standards Board (GASB) issued Statement 68 *Accounting and Financial Reporting for Pensions-An Amendment of GASB Statement No. 27*. The objective of this statement is to improve accounting and financial reporting by state and local governments for pensions that are provided to employees through pension plans that are administered through trusts. GASB 68 establishes standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources and expenses/expenditures. For defined benefit pensions, GASB 68 identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. The Office of the State Treasurer (the Office) adopted this statement effective July 1, 2015 which resulted in the restatement of beginning net assets of the Office. See Note 12.

In November 2013 GASB issued Statement 71 *Pension Transition for Contributions Made Subsequent to the Measurement Date-An Amendment of GASB Statement 68*. The objective of this statement is to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. The Office adopted this statement effective July 1, 2015 which resulted in the restatement of beginning net assets of the Office. See Note 12

In February 2015 GASB issued Statement 72 *Fair Value Measurement and Application* to address accounting and financial reporting issues related to fair value measurements. This statement provides guidance for determining a fair value measurement for financial reporting purposes. The statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The Office adopted this statement for the June 30, 2016 reporting year providing additional disclosures regarding the fair value of investments. See Note 3

In June of 2015, GASB Statement No. 73 *Accounting and Financial Reporting for Pension and Related assets That Are not within the Scope of Statement 68, and amendments to Certain Provisions of GASB Statements 67 and 68* establishes requirements for defined benefits pensions that are not within the scope of Statement No. 68, *Accounting and Financial Reporting for Pensions*, as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of Statement 68. It also amends certain provisions of Statement No. 67, *Financial Reporting for Pension Plans*, and Statement 68 for pension plans and pensions that are within their respective scopes.

The requirements of this Statement extend the approach to accounting and financial reporting established in Statement 68 to all pensions, to reflect that for accounting and financial reporting purposes, any assets accumulated for pensions that are provided through pension plans that are not administered through trusts that meet the criteria specified in Statement 68 should not be considered pension plan assets. The Office adopted this statement for the June 30, 2016 fiscal year.

In June of 2015, GASB Statement No. 76 *The Hierarchy of Generally Accepted Accounting Principles for the State and Local Governments* identifies, in the context of the current governmental financial reporting environment, the hierarchy of GAAP. The "GAAP hierarchy" consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those

principles. This statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and non-authoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP.

The result of this Statement is financial reporting guidance application with less variation, which improves the usefulness of financial statement information. The Office adopted this statement for the June 30, 2016 fiscal year.

A. Reporting Entity

The Office is established under authority of the Constitution of Oklahoma as an agency of the State. The State Treasurer performs duties as designated by the Constitution or prescribed by law. The Office is a part of the primary government of the State of Oklahoma.

The State Treasurer is elected every four years and takes office the second Monday in January following the election for the position in November. On January 10, 2011 the Honorable Ken Miller assumed the position of State Treasurer. He was unopposed in the 2014 election and began his second term of office on January 12, 2015.

The primary functions of the Office are the maintenance of bank accounts for the receipt and disbursement of state funds, the prudent investment of certain state funds, the recording and servicing of the long-term debt of the State, and the administration of the State's Unclaimed Property program. Additionally, the Office monitors the collateralization of state funds on deposit in state banks and performs investment functions for state agencies, and other entities as authorized by state statute. Various activities of the Office include receipt of warrants, vouchers, and debt instruments, management of cash and investments, and the reconciliation of account balances and transactions with banks and with the various state agencies. The Treasurer's office is also responsible for accounting functions associated with the Tobacco Settlement Endowment Trust Fund.

B. Basis of Presentation, Measurement Focus and Basis of Accounting Government-Wide Financial Statements

The government-wide financial statements are presented using the accrual basis of accounting and the economic resources measurement focus. All of the functions available to finance the Office are presented together as general government activities. Financial information for funds that are not available to finance these activities is not included; consequently, the government-wide financial statements exclude fiduciary assets and liabilities.

Using the economic resources measurement focus, all assets and liabilities, both current and long-term, associated with the operation of the Office activities are presented in the statement of net position. Under the accrual basis of accounting revenues are recognized as they are earned and expenses are recognized as they are incurred. General revenues include charges for banking and investment services rendered by this Office to individual state agencies. Additionally, the Office receives reimbursement for certain costs incurred in connection with the recovery, advertisement, and sale of unclaimed property. The Office also receives up to 4% of unclaimed property receipts to offset certain capital and administrative costs incurred in connection with the administration of the State's Unclaimed Property Program.

Fund Financial Statements

The fund financial statements report the detailed activities of the Office by fund type for governmental and fiduciary funds as described below.

Governmental Fund

General Fund - The General Fund is the primary operating fund of the Office. This fund is used to account for all financial transactions and resources except those required to be accounted for in another fund. The general fund financial statements are presented using the modified accrual basis of accounting and the current financial resources measurement focus. Using the current financial resources measurement focus, only current assets and current liabilities are included on the balance sheet in the general fund financial statements. The modified accrual basis of accounting provides for the recognition of revenues when they become both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Office considers revenues to be available if they are collected within 60 days of the end of the current fiscal year end. The Office is entitled to reimbursement for certain costs incurred in connection with administration of the Unclaimed Property Program. These revenues are recognized when the related expenditures are incurred. The Office also receives 4% of the monies accruing to the State according to state statute as service charges. Revenues for these service charges are recognized based on the monies that are remitted to the State. Expenditures are generally recognized when the related liability is incurred except for compensated absences where vested annual leave is recorded as an expenditure when utilized.

Since the general fund financial statements are presented on a different measurement focus and basis of accounting than the government-wide financial statements, a reconciliation is presented which briefly explains the adjustments necessary to reconcile the fund and government-wide presentations.

Governmental Fund – Fund Balance Reserves and Designations

The governmental fund financial statement presents fund balance in the categories defined by GASB Statement 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. The Office fund balance does not contain any nonspendable or restricted amounts. Committed fund balance is presented for each respective function of the Office as directed by Oklahoma law. Pursuant to Title 60 Section 668 of the Oklahoma Statutes, the Office receives 4% of the funds accruing to the state under the Uniform Unclaimed Property Act to be used to defray the administrative costs of the program. Pursuant to Title 62 Section 90 of the Oklahoma Statutes the Office receives funds from the securities lending program to pay banking fees.

Along with ratification by the Governor, the Senate and the House of Representatives write, prepare and approve legislative bills to allocate the state's available resources each fiscal year. The Office receives an appropriation from this legislative process over which the Treasurer is authorized to assign amounts to specific purposes. The Office is in the midst of several multi-year projects to upgrade or replace outdated unsupported systems and related hardware for better management and greater efficiency. Over 20% of Office employees may retire in the next five years, consequently succession planning is underway to reasonably ensure the success of continuing operations. It is expected that the costs of these ongoing efforts will exceed the Office's remaining fund balance as of June 30, 2016, accordingly, the entire amount has been reflected as assigned.

The committed and assigned fund balances are considered to be unrestricted fund balances. Generally when the Office has both restricted and unrestricted resources available, the restricted balances will be used first as expenditures are incurred as long as conditions that created the restriction are met. When unrestricted fund balance is used, the order of use would generally be committed and then assigned.

Fiduciary Fund

Fiduciary Fund - This fund is used to account for assets held by the Office in a trustee or agency capacity. The Office is the official depository for all agencies of the State and, accordingly, receives and disburses all monies of the State. The agency fund is accounted for using the accrual basis of accounting.

C. Cash and Cash Equivalents

The state uses a pooled cash concept in maintaining its bank accounts and other cash equivalents. All cash is pooled for operating and investment purposes and the Office has relative equity in the pooled amount. Interest earned on the Office's equity is allocated to the state's General Fund. Cash equivalents are defined as short-term, highly liquid investments with a maturity of three months or less that are readily convertible to cash.

D. Investment Holdings and Basis

Investments are generally stated at fair value, except for investments in nonparticipating interest-earning investment contracts (e.g. nonnegotiable certificates of deposit) which are stated at cost, or amortized cost which approximates market value. With the implementation of GASB Statement 72 *Fair Value Measurement and Application*, the Office categorizes its fair value measurements within the specified fair value hierarchy as further described in Note 3.

E. Capital Assets

All furniture, fixtures, and equipment costing more than \$2,500 and information systems equipment over \$500 that may be used repeatedly without material impairment of its physical condition and that has a calculable period of service of more than one year are recorded as capital assets. Capital assets are recorded at cost when purchased or estimated cost as determined by available records maintained by the Office. Donated capital assets are recorded at their fair value on the date of donation.

Depreciation is recorded on capital assets in the government-wide financial statements. Depreciation is calculated on a straight line basis over the following estimated useful lives.

	<u>Years</u>
Information systems	4 - 7
Office furniture, fixtures and equipment	6 - 12

No provision for depreciation is recorded in the general fund financial statements as expenditures for capital assets are recorded as period costs when the capital assets are purchased.

F. Compensated Absences

Employees of the Office entering State service earn annual vacation leave at the rate of 10 hours per month for the first 5 years of service, 12 hours per month for service of 5 to 10 years, 13.3 hours per month for service of 10 to 20 years, and 16.66 hours per month for over 20 years of service. Unused annual leave may be accumulated to a maximum of 240 hours for those with service of up to 5 years. After 5 years of service the maximum number of hours that can be accumulated and carried into the next year is 480 hours. All accrued annual leave is payable upon termination, resignation, retirement, or death. The following is a summary of the changes in compensated absences for the year ended June 30, 2016.

	Balance June 30, 2015	Increases	Decreases	Balance June 30, 2016
Compensated Absences	\$ 230,891	152,301	147,516	\$ 235,676

2. Deposits

The **custodial credit risk** for deposits is the risk that in the event of a bank failure, the State's deposits may not be recovered. In accordance with Title 62 O.S. § 72.4, the State Treasurer minimizes custodial credit risk by requiring financial institutions to pledge collateral securities and/or provide collateral instruments in an amount not less than the deposits of the State in each such institution. The amount of collateral securities to be pledged and/or coverage to be provided by collateral instruments is established by rules promulgated by the State Treasurer. In accordance with the rules established by the State Treasurer, the market value of collateral securities pledged by financial institutions combined with the coverage provided by additional collateral instruments, if any, is equal to or greater than 110% of the amount on deposit, less any federal insurance coverage. If only collateral instruments are provided, the coverage is equal to or greater than the amount on deposit, less any federal insurance coverage. Collateral securities are held in a restricted account by an agent of the State Treasurer (i.e., a Federal Reserve Bank, a Federal Home Loan Bank, or a third-party safekeeping bank approved by the State Treasurer).

3. Investments and Securities Lending

Investments

The Office maintains two investment portfolios as follows: Treasurer's Portfolio -- for the investments of all state monies that are under the control of the Treasurer for which the earnings accrue to the general fund of the State or state agencies; and State Agency Portfolio -- for the investments of a limited number of state agencies which are specifically authorized by statute to direct the investment activities of certain funds and accounts for which the investment earnings accrue to those funds and accounts.

The Treasurer or his investment officer is authorized to invest the state monies under his control in the types of securities specified in Title 62 O.S. § 89.2. The Treasurer's Portfolio investments during the year have included U.S. Treasury securities, U.S. agency and instrumentality obligations, commercial paper, SEC-registered money market mutual funds, certificates of deposit and foreign bonds.

The types of investments in which specific state agencies are authorized to invest are established by law or by their boards or commissions. Generally, the investments of the state agencies are

the same types as the Treasurer's investments, except for one agency which invests in equity mutual funds.

The State Treasurer operates an internal investment pool, OK Invest, for state funds and state agencies. Only those agencies and funds that are considered to be part of the State's reporting entity in the State's Comprehensive Annual Financial Report and who have funds deposited with the State Treasurer may participate in OK Invest.

Investment Policy

The State Treasurer has a formal investment policy which was updated June 30, 2016. This policy applies to all funds of the State entrusted to the Treasurer by specific statutory investment authority as delineated in Title 62 O.S. § 89.2. This policy also applies to the investments of state agencies when they request that the Treasurer act as their agent. Only investment transactions relating to the following are covered by this policy: U.S. Treasury Bills, Notes and Bonds, U.S. Government Agency Securities, collateralized or insured Certificates of Deposit and other evidences of deposit, negotiable Certificates of Deposit, Banker's acceptances, Commercial paper, obligations of state and local governments, including obligations of Oklahoma State public trusts, repurchase agreements and tri-party repurchase agreements, money market mutual funds, short term bond funds and foreign government bonds.

Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Generally, the State's investing activities are managed under the custody of the State Treasurer. The following table details credit ratings that are set by the State Treasurer's Investment Policy to mitigate this risk.

Custodial Credit Risk is the risk that in the event of the failure of a counterparty, the State will not be able to recover the value of its investments. Deposits are exposed to custodial credit risk if they are uninsured and uncollateralized. Investment securities are exposed to custodial credit risk if they are uninsured, not registered in the name of the State, or held by the counterparty or its trust department but not in the State's name.

Concentration of Credit Risk is the risk of loss attributed to the magnitude of the Treasurer's investments in a single issuer. As the following table depicts, the State Treasurer's Investment Policy places limits on the total dollar amount that may be invested in each investment type as well as a limit on the amount placed with each issuer or counterparty.

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Investments held for longer periods are subject to increased risk of adverse interest rate changes. Investments made by the State Treasurer are covered by the State Treasurer's Investment Policy. This policy dictates that the Treasurer's portfolio will not have an average maturity greater than four (4) years. Investments are made based upon prevailing market conditions at the time of the transaction with the intent to hold the instrument until maturity. In accordance with the Treasurer's Investment Policy, interest rate risk is managed by imposing maturity limitations by investment types.

The State Treasurer's Investment Policy uses diversification as a means to reduce overall portfolio risk. Investments are diversified by security type, institution and maturity. With the exception of obligations fully insured or unconditionally guaranteed as to the payment of principal and interest by the U.S. government, no more than 50% of the State's total funds available for investment will be invested in a single security type or with a single financial

institution. The Treasurer’s portfolio will not have an average maturity greater than four (4) years, unless otherwise designated by the Treasurer. Individual security type limits are shown in the following table. All investments held by the State Treasurer’s office are insured, registered, or held in the name of the State Treasurer of Oklahoma.

The following table outlines the diversification limits to control different types of risk placed on the Treasurer’s portfolio as detailed in the State Treasurer’s Investment Policy:

Investment Type Limitations	Percentage of Total Invested	By Issuer	Maturity Limit	Rating
U.S. Government Agency Securities	50%	35%	10 years	Aaa or AAA
U.S. Government Agency Mortgage Backed Securities – Passthroughs (as a % of U.S. Government Agency)	45%	No Limit	(7)	Aaa or AAA
Collateralized or Insured Certificates of Deposit	Limit of \$35,000,000 per financial institution		365 days (1) (4)	
Negotiable Certificates of Deposit	7.5%	2.5%	180 days (1)	A-1 or P-1
Banker’s Acceptance	7.5%	2.5%	270 days	A-1 & P-1
Commercial Paper	7.5%	2.5%	180 days	A-1 & P-1 (9)
State & Local Government Obligations	10%	5%	30 years	(2) (6)
Repurchase Agreements and Tri-party Repurchase Agreements	30%	10% (per counterparty)	14 days (1) (4)	(3)
Money Market Mutual Funds	30%	10%	1 day (1) (5)	AAAm
Foreign Government Bonds	2.5%	2.5%	5 years (8)	A-/A3 or better

- (1) Excluding weekends and holidays.
- (2) Must possess the highest rating from at least one nationally recognized statistical rating organization.
- (3) Counterparties must have the highest short-term debt rating of A-1 or equivalent by two (2) of the three (3) following nationally recognized statistical rating organizations, Moody’s Investor Service, Standard & Poor’s, and Fitch Ratings.
- (4) Collateralized according to Title 62 O.S. § 72.5.
- (5) Investments made by Money Market Mutual Funds which consist of repurchase agreements are collateralized by obligations of U.S. government and its agencies and instrumentalities.
- (6) Interest rate of variable rate securities must be tied to one of the following indices: LIBOR, Fed Funds, Treasury Bills or Commercial Paper and must reset no less frequently than quarterly.
- (7) Average life not to exceed seven (7) years based on Bloomberg Prepayment Speed using street consensus at the time of purchase.
- (8) Must be listed as an industrialized country by the International Monetary Fund and for which the full faith and credit of such nation has been pledged for the payment of principal and interest.

(9) Commercial Paper cannot exceed 5% of the outstanding paper of an issuing corporation.

Fair Value Measurement

With the implementation of GASB 72 *Fair Value Measurement and Application*, the Treasurer categorizes its fair value measurements, except for investment in nonparticipating interest earning investment contracts (e.g. nonnegotiable certificates of deposit) which are considered cash equivalents, within the fair value hierarchy established by generally accepted accounting principles. Fair value measurement is provided by the custodian for assets they hold using guidelines that recognize a three-tiered fair value hierarchy. The portfolio has the following recurring fair value measurements as of June 30, 2016:

Investments Measured at Fair Value

June 30, 2016 (\$ in millions)

	<u>6/30/2016</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>	<u>*Valued at Cost Not rated by Custodian</u>
TREASURER'S PORTFOLIO					
<u>POOLED INVESTMENTS</u>					
U. S. TREASURY TIPS	89.00		89.00		
U. S. AGENCIES	2,360.74		2,360.74		
MORTGAGED BACKED SECURITIES	2,359.92		2,359.92		
FOREIGN BONDS	50.00		50.00		
MUNICIPAL BONDS	105.20		105.20		
	<u>4,964.86</u>		<u>4,964.86</u>		
<u>NON-POOLED INVESTMENTS</u>					
STATE BOND ISSUES	49.40		9.40		40.00
	<u>49.40</u>		<u>9.40</u>		<u>40.00</u>
TOTAL TREASURER'S INVESTMENTS	<u>5,014.26</u>		<u>4,974.26</u>		<u>40.00</u>
STATE AGENCY PORTFOLIO					
MUTUAL FUNDS	2.15		2.15		
TOTAL STATE AGENCY PORTFOLIO	<u>2.15</u>		<u>2.15</u>		

Level 1 securities are valued using prices quoted in an active market.

Level 2 securities are comprised of observable market based inputs, such as a matrix pricing technique inclusive of an evaluated bid methodology.

Level 3 securities are comprised of unobservable inputs.

*Valued at cost securities are physical securities held by the Treasurer and not priced by the custodian.

Fair value according to GASB 72 focuses particular attention on the price that would be received to sell the asset (exit price) and not the price that would be required to acquire the asset (entry price). The valuation technique used was the "market approach" using prices and other relevant information generated by market transactions involving identical or similar assets, liabilities, or groups of assets and liabilities.

Stated fair value in the financial statements is determined by the custodial relationship existing at June 30, 2016. The custodian's hierarchy level for fixed income is classified as a level 2 assessment due to fair value observable inputs using market based pricing and an evaluated price provided by an independent pricing vendor or broker/dealer. Reporting at the lowest input level when fair value inputs are from more than one level is guidance from GASB 72.

Securities Lending

The Treasurer is authorized by State Statutes to participate in securities lending transactions. The Treasurer has authorized the custodial bank to act as a securities lending agent, lending securities to approved broker-dealers and banks. Through a Securities Lending Agreement, the securities lending agent provides indemnification against borrower default, has written agreements with each borrower, and requires acceptable collateralization of the fair value of the securities loaned. There are no restrictions regarding the amount of securities which may be lent. The maturities of the investments made with cash collateral generally do not match the maturities of the securities loaned. Cash collateral is invested in an investment pool and is included as an asset on the balance sheet with an offsetting liability for the return of the collateral.

During the fiscal year ended June 30, 2016, the securities lending agent lent U.S. Government Securities on behalf of the Treasurer and received cash as collateral in the amount of 102% of the fair value of the securities loaned. All security loans could be terminated on demand by either the Treasurer or the borrower. The maturity on these loans was one day as loans were contracted on an open basis and reset daily. There were no failures by any borrowers to return loaned securities or pay related income distributions during fiscal year 2016. At June 30, 2016, there were no securities on loan and no cash collateral invested due to the transition of investments to a new custodian on July 1, 2016.

Gross securities lending income for the period ending June 30, 2016 was \$211,739. Related bank fees in the amount of \$31,761 resulted in net securities income in the amount of \$179,978.

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Office of the State Treasurer of Oklahoma
 Financial Statement Report
 For the Year Ended June 30, 2016

The following schedule compares the cost or amortized cost to the fair value of investments held in the Fiduciary Funds at June 30, 2016:

TYPE OF INVESTMENT	FAIR VALUE	AMORTIZED COST	AVERAGE WEIGHTED CREDIT QUALITY RATING (1)	AVERAGE MATURITY (DAYS) (2)
TREASURER'S PORTFOLIO				
<u>POOLED INVESTMENTS</u>				
U.S. TREASURY TIPS	\$ 88,975,643	\$ 74,548,250	AA+ (5)	303
SECURITIES LENDING COLLATERAL POOL			NR	
U.S. AGENCIES	2,360,743,425	2,358,924,156	AA+ (5)	365
MORTGAGE BACKED AGENCIES	2,359,919,127	2,302,027,521	AA+ (5)	1,625
FOREIGN BONDS	50,002,290	50,000,000	NR	579
MUNICIPAL BONDS	105,206,762	99,353,070	(6)	1,179
CERTIFICATES OF DEPOSIT	207,051,000	207,051,000	NR	67
	<u>\$ 5,171,898,247</u>	<u>\$ 5,091,903,997</u>		
<u>NON-POOLED INVESTMENTS</u>				
STATE BOND ISSUE	49,400,000	49,400,000	(4)	41
	<u>\$ 49,400,000</u>	<u>\$ 49,400,000</u>		
TOTAL TREASURER'S INVESTMENTS	<u>\$ 5,221,298,247</u>	<u>\$ 5,141,303,997</u>		
STATE AGENCY PORTFOLIO				
MUTUAL FUND	2,152,481	1,108,894	N/A (3)	N/A
TOTAL STATE AGENCY PORTFOLIO	<u>\$ 2,152,481</u>	<u>\$ 1,108,894</u>		

See explanations following chart on next page.

Office of the State Treasurer of Oklahoma
Financial Statement Report
For the Year Ended June 30, 2016

	FAIR VALUE	AMORTIZED COST
INVESTMENTS SUMMARY		
U.S. TREASURY		
NOT ON SECURITIES LOAN	\$ 88,975,643	\$ 74,548,250
ON SECURITIES LOAN - BONDS BORROWED		
ON SECURITIES LOAN -		
U.S. AGENCIES		
NOT ON SECURITIES LOAN	4,720,662,552	4,660,951,677
ON SECURITIES LOAN - BONDS BORROWED		
ON SECURITIES LOAN -		
INVESTMENTS		
PURCHASED W/CASH COLLATERAL		
REPURCHASE AGREEMENTS		
CERTIFICATES OF DEPOSIT	207,051,000	207,051,000
FOREIGN BONDS	50,002,290	50,000,000
STATE BOND ISSUE	49,400,000	49,400,000
MUNICIPAL BONDS	105,206,762	99,353,070
MUTUAL FUND	2,152,481	1,108,894
TOTAL INVESTMENTS	\$ 5,223,450,728	\$ 5,142,412,891

- (1) Ratings are provided where applicable to indicate associated Credit Risk. N/A indicates not applicable.
- (2) Interest Rate Risk is estimated using weighted average days to maturity.
- (3) These agency directed investments are not covered by the State Treasurer's Investment Policy.
- (4) State Bond issues are comprised of \$9,400,000 Oklahoma Student Loan Authority municipal bond with no rating. The interest rate resets quarterly and is tied to the average bond equivalent rates of quotes of the 3-month commercial paper rate. Also included is \$40,000,000 Oklahoma Industrial Finance Authority State of Oklahoma Taxable General Obligation Refunding Bonds. These rates, adjusted quarterly, are tied to the Prime Rate minus 2.9% as published in the Wall Street Journal with a floor of 2.5% and are private placement.
- (5) These securities are implicitly or explicitly guaranteed by the U.S. Government and currently a rating is not provided by the nationally recognized statistical rating organization. GASB rating provided by JPM, Custodian was AA+.
- (6) All Municipal Bonds possessed a AAA rating when purchased. As of June 30, 2016, 13.03% had a rating of AAA, 28.86% were rated AA+, 15.79% were rated A+, 24.28% were rated AA, 7.73% were rated AA-, and 10.31% were not rated.

4. Interfund Accounts

Due from the Fiduciary Fund/ Due to the General Fund

Various charges are applied to individual state agencies for certain banking services rendered by this Office. Additionally, the Office receives reimbursement for certain costs incurred in connection with the recovery, advertisement, custody, and sale of unclaimed property. The Office also receives up to 4% of unclaimed property receipts to offset certain capital and administrative costs incurred in connection with the administration of the State's unclaimed property program. The Office pays the Office of Management and Enterprise Services for payroll, purchasing, accounts payable and information technology services. The balance of unpaid service charges

and unclaimed property revenues at year end are netted against the amount due to other state agencies and reflected as Due from the Fiduciary Fund/Due to the General Fund.

5. Operating Leases

The Office of the State Treasurer has entered into an operating lease agreement for the multi-function printer/scanner/copiers used for the operations of the agency. The lease on this equipment is effective until June 30, 2016 and the payments are based on usage; therefore, future payments are estimated based on historical information and the agency expects the payments to be \$25,000 for the period ended June 30, 2017.

6. Capital Assets

Capital assets accounted for in the government-wide financial statements are recorded at cost net of accumulated depreciation using the straight line method. The following is a summary of the changes in capital assets for the year ended June 30, 2016. Included in Capital Assets are systems under development. These systems will replace COBOL based systems that have reached the end of their product life cycle and are no longer supported by the application software vendors. Certain systems projects, including cash management and certain disbursement processing applications, were put on hold during the year ended June 30, 2016 as resources were redirected to effect changes to statewide payroll systems. The upgrades have been completed and the projects on hold are expected to be reactivated.

	Balance June 30, 2015	Capital Acquisitions	Completed Development	Balance June 30, 2016
Capital assets not being depreciated	\$1,525,515			\$1,525,515
Development in progress				
Capital assets being depreciated	463,435			463,435
Furniture, fixtures, and office equipment				
Less accumulated depreciation	(164,302)	(82,346)		(246,648)
Total	\$1,824,648	(82,346)		\$1,742,302

7. Bank Service Fees

During the year, the Office incurred fees for services rendered by various financial institutions. Service charges of \$278,540 were paid, as reflected in the financial statements; other charges were offset by earnings calculated on the compensating cash balances maintained in various banks. The current interest rate environment where overnight rates were low and the decline in securities lending revenue caused the Treasurer's Office to use earnings credit to offset bank service fees. The total bank fees offset in the current year was approximately \$390,000.

8. Risk Management

The Division of Capital Assets Management of OMES is responsible for the acquisition and

administration of all insurance purchased by the State and for administration of self-insurance plans and programs adopted for use by the State.

The Division of Capital Assets Management is authorized to settle claims of the State and oversee the dispensation and/or settlement of claims against a political subdivision. In no event shall self-insurance coverage provided to the State, an agency or other covered entity exceed the limitations on the maximum dollar amount of liability specified by the Oklahoma Governmental Tort Claims Act. The Division of Capital Assets Management oversees the collection of liability claims owed to the State incurred as the result of a loss through the wrongful or negligent act of a private person or other entity. The Division of Capital Assets Management is also charged with the responsibility to immediately notify the Attorney General of any claims against the State.

9. **Pension Plans**

During 2014, the State Legislature enacted legislation that established a defined contribution system for employees who begin their employment with the Office on or after November 1, 2015 and do not have prior service credit with the Oklahoma Public Employees Retirement System (OPERS). Pursuant to this authority OPERS established Pathfinder, a defined contribution retirement savings program. Participating employees make a mandatory contribution of 4.5% of their annual salary and the Office contributes 6%. Employees may increase their contribution rate to 7.0% of their salary and the Office will contribute 7%. Contributions and any earnings grow tax-deferred until money is withdrawn. Participating employees are immediately vested in their contributions and begin vesting in matching employer contributions at 20% after one year of service increasing by 20% each year until reaching 100% after 5 years of service. In 2016 the Office made all required contributions of \$3,189 to the Pathfinder program. Annual financial reporting for Pathfinder is available from OPERS as reflected below.

Defined Benefit Plan Description. The Office contributes to a cost-sharing, multi-employer public employee retirement plan, which is a defined benefit pension plan that is also administered by the OPERS. OPERS provides retirement, disability, and death benefits to plan members and beneficiaries. Benefit provisions are established and can be amended by the Oklahoma Legislature. Title 74 of the Oklahoma Statutes, Sections 901 through 943, as amended, provides more complete information about the Plan. OPERS issues a publicly available annual financial report that includes financial statements and required supplementary information for OPERS. That report may be obtained by writing to OPERS, P.O. Box 53007, Oklahoma City, Oklahoma 73152 or by calling 1-800-733-9008, or can be obtained at <http://www.opers.ok.gov/>.

Benefits. Permanent employees (employees scheduled for at least 1,000 hours per year at not less than the hourly rate of the monthly minimum wage for state employees) of the Office are eligible to participate in OPERS if they are not eligible for the Pathfinder program described above or if they are participating in another retirement system authorized under Oklahoma law, are not covered by Social Security and not participating in the U.S. Civil Service Retirement System.

OPERS provides members with full retirement benefits at their specified normal retirement age or, for any person who became a member prior to July 1, 1992, when the sum of the member's age and years of credited service equals or exceeds 80 (Rule of 80), and for any person who became a member after June 30, 1992, when the member's age and years of credited service equals or exceeds 90 (Rule of 90).

Normal retirement date is further qualified to require that all members employed on or after

January 1, 1983 must have 6 or more years of full-time equivalent employment with a participating employer before being eligible to receive benefits. Credited service is the sum of participating and prior service. Prior service includes nonparticipating service before January 1, 1975, or the entry date of the employer and active wartime military service.

A member with a minimum of 10 years of participating service may elect early retirement with reduced benefits beginning at age 55 if the participant became a member prior to November 1, 2011, or age 60 if the participant became a member on or after November 1, 2011.

Disability retirement benefits are available for members having 8 years of credited service whose disability status has been certified as being within 1 year of the last day on the job by the Social Security Administration. Disability retirement benefits are determined in the same manner as retirement benefits, but payable immediately without an actuarial reduction.

For state agency employees, benefits are determined at 2% of the average annual salary received during the highest 36 months of the last 10 years of participating service, but not to exceed the applicable annual salary cap, multiplied by the number of years of credited service. Members who join OPERS on or after July 1, 2013, will have their salary averaged over the highest 60 months of the last 10 years. Normal retirement age under the Plan is 62 or Rule of 80/90 if the participant became a member prior to November 1, 2011, or age 65 or Rule of 90 if the participant became a member on or after November 1, 2011.

Members who elect to pay the additional contribution rate, which became available in January 2004, will receive benefits using a 2.5% computation factor for each full year the additional contributions are made. In 2004, legislation was enacted to provide an increased benefit to retiring members who were not yet eligible for Medicare. The Medicare Gap benefit option became available to members under age 65 who retired on or after May 1, 2006. Members may elect to receive a temporary increased benefit to cover the cost of health insurance premiums until the member is eligible to receive Medicare. After the member becomes eligible for Medicare, the retirement benefit will be permanently reduced by an actuarially determined amount. The option is irrevocable, must be chosen prior to retirement, and is structured to have a neutral actuarial cost to the plan.

Members become eligible to vest fully upon termination of employment after attaining 8 years of credited service, or the members' contributions may be withdrawn upon termination of employment.

For elected officials, benefits are determined as the greater of the calculation described above or, based on the official's contribution election, either 1.9% or 4.0% of the highest annual covered compensation received as an elected official, but not to exceed the applicable annual salary cap, multiplied by the number of years of credited service. For members elected prior to November 1, 2011, normal retirement age under the Plan is 60 with 6 years of participation as an elected official or Rule of 80. For members elected on or after November 1, 2011, the normal retirement age is 62 with 10 years of participation as an elected official or 65 with 8 years of participation as an elected official. Members elected prior to November 1, 2011 become eligible to vest fully upon termination of employment after attaining 6 years of participating service as an elected official. Members elected on or after November 1, 2011 become eligible to vest fully upon termination of employment after attaining 8 years of participating service as an elected official. The members' contributions may be withdrawn upon termination of employment.

Upon the death of an active member, the accumulated contributions of the member are paid to the

member's named beneficiary(ies) in a single lump sum payment. If a retired member elected a joint annuitant survivor option or an active member was eligible to retire with either reduced or unreduced benefits or eligible to vest the retirement benefit at the time of death, benefits can be paid in monthly payments over the life of the spouse if the spouse so elects.

Benefits are payable to the surviving spouse of an elected official only if the elected official had at least 6 years of participating elected service and was married at least 3 years immediately preceding death. Survivor benefits are terminated upon death of the named survivor and, for elected officials, remarriage of the surviving spouse. Upon the death of a retired member, with no survivor benefits payable, the member's beneficiary(ies) are paid the excess, if any, of the member's accumulated contributions over the sum of all retirement benefit payments made.

Upon the death of a retired member, OPERS will pay a \$5,000 death benefit to the member's beneficiary or estate of the member if there is no living beneficiary. The death benefit will be paid in addition to any excess employee contributions or survivor benefits due to the beneficiary.

Legislation was enacted in 1999 which provided a limited additional benefit for certain terminated members eligible to vest as of July 1, 1998. This limited benefit is payable as an additional \$200 monthly benefit upon the member's retirement up to the total amount of certain excess contributions paid by the participant to the Plan. In April 2001, limited benefit payments began for qualified retired members.

Contributions. The contribution rates for each member category of OPERS are established by and can be amended by the Oklahoma Legislature and are based on an actuarial calculation which is performed to determine the adequacy of such contribution rates.

Each member participates based on their qualifying gross salary earned, excluding overtime. There is no cap on the qualifying gross salary earned, subject to Internal Revenue Service limitations on compensation.

Members have the option to elect to increase the benefit computation factor for all future service from 2.0% to 2.5%. The election is irrevocable, binding for all future employment under OPERS, and applies only to full years of service. Those who make the election pay the standard contribution rate plus an additional contribution rate, 2.91% which is actuarially determined. The election is available for all state government employees except elected officials and hazardous duty members.

The contribution rates applied to each participating state employee's salary for the fiscal year ended June 30, 2016, are listed below. For officials elected prior to November 1, 2011, the official must select an employee contribution rate of 4.5%, 6.0%, 7.5%, 8.5%, 9.0% or 10%. For officials first elected or appointed after November 1, 2011, the contribution rate is 3.5%

For 2016 state agency employers contributed 16.5% on all salary and state employees contributed 3.5% on all salary. The Office's contributions to the Plan for the years June 30, 2016 - \$351,075; June 30, 2015 - \$397,767; June 30, 2014 - \$358,401; were equal to the established required contributions for each year.

Pension Liabilities, Pension Expense, and Deferred Outflows and Inflows of Resources Related to Pensions. At June 30, 2016, the Office reported a liability for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial

valuation as of July 1, 2015. The Office's proportion of the net pension liability was based on the Office's contributions received by OPERS for all participating employers as of June 30, 2015. Based upon this information, the Office's proportion was 0.1363703%.

At June 30, 2016, accrued payroll expenses include \$8,244 payable to OPERS. For the year ended June 30, 2016, the Office recognized pension expense of \$24,438. At June 30, 2016, the Office reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflow of Resources	Deferred Inflow of Resources
Difference between expected and actual experience	\$ -	54,538
Net difference between projected and actual plan investment earnings	404,943	627,437
Changes in proportionate share	46,908	-
Changes in assumptions	7,631	-
Contributions made since measurement date	351,075	-
	<u>\$ 810,557</u>	<u>681,975</u>

Reported deferred outflows of resources of \$351,075, related to pensions resulting from the Office's contributions subsequent to the measurement date, will be recognized as a decrease of the net pension liability in the year ending June 30, 2017. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

For year ended June 30, 2016		
	Deferred Outflows	Deferred Inflows
2017	\$ 130,161	252,797
2018	124,404	219,491
2019	103,681	209,687
2020	101,236	-
	<u>\$ 459,482</u>	<u>681,975</u>

Actuarial Assumptions. The total pension liability was determined on an actuarial valuation prepared as of July 1, 2015, using the following actuarial assumptions:

Investment return:	7.5% compounded annually net of investment expense and including inflation
Salary increases:	4.5% to 8.4% per year including inflation
Mortality rates:	Active participants and nondisabled pensioners: RP-2000 Mortality Table projected to 2010 by Scale AA (disabled pensioners set forward 15 years).
Annual post-retirement benefit increases:	None
Assumed inflation rate:	3%
Payroll growth:	4% per year
Actuarial cost method:	Entry age

Select period for the termination of employment assumptions:	10 years
Percent of married employees:	85% Males; 85% Females
Spouse age difference:	Males 4 years older than females
Turnover:	Varies from 1% - 22%
Date of last experience study:	May 9, 2014 for the 3 year period from July 1, 2010 to June 30, 2013

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

The target asset allocation and best estimates of geometric real rates of return for each major asset class as of June 30, 2015, are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
U.S. Large Cap Equity	38.0%	5.3%
U.S. Small Cap Equity	6.0%	5.6%
U.S. Fixed Income	25.0%	0.7%
International Stock	18.0%	5.6%
Emerging Market Stock	6.0%	6.4%
TIPS	3.5%	0.7%
Rate Anticipation	<u>3.5%</u>	1.5%
Total	100.0%	

Discount Rate. The discount rate used to measure the total pension liability was 7.5%. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and the employers will be made at the current contribution rate as set out in state statute. Based on those assumptions, OPERS' fiduciary net position was projected through 2114 to be available to make all projected benefit payments of plan members. Therefore, the long-term expected rate of return on plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate. The following presents the net pension liability of the employer calculated using the discount rate of 7.5%, as well as what the Office's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.5%) or 1 percentage point higher (8.5%) than the current rate:

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net pension liability (asset)	\$ 1,827,732	490,501	(646,358)

Detailed information about OPERS' fiduciary net position is available in the separately issued financial report of OPERS which can be located at www.opers.ok.gov.

Legal and Accounting Liability. Attorney General opinions as well as the Oklahoma Supreme Court have implied that the State of Oklahoma is legally responsible for any pension liability over

the employers' set contribution amount. However, GASB Statement 68 requires that the net pension liability be accounted for and reported by the entity that created the liability. Therefore, the Office's portion of the State's net pension liability has been recorded and reported.

10. Other Post Employment Benefits (OPEB)

In addition to the pension benefits described in Note 9, employees of the Office are provided post-retirement health care benefits through their membership in the Oklahoma Public Employees Retirement System (OPERS). OPERS pays the Medicare supplement premium or \$105 per month, whichever is less, for all retirees who elect coverage at time of retirement through the OMES: Employees Group Insurance Division (EGID).

OPERS funds post employment health care benefits as part of the overall retirement requirement. OPEB expenditure and participant information is available for the state as a whole; however, information specific to the Oklahoma State Treasurer is not available or reasonably estimable.

11. Interagency Services Agreement

The Office entered into an agreement with the Office of Management and Enterprise Services (OMES) to obtain all information technology and telecommunication services. The cost of this agreement for fiscal year 2016 was \$653,000.

12. Restatement of Beginning Net Position

The beginning net position of the Office has been restated to effect the implementation of GASB 68 and GASB 71. The cumulative adjustment to the July 1, 2015 beginning net position consists of the following:

Beginning July 1, 2015, net position as	
Previously reported	\$ 10,006,721
Adjustments:	
Record contributions by the Office to	
OPERS as deferred outflows	411,235
Record the Office's proportionate share of the	
net pension liability of OPERS	(235,349)
Record contributions by the Office to	
OPERS as deferred inflows	<u>(864,443)</u>
Net effect of restatement	<u>(688,557)</u>
Beginning net position, as restated	<u>\$ 9,318,164</u>

REQUIRED SUPPLEMENTARY INFORMATION

**OFFICE OF THE STATE TREASURER
SCHEDULE OF RELATED RATIOS
Oklahoma Public Employees Retirement Plan**

	2015	2014
Proportion of the net pension liability	0.13637030%	0.12821044%
Proportional share of the net pension liability	\$ 490,501	235,349
Covered employee payroll	2,233,320	2,206,105
Net pension liability as a percentage of covered payroll	21.96%	10.67%
OPERS fiduciary net position as a percentage of the total pension liability	96.00%	97.90%

* Only the last 2 fiscal years are presented because 10-year data is not readily available.

**OFFICE OF THE STATE TREASURER
SCHEDULE OF CONTRIBUTIONS
Oklahoma Public Employees Retirement Plan**

	2016	2015	2014
Contractually required employer contributions	\$ 351,075	397,767	358,401
Actual employer contributions	351,075	397,767	358,401
Annual contribution deficiency (excess)	<u>\$ -</u>	<u>-</u>	<u>-</u>
Covered employee payroll	\$ 2,074,377	2,233,320	2,206,105
Contributions as a percentage of covered employee payroll	16.92%	17.81%	16.25%

*Only the 3 most recent years are presented because 10-year data is not readily available.

OTHER INFORMATION

**OFFICE OF THE STATE TREASURER
EXPENDITURES BY OBJECT CODE- GENERAL FUND
JUNE 30, 2016**

OBJECT CODE	CATEGORY	AMOUNT
1100	Salary Expense	\$ 2,207,703
1200	Insurance	445,033
1300	FICA & Retirement	524,120
1500	Professional Services	2,919,688
1900	Inter/Intra Agency Payments Professional Services	2,200
2100	Travel-Reimbursement	6,025
2200	Travel-Direct Expenditures	28,708
3100	Miscellaneous Administrative Expense	132,417
3100	Bank Service Charges	278,540
3100	Bank Service Charges Securities Lending	31,761
3200	Rent Expense	23,269
3300	Maintenance and Repair Expense	256,877
3600	Office Expense	9,905
4100	Office Furniture and Equipment	1,902
5200	Employee Recognition Awards	244
6100	Employee Reimbursements	1,073
6200	County Treasurers	95,000
Total		\$ 6,964,465

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL



Oklahoma State Auditor & Inspector

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

**TO THE HONORABLE KEN MILLER
STATE TREASURER OF OKLAHOMA**

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 the *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities and each major fund of the Office of the State Treasurer, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Office of the State Treasurer's basic financial statements, and have issued our report thereon dated January 5, 2017. The report includes an emphasis of matter paragraph stating that the financial statements of the Office of the State Treasurer are intended to present the financial position and results of daily operations of only that portion of the general fund of the State of Oklahoma attributable to the transactions of the Office of the State Treasurer. The report also includes an emphasis of matter paragraph stating that in FY 2016 the Office of the State Treasurer adopted new accounting guidance, GASB Statement No. 68, *Accounting and Financial Reporting for Pensions— An Amendment of GASB Statement No. 27* and GASB Statement No. 71, *Government Pension Transition for Contributions Made Subsequent to the Measurement Date—An Amendment to GASB Statement 68*.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or 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 the 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 Office of the State Treasurer's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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



GARY A. JONES, CPA, CFE
OKLAHOMA STATE AUDITOR AND INSPECTOR

January 5, 2017



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