

# STATE OF NORTH CAROLINA

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA



## NORTH CAROLINA DEPARTMENT OF REVENUE

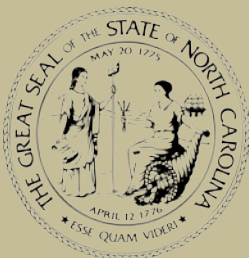
RALEIGH, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

AS OF JUNE 30, 2015 AND 2014 AND

FOR THE FISCAL YEAR ENDED JUNE 30, 2015

A DEPARTMENT OF THE STATE OF NORTH CAROLINA



**NC**  **OSA**  
The Taxpayers' Watchdog

STATE OF NORTH CAROLINA  
**Office of the State Auditor**



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## AUDITOR'S TRANSMITTAL

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The Honorable Pat McCrory, Governor  
The General Assembly of North Carolina  
Secretary Jeffrey M. Epstein  
Department of Revenue

We have completed a financial statement audit of the North Carolina Department of Revenue as of June 30, 2015 and 2014 and for the year ended June 30, 2015, and our audit results are included in this report. You will note from the independent auditor's report that we determined that the financial statements are presented fairly in all material respects.

The results of our tests disclosed no deficiencies in internal control over financial reporting that we consider to be material weaknesses in relation to our audit scope or any instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

*North Carolina General Statutes* require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA  
State Auditor

# AN OVERVIEW OF HOW TO USE THIS REPORT

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This report provides audited financial information on the Department of Revenue (DOR) and is designed to provide the information at a summarized departmental level in the beginning and in more detail further into the report. This report is made up of various components as listed in the Table of Contents. The Department of Revenue reports financial activities in two governmental funds. The governmental funds are used to report all activity of the DOR.

It is important to note that while the financial statements report all the activity of the DOR, most of the activity reported in the general fund is collections and disbursements in support of the State of North Carolina's general fund and is not a part of the budgeted activity of the Department. The distinctions between these activities are reflected in the company number. Company 99 reflects the State's overall general fund and company 45 reflects DOR's budgeted activity.

Where some numbers need further explanation, additional detail is provided in supplementary schedules or "Notes to the Financial Statements" which are referenced next to the line item caption.

**Required Information:** (Information required to be reported by a state agency per Governmental Reporting Standards):

The **Independent Auditor's Report** presents the auditor's opinion on the financial statements, which is that the financial statements, as presented, are materially correct.

The **Management's Discussion and Analysis** presents a discussion of the reasons for significant financial changes between years that is prepared by the agency and has not been audited.

**"A" Exhibits** present the Balance Sheets (for fiscal years ended June 30, 2015 and 2014) and the Statement of Revenues, Expenditures and Changes in Fund Balance (for fiscal year ending June 30, 2015) for the DOR **governmental funds as a whole**.

**Notes to the Financial Statements** are designed to give the reader additional information concerning the DOR and further support the financial statements.

**"B" Exhibit** presents budget-to-actual comparisons for the **General Fund** (for the fiscal year ending June 30, 2015).

**Supplementary Information:**

**"C" Exhibits** present the Balance Sheets and Statement of Revenues, Expenditures, and Changes in Fund Balance **by Company** (for fiscal year ending June 30, 2015, with comparative totals for fiscal year ending June 30, 2014).

**"D" Exhibits** present details of tax revenues collected by DOR (for fiscal years ended June 30, 2015 and 2014).

**"E" Exhibits** present schedule of unpaid taxes by tax type sorted by years outstanding (for fiscal years ended June 30, 2015 and 2014).

“F” Exhibit presents expenditures by purpose or natural classification (agrees to total general fund expenditures on Exhibit A-3).

**Required Information:**

The Independent Auditor’s Report on Internal Control and Compliance – this report is not an opinion on internal control or compliance but rather a report on the matters related to internal control and compliance that were noted as a part of the audit of the financial statements.



Beth A. Wood, CPA  
State Auditor

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Article V, Chapter 147 of the *North Carolina General Statutes*, gives the Auditor broad powers to examine all books, records, files, papers, documents, and financial affairs of every state agency. The Auditor also has the power to summon people to produce records and to answer questions under oath.

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# **INDEPENDENT AUDITOR'S REPORT**

STATE OF NORTH CAROLINA  
**Office of the State Auditor**



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## **INDEPENDENT AUDITOR'S REPORT**

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Secretary Jeffrey M. Epstein  
and Management of the North Carolina Department of Revenue

### Report on the Financial Statements

We have audited the accompanying financial statements of the governmental funds of the North Carolina Department of Revenue (Department) as of June 30, 2015 and 2014, and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the Department's basic financial statements as listed in the table of contents.

### Management's Responsibility for the Financial Statements

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

### Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our 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 Department'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 Department'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 positions of the governmental funds of the North Carolina Department of Revenue, as of June 30, 2015 and 2014, and the respective changes in financial position for the year ended June 30, 2015, in accordance with accounting principles generally accepted in the United States of America.

### Emphasis of Matter

As discussed in Note 1, the financial statements present only the Department of Revenue and are not intended to present fairly the financial position of the State of North Carolina, and the results of its operations in conformity with accounting principles generally accepted in the United States of America.

### Other Matters

#### *Required Supplementary Information*

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

#### *Other Information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Department's basic financial statements for the general and special revenue funds. The accompanying supplementary information, as listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The accompanying supplementary information is the responsibility of management and was derived from and relates 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 accompanying supplementary information, as listed on the table of contents, is fairly stated, in all material respects, in relation to the basic financial statements of governmental funds as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated July 7, 2016 on our consideration of the Department'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 Department's internal control over financial reporting and compliance.



Beth A. Wood, CPA  
State Auditor

Raleigh, North Carolina

July 7, 2016



# **MANAGEMENT'S DISCUSSION AND ANALYSIS**

The Management's Discussion and Analysis section of the North Carolina Department of Revenue's (Department) financial report is provided as an overview of the financial performance of the governmental funds for the fiscal years ended June 30, 2015 and 2014. This discussion and analysis should be read in conjunction with the financial statements and related notes which follow this section.

### **Overview of the Financial Statements**

The Department's financial statements are comprised of governmental funds (General Fund and Special Revenue Fund). The governmental funds' basic financial statements consist of the Balance Sheet and Statement of Revenues, Expenditures, and Changes in Fund Balances.

The Balance Sheet presents the governmental funds' assets and liabilities that are considered relevant to an assessment of near-term liquidity. Differences between assets and liabilities are reported as fund balances.

The Statement of Revenues, Expenditures, and Changes in Fund Balances reports the resource flows (revenues and expenditures) of the governmental funds.

Notes to the financial statements are designed to give the reader additional information concerning the Department and further support the statements noted above.

Required Supplementary Information (RSI) follows the basic financial statements and notes to the financial statements. The RSI is mandated by the GASB and includes General Fund budgetary comparison schedules reconciling the statutory to the generally accepted accounting principles fund balances at fiscal year-end.

Other supplementary information includes the combining financial statements for the Governmental Funds, Statement of Collections, Schedule of Aging of the Taxes Receivable, as well as the Schedule of Operating Expenditures by Purpose.

**Governmental Funds  
Condensed Balance Sheets**

The following condensed balance sheets show the governmental funds' financial positions at June 30, 2015 and 2014.

	2015	2014 (As Restated)	Change
Assets	\$ 2,016,352,497	\$ 1,959,625,807	\$ 56,726,690
Deferred Outflows of Resources	<u>0</u>	<u>0</u>	<u>0</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 2,016,352,497</u>	<u>\$ 1,959,625,807</u>	<u>\$ 56,726,690</u>
Liabilities	\$ 1,597,393,116	\$ 1,728,683,026	\$ (131,289,910)
Deferred Inflows of Resources	<u>72,231,906</u>	<u>59,721,986</u>	<u>12,509,920</u>
Fund Balance			
Nonspendable	1,972,450	2,054,650	(82,200)
Committed	88,600,021	93,137,701	(4,537,680)
Assigned	2,330,252		2,330,252
Unassigned	<u>253,824,752</u>	<u>76,028,444</u>	<u>177,796,308</u>
Total Liabilities, Deferred Inflows, and Fund Balance	<u>\$ 2,016,352,497</u>	<u>\$ 1,959,625,807</u>	<u>\$ 56,726,690</u>

Total assets increased by \$56.7 million during the year due to a \$50.5 million increase in taxes receivable. Taxes receivable increased \$50.5 million from the prior year primarily due to an increase in final assessments billed to taxpayers for individual income tax owed. The increase in final assessments of individual income tax is the result of the Department's write off reversal process.

The Department has procedures in place to write off receivables when they are deemed uncollectible; however, the liability to the Department does not cease to exist. Through the Department's write off reversal process, the collectability of each receivable is automatically re-evaluated each year. When the program identifies a levy source, a receivable that was previously written off is reversed and an attachment or garnishment is issued. This process was performed at the end of the 2015 fiscal year and generated more than \$60 million in write off reversals for individual income tax. There were not any write off reversals in the 2014 fiscal year.

Total liabilities decreased by \$131.3 million compared to the prior year. Tax refunds payable decreased \$215.9 million during the 2015 fiscal year resulting primarily from individual income tax law changes that took effect in tax year 2014.

Effective January 1, 2014, the State individual income tax rates changed from a multi-tiered bracket system with tax rates of 6%, 7%, and 7.75% to a flat rate of 5.8% for all payers of North Carolina individual income tax. In addition, the laws were changed such that individuals can no longer claim personal exemptions on their North Carolina individual

income tax returns, and many tax credits and deductions were repealed or expired. Beginning with the 2014 tax year, the standard deduction allowable amounts increased from \$6,000 to \$15,000 for married couples filing jointly, \$3,000 to \$7,500 for single taxpayers, and from \$4,400 to \$12,000 for heads of household. Additional standard deductions for the aged and blind no longer apply beginning with the 2014 tax year.

These tax law changes required all employees receiving wages in North Carolina to adjust the amounts withheld by their employers based on a new calculation model for wages earned beginning January 1, 2014. The tax law changes allowed for more accurate withholding tables, which will reduce individual tax refunds going forward.

The decrease in tax refunds payable during the 2015 fiscal year is offset by a \$71.4 million increase in unearned revenue. The majority of the unearned revenue account balance consists of corporate income tax overpayments that are estimated to be applied to tax liabilities for future periods instead of being refunded. The estimate of corporate income tax overpayments applied to future taxes increased significantly due to changes in the two factors that are used to determine this amount. First, the January - June 2015 corporate income tax collections from estimated payments and extension payments increased 15.7% from the same period in the prior year. Second, the estimated ratio of applied overpayments to collections increased from 25.4% to 27.5% based on the large increase in the actual ratio for tax year 2012, which was the most current information available at the time.

Deferred inflows of resources increased \$12.5 million compared to prior year due to an increase in unavailable revenue. Unavailable revenue is the amount of taxes receivable that is not expected to be collected within a measurable and available period after fiscal year-end. The majority of the reported unavailable revenues come from franchise taxes, sales and use taxes, tobacco product taxes, and corporate income taxes. These amounts are deferred and recognized as revenues in the period the amounts become available.

Overall fund balance increased by \$175.5 million as of fiscal year end 2015 with the largest increase in unassigned fund balance (\$177.8 million) attributable to the overall current year activity – see further details on the following Statement of Revenues, Expenditures, and Changes in Fund Balances.

**Condensed Statements of Revenues, Expenditures, and Changes in Fund Balances**

The following condensed statements show the governmental funds' resource flows at June 30, 2015 and 2014.

	2015	2014 (As Restated)	Change
Revenues			
Tax Revenues	\$ 21,326,012,680	\$ 19,964,828,916	\$ 1,361,183,764
Fees	2,118,213	1,647,938	470,275
Revenues from Other State Agencies (Note 12)	6,874,573	6,301,731	572,842
Other Revenues	313,252	85,009	228,243
Total Revenues	<u>21,335,318,718</u>	<u>19,972,863,594</u>	<u>1,362,455,124</u>
Expenses:			
Expenses to Other State Agencies (Note 12)	1,548,561	1,724,288	(175,727)
Statutory Tax Distributions	604,370,256	540,784,150	63,586,106
Personal Services	62,646,996	62,513,718	133,278
Employee Benefits	22,872,463	22,455,343	417,120
Other Expenditures	41,300,622	38,936,036	2,364,586
Total Expenditures	<u>732,738,898</u>	<u>666,413,535</u>	<u>66,325,363</u>
Excess of Revenues Over Expenditures	<u>20,602,579,820</u>	<u>19,306,450,059</u>	<u>1,296,129,761</u>
Other Financing Sources (Uses)			
State Appropriation	80,074,647	76,257,110	3,817,537
Sale of Capital Assets	522	662	(140)
Transfers In	537,095	567,937	(30,842)
Transfers Out	(20,507,685,404)	(19,139,860,154)	(1,367,825,250)
Total Other Financing Sources (Uses)	<u>(20,427,073,140)</u>	<u>(19,063,034,445)</u>	<u>(1,364,038,695)</u>
Net Change in Fund Balance	175,506,680	243,415,614	(67,908,934)
Fund Balance - July 1, as Restated (Note 16)	<u>171,220,795</u>	<u>(72,194,819)</u>	<u>243,415,614</u>
Fund Balance - June 30	<u>\$ 346,727,475</u>	<u>\$ 171,220,795</u>	<u>\$ 175,506,680</u>

**Tax Revenues**

Total tax revenues were \$21.3 billion at June 30, 2015, an increase of \$1.4 billion from the prior year. This increase is due to an increase in net sales and use tax revenues of \$759.3 million, a decrease in net franchise tax revenues of \$164.4 million, and a decrease in tax refunds of \$810.5 million.

The increase in net sales and use tax revenues can be attributed to an improved economy and provisions passed by the 2013 Session of the North Carolina General Assembly that broadened the sales and use tax base. The improvements in the economy over the previous year, as evidenced by the growing number of jobs in the State, have increased the disposable incomes of consumers. The U.S. Consumer Sentiment Index reached levels exceeding 90 during the 2015 fiscal year for the first time since 2007, which also tends to be reflected in higher consumer spending.

In addition, the following legislation enacted during the 2013 Session of the General Assembly positively impacted sales & use tax revenues:

1. Effective January 1, 2014, sales and use tax at the full State general rate of 4.75% is levied on the admission charges to an entertainment activity including a live performance or live event of any kind, movie, motion picture or film, or museum, cultural site, garden, exhibit, show or similar attraction or guided tour at a museum, a cultural site, a garden, an exhibit, a show, or a similar attraction.
2. Effective January 1, 2014, sales and use tax at the full State general rate of 4.75% is levied on the sales price of a service contract. A service contract is defined in G.S. 105-164.3(38b) and includes a warranty agreement, a maintenance agreement, a repair contract, or a similar agreement or contract which the obligor agrees to maintain or repair tangible personal property or a motor vehicle.
3. Effective July 1, 2014, prepaid meal plans sold at retail, sourced to this State, and sold or billed on or after July 1, 2014 are subject to the general 4.75% State rate of sales and use tax.
4. Effective July 1, 2014, the combined general sales and use tax rate of 7% is levied on the gross receipts derived from the sales of electricity billed on or after July 1, 2014. These receipts were previously subject to the utility franchise tax which was repealed July 1, 2014.
5. Effective July 1, 2014, the combined general sales and use tax rate of 7% is levied on the sales of piped natural gas sold at retail, sourced to the State, and billed on or after July 1, 2014. These receipts were previously subject to the piped natural gas tax which was repealed July 1, 2014.
6. Effective July 1, 2014, the provision in G.S. 105-164.13C for a sales tax holiday for certain clothing, school supplies, school instructional materials, computers, computer supplies and sports or recreational equipment was repealed. The sales tax holiday for these items occurred annually the first weekend in August. In addition, the provision in G.S. 105-164.13D for a sales tax holiday for certain Energy Star qualified products was repealed. The sales and use tax holiday for Energy Star products occurred annually the first weekend in November. Fiscal year 2014-2015 was the first year these sales tax holidays were repealed.

The decrease in net franchise tax revenues is due to the repeal of G.S. 105-116. This statute imposed a 3.22% tax rate on retailers' gross receipts derived from sales of electricity. This statute was repealed by Session Laws 2013-316, effective July 1, 2014, and applicable to gross receipts billed on or after July 1, 2014. As discussed above, the gross receipts derived from the sales of electricity billed on or after July 1, 2014, are subject to sales and use tax at the 7% combined general rate effective July 1, 2014.

Tax refunds decreased from the prior year by \$810.5 million due to a decline in individual income tax refunds of \$744.1 million. The decline is the result of law changes that impacted individual income tax that took effect in tax year 2014 as explained above.

### **Fees**

Fees increased \$470,000 from the prior year due to an increase in credit card and debit card transaction fees. Tax payments can be made online by bank draft, credit card or debit card. There is a convenience fee to remit payments by credit card or debit card. The incremental



fee is calculated as \$2 for every \$100 of payment. Credit card transactions increased 49.6% from the prior year.

### **Expenditures**

Total expenditures increased \$66.3 million from the prior year due primarily to an increase in statutory tax distributions. As discussed above, as a result of legislation enacted during the 2013 Session of the General Assembly, the amount of tax revenues collected by the Department on the sales of electricity increased. Statute requires that a portion of the net proceeds of the tax collected on sales of electricity be distributed to cities. Therefore, the increase in revenues collected on the sales of electricity increased the amount distributed to local governments.

### **Other Financing Sources (Uses)**

Total other financing uses increased \$1.4 billion from the prior year due to an increase in the year-end transfer of net tax revenues to the Office of the State Controller. This transfer amount increased from \$19.1 billion at the end of fiscal year 2014 to \$20.5 billion at the end of fiscal year 2015. This increase is attributable to the increase in tax revenues as discussed above.

### **Budget Variations**

Data for the budget variances is presented in Exhibit B-1: Schedule of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual (Budgetary Basis – Non-GAAP) of this report.

#### ***VariANCES – Original and Final Budget:***

The final budgeted revenues were \$1.4 million more than the original budget. The final budgeted expenditures decreased less than one percent from the original budget.

The increases in the final budgeted revenues are primarily due to increases in the budgets for the Joint Operations Center (JOC) for National Fuel Tax Compliance grant and an increase in credit card and debit card transaction fees. The JOC grant's original budget was not certified for the past few years and the final budget was determined based on the budget remaining in the grant from the prior fiscal year. The final budgeted revenues for the JOC grant were \$591,000 more than the original budget, which agrees to the balance remaining in the grant at the end of the 2014 fiscal year. The increase in the final budgeted revenues for credit card and debit card transactions fees relates directly to the increase in credit card transactions as discussed above. Actual credit card and debit card transaction fees collected were significantly higher than the original budget of \$674,000. Therefore, the final budget was increased by \$578,000.

#### ***VariANCES – Final Budget and Actual Results:***

Actual total revenue collected was \$489.6 million more than the final budgeted amounts. This result occurred due to greater than anticipated individual income and corporate income collections. As corporate taxable profits accelerated and write-offs on losses from the recession dropped, corporate income tax collections surged more than 20% above forecasted expectations. For individual income taxes, the forecast did not fully anticipate the timing of significant State tax law changes enacted during fiscal year 2013-14, resulting in a surplus in fiscal year 2014-15. Sales and use tax collections, which comprise approximately 30% of total general fund revenue collections, finished on target in fiscal year 2014-15.

Actual total expenditures were \$31.3 million less than budgeted expenditures. Budgeted expenditures were unrealized primarily because \$24.6 million less was spent on contracted services, personal services, and employee benefits than budgeted. Less was spent on contracted services needed for information technology projects during the 2015 fiscal year than budgeted due primarily to changes in architectural approach related to the projects. Variances between the budgeted and actual expenditures for personal services and employee benefits are largely due to vacancies that are paid for from receipt supported funds. Some of these vacancies are attributable to the Guilford Call Center not opening until January 2015.

Actual total other financing sources (uses) was \$458.3 million above budgeted amounts due to transfers out. Transfers out consist solely of the year-end transfer of net revenues to the Office of the State Controller. This increase is attributable to the increase in revenues as discussed above.

## **Future Outlook**

### **General Operations**

The 2015 Session of the N.C. General Assembly enacted Session Law 2015-241 (2015 Appropriations Act), which appropriated \$81.1 million to the Department of Revenue for general operations in fiscal year 2015-16. The Department was also authorized to spend \$6.8 million from the Integrated Tax Administration System (ITAS) replacement fund to fund maintenance costs for the ITAS and Tax Information Management tax systems. Additionally, the Department received \$4.1 million from the ITAS replacement fund for the continued modernization of electronic filing. Authority to use \$10 million of receipts from the Collection Assistance Fee was also given to the Department for the e-Services initiative as well as \$5.9 million to fund salary increases for auditors in the Department.

### **Tax Changes**

Individual income tax changes included allowing federally deductible medical and dental expenses to be deductible on state tax returns as of tax year 2015, increasing the standard deduction by 3.3% as of tax year 2016, and reducing the tax rate from 5.75% to 5.499% as of tax year 2017. Changes to the corporate income tax included repealing the sunset on the revenue "trigger" for reducing the tax rate from 4% to 3% and phasing in sales-only apportionment (the method over which multistate corporations are taxed) over three years. The budget also repealed the state privilege license tax on banks while reducing corporate tax expenditures related to banks and bank holding companies. Other significant changes to the tax code included extending the sales and use tax to include installation, repair, and maintenance of currently taxable tangible property, enacting a modified historic preservation tax credit, and implementing revenue-neutral changes to simplify the corporate franchise tax.



# FINANCIAL STATEMENTS

**Department of Revenue  
Balance Sheet  
Governmental Funds  
As of June 30, 2015**

**Exhibit A-1**

	<u>General Fund</u>	<u>Special Revenue</u>	<u>Total</u>
<b>ASSETS</b>			
Cash and Cash Equivalents (Note 2)	\$ 101,419,139	\$ 2,243,271	\$ 103,662,410
Receivables:			
Accounts Receivable	755,608		755,608
Intergovernmental Receivables (Note 6)	13,681,635	5,453	13,687,088
Taxes Receivable, Net (Note 3)	1,891,381,837	4,451,250	1,895,833,087
Securities Held in Trust (Sureties)	392,600		392,600
Due from Other Funds	49,254		49,254
Inventories	1,972,450		1,972,450
Total Assets	<u>2,009,652,523</u>	<u>6,699,974</u>	<u>2,016,352,497</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>			
Total Deferred Outflows of Resources	<u>0</u>	<u>0</u>	<u>0</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 2,009,652,523</u>	<u>\$ 6,699,974</u>	<u>\$ 2,016,352,497</u>
<b>LIABILITIES</b>			
Accounts Payable and Accrued Liabilities:			
Accounts Payable (Note 5)	\$ 1,901,526	\$ 0	\$ 1,901,526
Accrued Payroll	9,851		9,851
Intergovernmental Payables (Note 6)	131,633,293	927,741	132,561,034
Funds Held for Others	392,450		392,450
Due to NC Housing Finance Agency	82,099,679		82,099,679
Due to Fiduciary Funds	26,986,670		26,986,670
Tax Refunds Payable (Note 3)	965,641,906		965,641,906
Unearned Revenue	387,800,000		387,800,000
Total Liabilities	<u>1,596,465,375</u>	<u>927,741</u>	<u>1,597,393,116</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>			
Unavailable Revenues (Note 7)	<u>68,051,461</u>	<u>4,180,445</u>	<u>72,231,906</u>
<b>FUND BALANCES (Note 10)</b>			
Nonspendable	1,972,450		1,972,450
Committed	87,008,233	1,591,788	88,600,021
Assigned	2,330,252		2,330,252
Unassigned	253,824,752		253,824,752
Total Fund Balances	<u>345,135,687</u>	<u>1,591,788</u>	<u>346,727,475</u>
Total Liabilities, Deferred Inflows, and Fund Balances	<u>\$ 2,009,652,523</u>	<u>\$ 6,699,974</u>	<u>\$ 2,016,352,497</u>

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

**Department of Revenue  
Balance Sheet  
Governmental Funds  
As of June 30, 2014**

**Exhibit A-2**

	<u>General Fund</u>	<u>Special Revenue</u>	<u>Total</u>
<b>ASSETS</b>			
Cash and Cash Equivalents (Note 2)	\$ 98,242,791	\$ 2,451,667	\$ 100,694,458
Receivables:			
Accounts Receivable	772,475		772,475
Intergovernmental Receivables (Note 6)	10,321,484	5,453	10,326,937
Taxes Receivable, Net (Note 3)	1,841,264,615	4,061,686	1,845,326,301
Securities Held in Trust (Sureties)	396,300		396,300
Due from Other Funds	54,686		54,686
Inventories	2,054,650		2,054,650
	<u>\$ 1,953,107,001</u>	<u>\$ 6,518,806</u>	<u>\$ 1,959,625,807</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>			
Total Deferred Outflows of Resources	<u>0</u>	<u>0</u>	<u>0</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 1,953,107,001</u>	<u>\$ 6,518,806</u>	<u>\$ 1,959,625,807</u>
<b>LIABILITIES</b>			
Accounts Payable and Accrued Liabilities:			
Accounts Payable (Note 5)	\$ 1,883,742	\$ 0	\$ 1,883,742
Accrued Payroll	14,957		14,957
Intergovernmental Payables (Note 6)	129,637,016	1,053,425	130,690,441
Funds Held for Others	396,150		396,150
Due to NC Housing Finance Agency	71,618,378		71,618,378
Due to Fiduciary Funds	26,170,130		26,170,130
Tax Refunds Payable (Note 3)	1,181,509,228		1,181,509,228
Unearned Revenue	316,400,000		316,400,000
	<u>1,727,629,601</u>	<u>1,053,425</u>	<u>1,728,683,026</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>			
Unavailable Revenues (Note 7)	<u>55,916,349</u>	<u>3,805,637</u>	<u>59,721,986</u>
<b>FUND BALANCES (Note 10)</b>			
Nonspendable	2,054,650		2,054,650
Committed	91,477,957	1,659,744	93,137,701
Unassigned	76,028,444		76,028,444
	<u>169,561,051</u>	<u>1,659,744</u>	<u>171,220,795</u>
Total Fund Balances	<u>169,561,051</u>	<u>1,659,744</u>	<u>171,220,795</u>
Total Liabilities, Deferred Inflows, and Fund Balances	<u>\$ 1,953,107,001</u>	<u>\$ 6,518,806</u>	<u>\$ 1,959,625,807</u>

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

**Department of Revenue**  
**Statement of Revenues, Expenditures, and Changes in Fund Balances**  
**Governmental Funds**  
**For the Fiscal Year Ended June 30, 2015**  
**(With Comparative Totals for June 30, 2014)**

**Exhibit A-3**

	General Fund	Special Revenue	Total	2014 (Unaudited)
<b>REVENUES</b>				
Tax Revenues	\$ 21,320,118,118	\$ 5,894,562	\$ 21,326,012,680	\$ 19,964,828,916
Revenues from Other State Agencies (Note 12)	6,874,573		6,874,573	6,301,731
Sales and Services	307,128		307,128	73,319
Fees	2,118,213		2,118,213	1,647,938
Miscellaneous	6,124		6,124	11,690
Total Revenues	<u>21,329,424,156</u>	<u>5,894,562</u>	<u>21,335,318,718</u>	<u>19,972,863,594</u>
<b>EXPENDITURES</b>				
Statutory Tax Distributions	600,345,714	4,024,542	604,370,256	540,784,150
Contracted Services	8,673,562		8,673,562	14,863,222
Personal Services	62,646,996		62,646,996	62,513,718
Employee Benefits	22,872,463		22,872,463	22,455,343
Supplies and Materials	1,167,533		1,167,533	1,509,516
Travel	1,401,306		1,401,306	1,308,938
Communication	3,065,551		3,065,551	2,860,269
Utilities	143,026		143,026	132,457
Data Processing Services	4,205,676		4,205,676	4,632,232
Claims and Benefits	70,908		70,908	67,377
Other Services	4,033,094	36,820	4,069,914	3,442,428
Other Fixed Charges	7,216,767		7,216,767	4,462,242
Expenditures to Other State Agencies (Note 12)	184,500	1,364,061	1,548,561	1,724,288
Capital Outlay	7,248,975		7,248,975	2,259,613
Insurance	35,933		35,933	38,445
Other Expenditures	4,001,471		4,001,471	3,359,297
Total Expenditures	<u>727,313,475</u>	<u>5,425,423</u>	<u>732,738,898</u>	<u>666,413,535</u>
Excess of Revenues Over Expenditures	<u>20,602,110,681</u>	<u>469,139</u>	<u>20,602,579,820</u>	<u>19,306,450,059</u>
<b>OTHER FINANCING SOURCES (USES)</b>				
State Appropriations	80,074,647		80,074,647	76,257,110
Sale of Capital Assets	522		522	662
Transfers In (Note 11)	537,095		537,095	567,937
Transfers Out (Note 11)	(20,507,148,309)	(537,095)	(20,507,685,404)	(19,139,860,154)
Total Other Financing Sources (Uses)	<u>(20,426,536,045)</u>	<u>(537,095)</u>	<u>(20,427,073,140)</u>	<u>(19,063,034,445)</u>
Net Change in Fund Balances	175,574,636	(67,956)	175,506,680	243,415,614
Fund Balances - July 1, as Restated (Note 16)	<u>169,561,051</u>	<u>1,659,744</u>	<u>171,220,795</u>	<u>(72,194,819)</u>
Fund Balances - June 30	<u>\$ 345,135,687</u>	<u>\$ 1,591,788</u>	<u>\$ 346,727,475</u>	<u>\$ 171,220,795</u>

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



# **NOTES TO THE FINANCIAL STATEMENTS**

**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES**

- A. Organization** – The North Carolina Department of Revenue (Department) is a part of the State of North Carolina and is not a separate legal or reporting entity. The Department was created to administer, enforce, and collect the taxes due to the State of North Carolina. The Department has approximately 1,500 employees and 11 service centers located through the state for walk-in assistance that offer a variety of services ranging from providing tax forms to answering questions.

The operations of the Department are led by the Secretary of Revenue, a member of the governor's cabinet.

- B. Financial Reporting Entity** – The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America (GAAP), the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. The Department is a part of the State of North Carolina and an integral part of the State's Comprehensive Annual Financial Report.

The accompanying financial statements present all funds belonging to or under the stewardship of the Department. The Department's accounts and transactions are included in the State's *Comprehensive Annual Financial Report* as part of the State's governmental funds.

- C. Basis of Presentation** – The Department's records are maintained on a cash basis throughout the year, but adjustments are made at the end of the fiscal year to convert to GAAP for government entities. The financial statements are prepared according to GAAP as follows:

The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Boards (GASB). GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* requires the presentation of both government-wide and fund level financial statements. The financial statements presented are governmental funds of the Department. Because the Department is not a separate entity, government-wide financial statements are not prepared.

The fund financial statements provide information about the Department's funds. The emphasis of fund financial statements is on each governmental fund.



The Department's financial statements consist of the following governmental funds:

**General Fund** – This is the Department's only major fund and its primary operating fund. The General Fund is made up of two sub-accounts, Company 99 and Company 45. Company 99 is used to record tax collections on behalf of the State while Company 45 is used to record the Department's general operations. The General Fund accounts for all financial resources of the general government, except those required to be accounted for in another fund. The services, which are administered by the Department and accounted for in the General Fund, include the administration, enforcement and collection of taxes due to the State of North Carolina.

**Special Revenue Fund** – Authorized by the legislature (G.S. 105-113.113), this fund accounts for the excise tax imposed on unauthorized substances. Once these proceeds are unencumbered, 75% of the proceeds are distributed to state and local law enforcement agencies involved in the arrest and 25% are distributed to the General Fund of the State of North Carolina. This fund does not receive any appropriation from the General Assembly. The Special Revenue Fund is made up of Company 45 – Special Revenue, which is used to record the general operations of the Special Revenue Fund.

- D. Measurement Focus and Basis of Accounting** – Governmental funds financial statements are prepared using the current financial resources measurement focus and the modified accrual basis of accounting. With this measurement focus, only current assets and liabilities are generally included on the balance sheet. The operating statement presents increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in spendable resources. General capital asset acquisitions are reported as expenditures.

Under the modified accrual basis of accounting, revenues are recognized as soon as they are 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 Department considers revenues to be available if they are collected within 31 days of the end of the current fiscal period (an exception is individual income tax revenues, which the Department considers to be available if they are collected within 12 months after year-end). Expenditures are recorded when a liability is incurred, except for compensated absences, workers' compensation, and claims and judgements, which are recognized as expenditures when payment is due. Pension contributions to cost-sharing plans are recognized as expenditures in the period to which the payment relates, even if payment is not due until the subsequent period.

Since capital asset and long-term liability accounts relating to the governmental funds are reported only at the statewide level, these amounts are not included in the Department's governmental fund

financial statements. However, these amounts are reported in the Notes to the Financial Statements.

Nonexchange transactions, in which the Department receives (or gives) value without directly giving (or receiving) equal value in exchange, including taxes; fines and forfeitures. Revenues are recognized, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, if probable of collection.

The preparation of financial statements, in conformity with GAAP, requires management of the Department to make estimates and judgments that affect the reported amounts of assets, liabilities, and deferred inflows of resources and the disclosures and contingencies at the date of the financial statements and revenues and expenditures recognized during the reporting period. Actual results could differ from those estimates. Should actual results differ from those estimates, changes will flow through the financial statements during the year of change and will be disclosed, if material.

- E. Cash and Cash Equivalents** – This classification includes undeposited receipts and deposits held by the State Treasurer in the Short-Term Investment Fund (STIF). The STIF maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.
- F. Receivables** – Accounts receivable represents amounts owed to the Department that have arisen during the ordinary course of business and are shown at book value with no provision for doubtful accounts considered necessary.

Taxes receivable primarily consists of (1) taxes owed that are expected to be received in approximately 31 days of year-end but have not been billed (with the exception of individual income taxes which is 12 months after year-end); (2) actual taxpayer assessed unpaid taxes less an allowance for uncollectible taxes; and (3) an estimate of under-withholding for individual income taxes for the first half of the calendar year.

Intergovernmental receivables include amounts due from the state and local governments. All amounts are considered collectible and therefore, no allowance for doubtful accounts is recorded.

- G. Inventories** – Inventories, consisting of general supplies and materials, are valued at cost using the first-in, first-out (FIFO) method. Inventories of the governmental fund are recorded as expenditures when consumed rather than when purchased.
- H. Intergovernmental Payables** – Intergovernmental Payables consist primarily of tax distributions due to local governments and law enforcement agencies.

- I. **Unearned Revenue** – Unearned revenue for the governmental fund represents the cumulative excess of cash received for various taxes that is to be applied in a future year.
- J. **Tax Refund Liabilities** – Tax refund liabilities consist primarily of accrued income and sales and use tax refunds due to taxpayers. During the calendar year, the Department collects employee withholdings and taxpayers’ payments for income taxes. At June 30, the Department estimates the amount it owes taxpayers for income tax overpayments during the preceding six months. Sales and use tax refund liabilities are also estimated at June 30. These liabilities are recorded as “tax refunds payable.”
- K. **Long-Term Liabilities** – General long-term liabilities for the governmental funds are not recognized in the governmental fund until they become due. Consequently, general long-term liabilities not yet due are not reported on the face of the financial statements. The noncurrent portion represents amounts that will not be paid within the next fiscal year. The Department’s claims and judgements payable, net pension liability, and compensated absences are the only significant general long-term liabilities of the Department.

**Claims and Judgments Payable** – The North Carolina Supreme Court ruled in *North Carolina School Boards Association v. Moore* that certain specified tax penalties collected from July 1, 1996, to June 30, 2005, must be paid to the State Civil Penalty and Forfeiture Fund for the benefit of public schools, rather than to the State’s General Fund. The court found that the civil penalties collected during this time totaled \$767,814,048, of which \$585,741,703 represented amounts collected by the Department of Revenue. The Supreme Court remanded the case to the superior court for implementation. The superior court issued an order requiring the prospective payments to commence effective July 1, 2005; however, compliance with the superior court’s judgment is currently dependent on legislative action.

**Net Pension Liability** – The net pension liability represents the Department’s proportionate share of the collective net pension liability reported in the State of North Carolina’s 2014 *Comprehensive Annual Financial Report*. This liability represents the Department’s portion of the collective total pension liability less the fiduciary net position of the Teachers’ and State Employees’ Retirement System. See Note 13 for further information regarding the Department’s policies for recognizing liabilities, expenses, and deferred outflows and inflows related to pensions.

**Compensated Absences** – Employees of the Department are permitted to accumulate earned but unused vacation pay benefits. All vacation pay is accrued when incurred in the propriety fund. In the governmental fund, a liability for these amounts is reported only as payments come due each period upon the occurrence of relevant events such as employee resignations and retirements. Consequently, compensated absence

balances are not reported on the face of the governmental fund financial statements, but are reported in the Notes to the Financial Statements. When determining the vacation pay liability due within one year, leave is considered taken on a last in, first out (LIFO) basis. The Department's policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at calendar year end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

In addition to the vacation leave described above, compensated absences include the accumulated unused portion of the special annual leave bonuses awarded by the North Carolina General Assembly. The bonus leave balance on December 31 is retained by employees and transferred into the next calendar year. It is not part of the 30 day maximum applicable to regular vacation leave and is not subject to conversion to sick leave.

There is no liability for unpaid accumulated sick leave because the Department has no obligation to pay sick leave upon employee termination or retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

- L. Fund Balance** – Fund balance for the governmental fund is reported in the following classifications depicting the relative strength of the constraints that control how specific amounts can be spent.

The nonspendable fund balance 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.

Restricted fund balances have constraints placed on the use of resources that are either (a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or (b) imposed by law through constitutional provisions.

Committed fund balances can only be used for specific purposes pursuant to constraints imposed by formal action of the N.C. General Assembly, the state's highest level of decision-making authority. The N.C. General Assembly establishes commitments through the passage of legislation that becomes State law. Commitments may be changed or lifted only by taking the same formal action that imposed the constraint originally. The Department has fund balance committed for the following purposes:

- Project Collect Tax – Collection assistance fee imposed by the General Assembly under General Statute (G.S.) 105-243.1. Fee is

imposed on an overdue tax debt that remains unpaid 30 days or more after the fee notice is mailed to the tax payer. The proceeds of the fee must be deposited into a special account and must be applied to the costs of collecting overdue tax debts. The proceeds of the fee may not be used for any purpose that is not directly and primarily related to collecting overdue tax debts.

- Modernized E-File 1040 – Imposed by the General Assembly under Senate Bill 897. The Department will use the funds for the Internal Revenue Service mandated modernization of the e-File platform.
- Transaction Fees – Imposed by the General Assembly under G.S. 66-58.12. A transaction fee is charged on a tax transaction made via a merchant card. The proceeds derived from the fee may be expended only for e-commerce initiatives and projects.
- Unauthorized Substance Tax – Imposed by General Assembly under G.S. 105.113. Unauthorized substance tax is an excise tax imposed on unauthorized substances and, when proceeds are unencumbered, 75% of the proceeds are distributed to state and local law enforcement agencies involved in the arrest. The remaining 25% of proceeds are distributed to the General Fund.

Assigned fund balances are constrained by an intent to be used for specific purposes, but are neither restricted nor committed. The Office of State Budget and Management (OSBM) is authorized to assign unexpended funds at year-end as a carryforward of budget authority to the subsequent fiscal year. The North Carolina Constitution (Article III, Sec. 5(3)) provides that the "budget as enacted by the General Assembly shall be administered by the Governor." The Governor has delegated the authority to perform certain powers and duties of this role as the Director of the Budget to OSBM.

Unassigned fund balance is the residual classification for the General Fund. Other governmental funds cannot report positive unassigned fund balance but can report negative unassigned fund balance if expenditures incurred for specific purposes exceeded the amounts restricted or committed to those purposes.

Expenditures are considered to be made from the most restrictive resource (i.e., restricted, committed, assigned, and unassigned in that order) when more than one fund balance classification is available for use.

- M. Deferred Inflows of Resources** – An acquisition of net position applicable to a future period(s) that will not be recognized as revenue until that time. The Department has unavailable revenues reported in this category which represent taxes collected before the fiscal year end that do not qualify for recognition as revenue as they are not yet considered to be available.

- N. Revenues and Expenditures from/to Other State Agencies** – Revenues and Expenditures from/to Other State Agencies for the governmental fund represent funds that the Department obtains from or transfers to other agencies, institutions, or entities within the State of North Carolina. These transfers are not considered other financing sources or uses per GAAP, nor are they considered interfund transfers. These revenues and expenditures are eliminated at the statewide reporting level in the State's *Comprehensive Annual Financial Report*.
- O. Statutory Tax Distributions** – Statutory Tax Distributions represent legislatively mandated amounts transferred to local governments or law enforcement agencies for their portion of tax collections for sales and use, white goods, scrap tire, solid waste tax, beverage, and unauthorized substances.

**NOTE 2 - DEPOSITS**

Unless specifically exempt, the Department is required by North Carolina General Statute 147-77 to deposit any funds collected or received that belong to the State of North Carolina with the State Treasurer or with a depository institution in the name of the State Treasurer. General Statute 147-69.1, applicable to the General Fund and General Statute 147-69.2, applicable to the Special Revenue Fund, authorize the State Treasurer to invest all deposits in the following: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; specified repurchase agreements; obligations of the State of North Carolina; certificates of deposit and other deposit accounts of specified financial institutions; prime quality commercial paper; asset-backed securities with specified ratings, specified bills of exchange or time drafts, and corporate bonds/notes with specified ratings; general obligations of other states; general obligations of North Carolina local governments; and obligations of certain entities with specified ratings.

The North Carolina Administrative Code (20 NCAC 7) requires all depositories to collateralize public deposits in excess of federal depository insurance coverage by using one of two methods, dedicated or pooled. Under the dedicated method, a separate escrow account is established by each depository in the name of each local governmental unit and the responsibility of monitoring collateralization rests with the local unit. Under the pooling method, each depository establishes an escrow account in the name of the State Treasurer to secure all of its public deposits. This method shifts the monitoring responsibility from the local unit to the State Treasurer.

Custodial credit risk is the risk that in the event of a bank failure, the Department's deposits may not be returned to it. As of June 30, 2015 and 2014, the Department's bank balance in excess of federal depository insurance coverage was covered under the pooling method.

At June 30, 2015 and 2014, the governmental fund's Balance Sheet reported cash and cash equivalents of \$103,662,410 and \$100,694,458, respectively. These amounts represent the Department's equity position in the State



Treasurer’s Short-Term Investment portfolio (STIF). The STIF (a portfolio within the State Treasurer’s Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission or subject to any other regulatory oversight and does not have a credit rating), had a weighted average maturity of 1.5 years and 1.3 years as of June 30, 2015 and 2014, respectively. Assets and shares of the STIF are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer’s Investment Pool (which includes the State Treasurer’s STIF) are included in the State of North Carolina’s *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller’s Internet home page <http://www.osc.nc.gov/> and clicking on “Reports” or by calling the State Controller’s Financial Reporting Section at (919) 707-0500.

**NOTE 3 - TAXES RECEIVABLE AND TAX REFUNDS PAYABLE**

Taxes Receivable as of June 30, 2015, were as follows:

Tax Receivable as of June 30, 2015 were as follows:

	Gross Receivables	Less Allowance for Uncollectible Taxes	Net Receivables
<b>Taxes Receivable:</b>			
<b>General Fund</b>			
Individual	\$ 340,200,000	\$ 0	\$ 340,200,000
Sales and Use	294,800,000		294,800,000
Corporate	36,400,000		36,400,000
Underwithholding - Individual	624,300,000		624,300,000
Other	130,835,824		130,835,824
<b>Delinquent Receivables:</b>			
Individual	871,477,685	505,576,676	365,901,009
Sales and Use	157,841,533	77,452,286	80,389,247
Corporate	21,595,845	16,688,285	4,907,560
Tobacco Products	12,887,003	10,140,750	2,746,253
Franchise	10,020,873	1,549,665	8,471,208
Estate	9,153,650	8,964,770	188,880
License and Excise	4,092,049	2,501,278	1,590,771
Alcoholic Beverage	897,562	692,792	204,770
Other	833,039	386,724	446,315
<b>Total Taxes Receivable</b>	<u>\$ 2,515,335,063</u>	<u>\$ 623,953,226</u>	<u>\$ 1,891,381,837</u>

Within governmental activities, the significant receivables not expected to be collected within one year in the General Fund were \$626 million of taxes receivable.

See Exhibit E-1 for a Schedule of Aging of the Taxes Receivable (Gross)

	Gross Receivables	Less Allowance for Uncollectible Taxes	Net Receivables
<b>Taxes Receivable:</b>			
<b>Special Revenue Fund</b>			
Unauthorized Substance Tax	\$ 445,124,959	\$ 440,673,709	\$ 4,451,250
<b>Total Taxes Receivable</b>	<u>\$ 445,124,959</u>	<u>\$ 440,673,709</u>	<u>\$ 4,451,250</u>

Taxes Receivable as of June 30, 2014, were as follows:

	Gross Receivables	Less Allowance for Uncollectible Taxes	Net Receivables
<b>Taxes Receivable:</b>			
<b>General Fund</b>			
Individual	\$ 336,500,000	\$ 0	\$ 336,500,000
Sales and Use Tax	305,900,000		305,900,000
Corporate	48,100,000		48,100,000
Underwithholding - Individual	627,500,000		627,500,000
Other	101,732,872		101,732,872
<b>Delinquent Receivables:</b>			
Individual	820,053,652	486,737,633	333,316,019
Sales and Use	154,799,485	77,487,432	77,312,053
Corporate	10,727,261	6,695,263	4,031,998
Tobacco Products	11,669,127	10,877,981	791,146
Franchise	6,389,996	1,875,196	4,514,800
Estate	10,194,620	9,989,132	205,488
License and Excise	3,669,702	2,763,425	906,277
Alcoholic Beverage	650,229	553,991	96,238
Other	935,055	577,331	357,724
<b>Total Taxes Receivable</b>	<u>\$ 2,438,821,999</u>	<u>\$ 597,557,384</u>	<u>\$ 1,841,264,615</u>

Within governmental activities, the significant receivables not expected to be collected within one year in the General Fund were \$606 million of taxes receivable.

See Exhibit E-2 for a Schedule of Aging of the Taxes Receivable (Gross)



	Gross Receivables	Less Allowance for Uncollectible Taxes	Net Receivables
Taxes Receivable:			
Special Revenue Fund			
Unauthorized Substance Tax	\$ 406,168,603	\$ 402,106,917	\$ 4,061,686
Total Taxes Receivable	<u>\$ 406,168,603</u>	<u>\$ 402,106,917</u>	<u>\$ 4,061,686</u>

Tax Refunds Payable as of June 30, 2015 and 2014, were as follows:

	<u>2,015</u>	<u>2014</u>
Tax Refunds Payable:		
Individual	\$ 558,000,000	\$ 734,000,000
Sales and Use Tax	240,700,000	246,300,000
Corporate	160,500,000	190,530,657
Other	6,441,906	10,678,571
Total Tax Refunds Payable	<u>\$ 965,641,906</u>	<u>\$ 1,181,509,228</u>

**NOTE 4 - CAPITAL ASSETS**

Capital assets, which include property, plant, and equipment, are reported as expenditures in governmental funds. Consequently, capital asset balances are not reported on the face of the fund financial statements. Purchased or constructed capital assets are reported at cost or estimated historical cost. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend its useful are not capitalized. Donated capital assets are recorded at their estimated fair value at the date of donation.

Generally, capital assets are defined by the Department as assets with an initial value or cost greater than or equal to \$5,000 and an estimated useful life of two or more years, except for internally generated computer software and other intangible assets, which are capitalized when the value or cost is greater than or equal to \$1 million and \$100 thousand, respectively.

Depreciation, which is recorded at the statewide level, is computed using the straight-line method over the estimated useful lives of the assets, generally 2 to 30 years for machinery and equipment and 2 to 30 years for computer software.

A summary of changes in the Department's capital asset balances is presented as follows:

	July 1, 2014 (As Restated) <sup>1</sup>	Increases	Decreases	Balance June 30, 2015
Capital Assets, Nondepreciable:				
Computer Software in Development <sup>1</sup>	\$ 302,802	\$ 1,114,300	\$ 0	\$ 1,417,102
<b>Total Capital Assets, Nondepreciable</b>	<u>302,802</u>	<u>1,114,300</u>		<u>1,417,102</u>
Capital Assets, Depreciable:				
Equipment	10,495,507	2,489,578	165,657	12,819,428
Computer Software <sup>1</sup>	28,136,986			28,136,986
<b>Total Capital Assets, Depreciable</b>	<u>38,632,493</u>	<u>2,489,578</u>	<u>165,657</u>	<u>40,956,414</u>
Less Accumulated Depreciation for:				
Equipment	3,941,674	526,317	65,174	4,402,817
Computer Software <sup>1</sup>	644,806	1,406,849		2,051,655
<b>Total Accumulated Depreciation</b>	<u>4,586,480</u>	<u>1,933,166</u>	<u>65,174</u>	<u>6,454,472</u>
<b>Total Capital Assets, Depreciable, Net</b>	<u>34,046,013</u>	<u>556,412</u>	<u>100,483</u>	<u>34,501,942</u>
<b>Capital Assets, Net</b>	<u>\$ 34,348,815</u>	<u>\$ 1,670,712</u>	<u>\$ 100,483</u>	<u>\$ 35,919,044</u>

**NOTE 5 - ACCOUNTS PAYABLE**

Accounts payable at June 30, 2015 and 2014, were as follows:

Accounts Payable	2015	2014
Accounts Payable	\$ 1,793,930	\$ 1,791,977
Due to Employees	107,596	91,765
<b>Total Accounts Payable</b>	<u>\$ 1,901,526</u>	<u>\$ 1,883,742</u>

<sup>1</sup>The July 1, 2014 Computer Software in Development was restated by \$54,331,154 because the development of the Tax Information Management System (TIMS project) ceased in January 2014. However, a portion of that project in the amount of \$28,136,986 was in service as of June 30, 2014, and should have been included as computer software, which was also restated.

**NOTE 6 - INTERGOVERNMENTAL RECEIVABLES AND PAYABLES**

Intergovernmental receivables and payables at June 30, 2015, were as follows:

	2015	
	General Fund	Special Revenue
<b>Intergovernmental Receivables</b>		
Local Governments:		
Fines and Forfeitures Overpaid	\$ 0	\$ 5,453
Medicaid Hold Harmless Distribution Returned	3,212,310	
<b>Total from Local Governments</b>	3,212,310	5,453
State Agencies - Payroll Taxes	10,469,325	
<b>Total Intergovernmental Receivables</b>	<u>\$ 13,681,635</u>	<u>\$ 5,453</u>
<b>Intergovernmental Payables</b>		
Local Government Tax Distributions:		
Medicaid Hold Harmless	\$ 1,642,404	\$ 0
Alcoholic Beverage	6,650,477	
Real Estate Conveyance, White Goods Disposal, Scrap Tire Disposal, and Solid Waste Disposal	3,012,366	
Utility Franchise	73,359,721	
Video Program	20,054,958	
Telecom	14,436,677	
Piped Natural Gas	259,372	
Unauthorized Substance		588,925
<b>Total to Local Governments</b>	<u>119,415,975</u>	<u>588,925</u>
Statutory Tax Distribution to the General Fund:		
White Goods Disposal	540,729	
Scrap Tire Disposal	3,344,775	
Solid Waste Disposal	1,588,993	
Unauthorized Substance		338,816
<b>Total to General Fund</b>	<u>5,474,497</u>	<u>338,816</u>
State Agencies:		
Department of Environmental Quality - Solid Waste Taxes	3,932,068	
Department of Information Technology - 911 Service Charges	2,200,623	
Department of Information Technology - Other Payments	590,245	
Department of Administration - Motor Fleet	19,885	
<b>Total to State Agencies</b>	<u>6,742,821</u>	<u>0</u>
<b>Total Intergovernmental Payables</b>	<u>\$ 131,633,293</u>	<u>\$ 927,741</u>

Intergovernmental receivables and payables at June 30, 2014, were as follows:

	2014	
	General Fund	Special Revenue
<b>Intergovernmental Receivables</b>		
Local Governments - Fines and Forfeitures Overpaid	\$ 0	\$ 5,453
State Agencies - Payroll Taxes	10,321,484	
<b>Total Intergovernmental Receivables</b>	<u>\$ 10,321,484</u>	<u>\$ 5,453</u>
<b>Intergovernmental Payables</b>		
Local Government Tax Distributions:		
Medicaid Hold Harmless	\$ 17,260,605	\$ 0
Alcoholic Beverage	10,537,474	
Real Estate Conveyance, White Goods Disposal, Scrap Tire Disposal and Solid Waste Disposal	3,007,339	
Utility Franchise	48,299,502	
Video Program	19,498,157	
Telecom	15,841,455	
Piped Natural Gas	4,245,312	
Unauthorized Substance		680,987
<b>Total to Local Governments</b>	<u>118,689,844</u>	<u>680,987</u>
Statutory Tax Distributions to the General Fund:		
White Goods Disposal	557,363	
Scrap Tire Disposal	2,990,076	
Solid Waste Disposal	1,481,225	
Unauthorized Substance		372,438
<b>Total to General Fund</b>	<u>5,028,664</u>	<u>372,438</u>
State Agencies:		
Department of Environmental Quality - Solid Waste Taxes	3,941,959	
Department of Information Technology - 911 Service Charges	1,444,526	
Department of Information Technology - Other Payments	508,636	
Department of Administration - Motor Fleet	23,387	
<b>Total to State Agencies</b>	<u>5,918,508</u>	<u>0</u>
<b>Total Intergovernmental Payables</b>	<u>\$ 129,637,016</u>	<u>\$ 1,053,425</u>

**NOTE 7 - DEFERRED INFLOWS OF RESOURCES**

The various components of deferred inflows of resources at June 30, 2015 and 2014 are as follows:

	2015			
	Unavailable at June 30, 2014	Current Year Unavailable Increase	Prior Year Unavailable Earned in Current Year	Unavailable at June 30, 2015
<b>General Fund:</b>				
Estate Taxes	\$ 196,901	\$ 188,880	\$ (196,901)	\$ 188,880
Gift Taxes		417		417
License Taxes	863,658	1,554,242	(863,658)	1,554,242
Tobacco Taxes	778,121	2,743,067	(778,121)	2,743,067
Beverage Taxes	61,485	203,333	(61,485)	203,333
Franchise Taxes	3,541,352	8,105,986	(3,541,352)	8,105,986
Sales & Use Taxes	47,531,820	50,319,981	(47,531,820)	50,319,981
Corporate Taxes	2,635,139	4,528,885	(2,635,139)	4,528,885
White Goods Taxes	27,350	356	(27,350)	356
Scrap Tire Taxes	241,569	324,138	(241,569)	324,138
Manufacturing Taxes	37,069	66,017	(37,069)	66,017
Solid Waste Taxes	1,885	16,159	(1,885)	16,159
<b>Total General Fund</b>	<b>\$ 55,916,349</b>	<b>\$ 68,051,461</b>	<b>\$ (55,916,349)</b>	<b>\$ 68,051,461</b>
<b>Special Revenue Fund:</b>				
Unauthorized Substance Taxes	\$ 3,805,637	\$ 4,180,445	\$ (3,805,637)	\$ 4,180,445
<b>Total Special Revenue Fund</b>	<b>\$ 3,805,637</b>	<b>\$ 4,180,445</b>	<b>\$ (3,805,637)</b>	<b>\$ 4,180,445</b>
	2014			
	Unavailable at June 30, 2013	Current Year Unavailable Increase	Prior Year Unavailable Earned in Current Year	Unavailable at June 30, 2014
<b>General Fund:</b>				
Estate Taxes	\$ 3,570,990	\$ 196,901	\$ (3,570,990)	\$ 196,901
Gift Taxes	97,224		(97,224)	
License Taxes	1,326,138	863,658	(1,326,138)	863,658
Tobacco Taxes	5,088,165	778,121	(5,088,165)	778,121
Beverage Taxes	231,971	61,485	(231,971)	61,485
Franchise Taxes	5,417,914	3,541,352	(5,417,914)	3,541,352
Sales & Use Taxes	54,034,951	47,531,820	(54,034,951)	47,531,820
Corporate Taxes	16,477,531	2,635,139	(16,477,531)	2,635,139
White Goods Taxes	2,926	27,350	(2,926)	27,350
Scrap Tire Taxes	274,054	241,569	(274,054)	241,569
Manufacturing Taxes	74,253	37,069	(74,253)	37,069
Solid Waste Taxes	6	1,885	(6)	1,885
<b>Total General Fund</b>	<b>\$ 86,596,123</b>	<b>\$ 55,916,349</b>	<b>\$ (86,596,123)</b>	<b>\$ 55,916,349</b>
<b>Special Revenue Fund:</b>				
Unauthorized Substance Taxes	\$ 3,208,894	\$ 3,805,637	\$ (3,208,894)	\$ 3,805,637
<b>Total Special Revenue Fund</b>	<b>\$ 3,208,894</b>	<b>\$ 3,805,637</b>	<b>\$ (3,208,894)</b>	<b>\$ 3,805,637</b>

**NOTE 8 - LONG-TERM LIABILITIES**

A summary of changes in long-term liabilities is presented as follows:

Governmental Fund - General Fund	Balance July 1, 2014	Additions	Reductions	Balance June 30, 2015	Due Within One Year
Claims and Judgements Payable	\$ 583,340,162	\$ 0	\$ 0	\$ 583,340,162	\$ 0
Compensated Absences	7,182,974	6,830,852	5,467,379	8,546,447	1,137,532
Net Pension Liability <sup>1</sup>	25,923,251		20,947,614	4,975,637	
<b>Total Long-Term Liabilities</b>	<b>\$ 616,446,387</b>	<b>\$ 6,830,852</b>	<b>\$ 26,414,993</b>	<b>\$ 596,862,246</b>	<b>\$ 1,137,532</b>

<sup>1</sup> See Note 13, Retirement Plans, for more information on the net pension liability.

**NOTE 9 - OPERATING LEASE OBLIGATIONS**

The Department entered into operating leases for facilities. Future minimum lease payments under noncancellable operating leases consist of the following at June 30, 2015:

Fiscal Year	General Fund
2016	\$ 2,262,771
2017	1,243,508
2018	1,137,432
2019	1,102,222
2020	1,033,847
2021-2025	1,723,811
<b>Total Minimum Lease Payments:</b>	<b>\$ 8,503,591</b>

Rental expense for all operating leases during the year ended June 30, 2015, was \$2,252,187.

**NOTE 10 - FUND BALANCE**

The details of the fund balance classifications for the governmental funds at June 30, 2015 and 2014, are as follows:

	2015		
	<u>General Fund</u>	<u>Special Revenue</u>	<u>Total</u>
Fund Balance:			
Nonspendable:			
Inventory of Supplies	\$ 1,972,450	\$ 0	\$ 1,972,450
Committed to:			
General Government			
Project Collect Tax	57,664,939		57,664,939
Transaction Fees	3,158,988		3,158,988
Operations and Maintenance for Tax Systems	25,643,964		25,643,964
Other Committed	540,342		540,342
Unauthorized Substance Tax		1,591,788	1,591,788
Assigned to:			
OSBM Carryforward	2,330,252		2,330,252
Unassigned	<u>253,824,752</u>		<u>253,824,752</u>
<b>Total Fund Balance</b>	<u><u>\$ 345,135,687</u></u>	<u><u>\$ 1,591,788</u></u>	<u><u>\$ 346,727,475</u></u>
	2014		
	<u>General Fund</u>	<u>Special Revenue</u>	<u>Total</u>
Fund Balance:			
Nonspendable:			
Inventory of Supplies	\$ 2,054,650	\$ 0	\$ 2,054,650
Committed to:			
General Government			
Project Collect Tax	58,586,098		58,586,098
Transaction Fees	2,517,032		2,517,032
Operations and Maintenance for Tax Systems	29,768,712		29,768,712
Other Committed	606,115		606,115
Unauthorized Substance Tax		1,659,744	1,659,744
Unassigned	<u>76,028,444</u>		<u>76,028,444</u>
<b>Total Fund Balance</b>	<u><u>\$ 169,561,051</u></u>	<u><u>\$ 1,659,744</u></u>	<u><u>\$ 171,220,795</u></u>

**NOTE 11 - INTERFUND TRANSFERS**

Transfers in/out of other funds for the fiscal year ended June 30, 2015 consisted of the following:

	Transfers In			Total
	General Fund	Special	State General Fund	
<u>Transfers Out</u>				
General Fund	\$ 0	\$ 0	\$ 20,507,148,309	\$ 20,507,148,309
Special Revenue	537,095			537,095
Total	<u>\$ 537,095</u>	<u>\$ 0</u>	<u>\$ 20,507,148,309</u>	<u>\$ 20,507,685,404</u>

Transfers are primarily used to (1) transfer revenues and bond proceeds from the funds required by State statute or budget to collect the revenue to the fund required by State statute or budget to expend them, (2) to provide unrestricted revenues collected in the General Fund to finance operating and capital programs accounted for in other funds in accordance with budgetary authorizations, and (3) reflect reversions of State funds from other funds to the General Fund in accordance with Office of State Budget and Management or legislative requirements.

The Department also had intrafund transfers from Company 99 to Company 45 for fiscal years ended June 30, 2015 and 2014, in the amounts of \$34,739,591 and \$44,864,391, respectively, which have been eliminated on the governmental funds financial statements. These General Fund transfers primarily consist of a 20 percent collection assistance fee authorized by G.S. §105.243.1, which the Department uses to offset the costs of collecting and reducing the incidence of overdue tax debts.



**NOTE 12 - REVENUES AND EXPENDITURES FROM/TO OTHER STATE AGENCIES**

The governmental funds' Revenues and Expenditures from/to Other State Agencies by entity and purpose at June 30, 2015, are as follows:

General Fund:	Purpose	Amount
Revenues from Other State Agencies:		
Department of Transportation	Motor Fuels Reimbursement	\$ 3,843,056
Department of Transportation	Fuel Tax Compliance Reimbursement	1,191,127
Department of Transportation	International Regulations Reimbursement	61,866
Department of Transportation	Motor Tax Project Reimbursement	1,411,480
Department of Insurance	Insurance Reimbursement	170,358
Department of Agriculture and Consumer Services	Forestry Reimbursement	101,761
Department of Transportation	20% Fee for Motor Fuels	79,141
Department of Commerce	Job Development Investment Grants	15,784
<b>Total Revenues from Other State Agencies</b>		<b>\$ 6,874,573</b>
	<b>Purpose</b>	<b>Amount</b>
Expenditures to Other State Agencies:		
Office of the State Controller	William S. Lee Fees	\$ 184,500
<b>Total Expenditures to Other State Agencies</b>		<b>\$ 184,500</b>
	<b>Purpose</b>	<b>Amount</b>
Special Revenue Fund:		
Expenditures to Other State Agencies:		
Office of the State Controller	25% Transfer to General Fund	\$ 1,342,893
Office of State Budget and Management	Penalties to OSBM	21,168
<b>Total Expenditures to Other State Agencies</b>		<b>\$ 1,364,061</b>

**NOTE 13 - PENSION PLANS**

**Defined Benefit Plan**

*Plan Administration:* The State of North Carolina administers the Teachers' and State Employees' Retirement System (TSERS) plan. This plan is a cost-sharing, multiple-employer, defined benefit pension plan established by the State to provide pension benefits for general employees and law enforcement officers (LEOs) of the State, general employees and LEOs of its component units, and employees of Local Education Agencies (LEAs) and charter schools not in the reporting entity. Membership is comprised of employees of the State (state agencies and institutions), universities, community colleges, and certain proprietary component units along with the LEAs and charter schools. Benefit provisions are established by General Statute 135-5 and may be amended only by the North Carolina General Assembly.

*Benefits Provided:* TSERS provides retirement and survivor benefits. Retirement benefits are determined as 1.82% of the member's average final compensation times the member's years of creditable service. A member's

average final compensation is calculated as the average of a member's four highest consecutive years of compensation. General employee plan members are eligible to retire with full retirement benefits at age 65 with five years of creditable service, at age 60 with 25 years of creditable service, or at any age with 30 years of creditable service. General employee plan members are eligible to retire with partial retirement benefits at age 50 with 20 years of creditable service or at age 60 with five years of creditable service. Survivor benefits are available to eligible beneficiaries of general members who die while in active service or within 180 days of their last day of service and who also have either completed 20 years of creditable service regardless of age, or have completed five years of service and have reached age 60. Eligible beneficiaries may elect to receive a monthly Survivor's Alternate Benefit for life or a return of the member's contributions. The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains of the plan.

*Contributions:* Contribution provisions are established by General Statute 135-8 and may be amended only by the North Carolina General Assembly. Employees are required to contribute 6% of their compensation. The contribution rate for employers is set each year by the NC General Assembly in the Appropriations Act based on the actuarially-determined rate recommended by the actuary. The Department's contractually-required contribution rate for the year ended June 30, 2015 was 9.15% of covered payroll. The Department's contributions to the pension plan were \$5,761,005, and employee contributions were \$3,777,708 for the year ended June 30, 2015.

The TSERS Plan's financial information, including all information about the plan's assets, deferred outflows of resources, liabilities, deferred inflows of resources, and fiduciary net position, is included in the State of North Carolina's fiscal year 2014 *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Reports" or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

*TSERS Basis of Accounting:* The financial statements of the TSERS plan were prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has a legal requirement to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan. The plan's fiduciary net position was determined on the same basis used by the pension plan.

*Methods Used to Value TSERS Investment:* Pursuant to *North Carolina General Statutes*, the State Treasurer is the custodian and administrator of the retirement systems. The State Treasurer maintains various investment portfolios in its Investment Pool. The pension trust funds are the primary participants in the Long-Term Investment portfolio and the sole participants in the External Fixed Income Investment, Equity Investment, Real Estate

Investment, Alternative Investment, Credit Investment, and Inflation Protection Investment portfolios. The investment balance of each pension trust fund represents its share of the fair market value of the net position of the various portfolios within the pool. Detailed descriptions of the methods and significant assumptions regarding investments of the State Treasurer are provided in the 2014 *Comprehensive Annual Financial Report*.

*Net Pension Liability:* At June 30, 2015, the Department reported a liability of \$4,975,637 for its proportionate share of the collective net pension liability. The net pension liability was measured as of June 30, 2014. The total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of December 31, 2013, and update procedures were used to roll forward the total pension liability to June 30, 2014. The Department's proportion of the net pension liability was based on the present value of future salaries for the Departments relative to the present value of future salaries for all participating employers, actuarially-determined. As of June 30, 2014, the Department's proportion was .42439%, which was a decrease of .00261% from its proportion measured as of June 30, 2013.

*Actuarial Assumptions:* The following table presents the actuarial assumptions used to determine the total pension liability for the TSERS plan at the actuarial valuation date:

Valuation Date	12/31/2013
Inflation	3%
Salary Increases*	4.25% - 9.10%
Investment Rate of Return**	7.25%

\* Salary increases include 3.5% inflation and productivity factor.

\*\* Investment rate of return is net of pension plan investment expense, including inflation.

TSERS currently uses mortality tables that vary by age, gender, employee group (i.e. teacher, general, law enforcement officer) and health status (i.e. disabled and healthy). The current mortality rates are based on published tables and based on studies that cover significant portions of the U.S. population. The healthy mortality rates also contain a provision to reflect future mortality improvements.

The actuarial assumptions used in the December 31, 2013 valuations were based on the results of an actuarial experience study for the period January 1, 2005 through December 31, 2009.

Future ad hoc Cost of Living Adjustment (COLA) amounts are not considered to be substantively automatic and are therefore not included in the measurement.

The projected long-term investment returns and inflation assumptions are developed through review of current and historical capital markets data, sell-side investment research, consultant whitepapers, and historical performance of investment strategies. Fixed income return projections reflect current yields

across the U.S. Treasury yield curve and market expectations of forward yields projected and interpolated for multiple tenors and over multiple year horizons. Global public equity return projections are established through analysis of the equity risk premium and the fixed income return projections. Other asset categories and strategies' return projections reflect the foregoing and historical data analysis. These projections 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 pension plan's target asset allocation as of June 30, 2014 (the valuation date) are summarized in the following table:

<u>Asset Class</u>	<u>Long-Term Expected Real Rate of Return</u>
Fixed Income	2.5%
Global Equity	6.1%
Real Estate	5.7%
Alternatives	10.5%
Credit	6.8%
Inflation Protection	3.7%

The information above is based on 30-year expectations developed with the consulting actuary for the 2013 asset, liability and investment policy study for the North Carolina Retirement Systems. The long-term nominal rates of return underlying the real rates of return are arithmetic annualized figures. The real rates of return are calculated from nominal rates by multiplicatively subtracting a long-term inflation assumption of 3.19%. All rates of return and inflation are annualized.

*Discount Rate:* The discount rate used to measure the total pension liability was 7.25%. The projection of cash flows used to determine the discount rate assumed that contributions from plan members will be made at the current contribution rate and that contributions from employers will be made at statutorily required rates, actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of the current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

*Sensitivity of the Net Pension Liability to Changes in the Discount Rate:* The following presents the net pension liability of the plan calculated using the discount rate of 7.25%, as well as what the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (6.25%) or 1-percentage point higher (8.25%) than the current rate:

<u>Net Pension Liability (Asset)</u>		
<u>1% Decrease (6.25%)</u>	<u>Current Discount Rate (7.25%)</u>	<u>1% Increase (8.25%)</u>
\$35,718,576	\$4,975,637	(\$20,982,296)

*Deferred Inflows of Resources and Deferred Outflows of Resources Related to Pensions:* For the year ended June 30, 2015, the Department recognized pension expense of \$2,179,555. At June 30, 2015, the Department reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

Employer Balance of Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions by Classification:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Difference Between Actual and Expected Experience	\$ 0	\$ 1,159,794
Changes of Assumptions		
Net Difference Between Projected and Actual Earnings on Pension Plan Investments		16,810,680
Change in Proportion and Differences Between Agency's Contributions and Proportionate Share of Contributions	188,468	
Contributions Subsequent to the Measurement Date	<u>5,761,005</u>	
Total Deferred Inflows and Outflows of Resources Related to Pensions	<u>\$ 5,949,473</u>	<u>\$ 17,970,474</u>

\$5,761,005 reported as deferred outflows of resources related to pensions will be included as a reduction of the net pension liability in the fiscal year ended June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Schedule of the Net Amount of the Employer's Balance of Deferred Outflows of Resources and Deferred Inflows of Resources that will be Recognized in Pension Expense:

	<u>Amount</u>
Year ended June 30:	
2016	\$ (4,459,004)
2017	(4,459,004)
2018	(4,459,004)
2019	<u>(4,405,174)</u>
Total	<u>\$ (17,782,186)</u>

**NOTE 14 - OTHER POSTEMPLOYMENT BENEFITS**

- A. Health Benefits** - The Department participates in the Comprehensive Major Medical Plan (the Plan), a cost-sharing, multiple-employer defined benefit health care plan that provides postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System (TSERS). Coverage eligibility varies depending on years of contributory membership service in their retirement system prior to disability or retirement.

The Plan's benefit and contribution provisions are established by Chapter 135, Article 3B, of the General Statutes, and may be amended only by the North Carolina General Assembly. The Plan does not provide for automatic post-retirement benefit increases.

By General Statute, a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those contributions shall be used to provide health benefits to retired and disabled employees and applicable beneficiaries. By statute, the Fund is administered by the Board of Trustees of TSERS and contributions to the Fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are established by the General Assembly.

For the current fiscal year the Department contributed 5.49% of the covered payroll under TSERS to the Fund. Required contribution rates for the years ended June 30, 2014, and 2013, were 5.40% and 5.30%, respectively. The Department made 100% of its annual required contributions to the Plan for the years ended June 30, 2015, 2014, and 2013, which were \$3,456,603, \$3,349,517, and \$3,310,907, respectively. The Department assumes no liability for retiree health care benefits provided by the programs other than its required contribution.

Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Reports" or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

- B. Disability Income** - The Department participates in the Disability Income Plan of North Carolina (DIPNC), a cost-sharing, multiple-employer defined benefit plan, to provide short-term and long-term disability benefits to eligible members of TSERS. Benefit and contribution provisions are established by Chapter 135, Article 6, of the General

Statutes, and may be amended only by the North Carolina General Assembly. The Plan does not provide for automatic post-retirement benefit increases.

Disability income benefits are funded by actuarially determined employer contributions that are established by the General Assembly. For the fiscal year ended June 30, 2015, the Department made a statutory contribution of .41% of covered payroll under TSERS to the DIPNC. Required contribution rates for the years ended June 30, 2014, and 2013, was .44% in both years. The Department made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2015, 2014, and 2013, which were \$258,143, \$272,924, and \$274,868, respectively. The Department assumes no liability for long-term disability benefits under the Plan other than its contribution.

Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

**NOTE 15 - RISK MANAGEMENT**

The Department is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These exposures to loss are handled via a combination of methods, including participation in state-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

**A. Employee Benefit Plans**

**1. State Health Plan**

Department employees and retirees are provided comprehensive major medical care benefits. Coverage is funded by contributions to the State Health Plan (Plan), a discretely presented component unit of the State of North Carolina. The Plan has contracted with third parties to process claims.

**2. Death Benefit Plan of North Carolina**

Term life insurance (death benefits) of \$25,000 to \$50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. The employer contribution rate was .16% for the current fiscal year.



## **B. Other Risk Management and Insurance Activities**

### **1. Automobile, Fire, and Other Property Losses**

The Department is required to maintain fire and lightning coverage on all state-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to the Department for operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a \$5,000 per occurrence deductible. However, some agencies have chosen a higher deductible for a reduction in premium.

All state-owned vehicles are covered by liability insurance through a private insurance company and handled by the North Carolina Department of Insurance. The liability limits for losses are \$1,000,000 per claim and \$10,000,000 per occurrence. The Department pays premiums to the North Carolina Department of Insurance for the coverage.

### **2. Public Officers' and Employees' Liability Insurance**

The risk of tort claims of up to \$1,000,000 per claimant is retained under the authority of the State Tort Claims Act. In addition, the State provides excess public officers' and employees' liability insurance up to \$10,000,000 via contract with a private insurance company. The Department pays the premium, based on a composite rate, directly to the private insurer.

### **3. Employee Dishonesty and Computer Fraud**

The Department is protected for losses from employee dishonesty and computer fraud. This coverage is with a private insurance company and is handled by the North Carolina Department of Insurance. The Department is charged a premium by the private insurance company. Coverage limit is \$5,000,000 per occurrence. The private insurance company pays 90% of each loss less a \$75,000 deductible.

### **4. Statewide Workers' Compensation Program**

The North Carolina Workers' Compensation Program provides benefits to workers injured on the job. All employees of the State and its component units are included in the program. When an employee is injured, the Department's primary responsibility is to arrange for and provide the necessary treatment for work related injury. The Department is responsible for paying medical benefits and compensation in accordance with the North Carolina Workers' Compensation Act. The Department retains the risk for workers' compensation.



Additional details on the state-administered risk management programs are disclosed in the State's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

**NOTE 16 - FUND BALANCE RESTATEMENTS**

As of July 1, 2014 and 2015, the General Fund's fund balance as previously reported was restated as follows:

	<u>2015</u>	<u>2014<sup>1</sup></u>
Beginning Fund Balance as Previously Reported	\$ 169,560,882	\$ (57,045,398)
Restatements:		
To Correct Prior Year Accrual for Tax Refunds Payable		(16,011,166)
To Correct Prior Year Error in Transfers	169	186
<b>Beginning Fund Balance as Restated</b>	<u><u>\$ 169,561,051</u></u>	<u><u>\$ (73,056,378)</u></u>

As of July 1, 2014 and 2015, the Special Revenue Fund's fund balance as previously reported was restated as follows:

	<u>2015</u>	<u>2014<sup>1</sup></u>
Beginning Fund Balance as Previously Reported	\$ 2,402,604	\$ 2,288,917
Restatements:		
To Correct Prior Year Error in Tax Distributions	(998,909)	(1,427,358)
To Correct Prior Year Error in Tax Revenue	256,049	
<b>Beginning Fund Balance as Restated</b>	<u><u>\$ 1,659,744</u></u>	<u><u>\$ 861,559</u></u>

<sup>1</sup> Previously reported in the State's *Comprehensive Annual Financial Report*



# REQUIRED SUPPLEMENTARY INFORMATION

**North Carolina Department of Revenue  
Schedule of Revenues, Expenditures, and Changes in Fund Balance  
Budget and Actual (Budgetary Basis-Non-GAAP) - General Fund  
For the Fiscal Year Ended June 30, 2015**

**Exhibit B-1**

	Budgeted Amounts		Actual	Favorable (Unfavorable)
	Original	Final		
<b>REVENUES</b>				
Tax Revenues <sup>1</sup>	\$ 19,972,560,000	\$ 19,972,560,000	\$ 20,464,491,374	\$ 491,931,374
Revenues from Other State Agencies	8,976,187	8,976,187	6,870,398	(2,105,789)
Sales and Services	571,925	500,435	307,128	(193,307)
Fee	723,507	1,601,366	2,118,213	516,847
Miscellaneous	750	591,593	6,124	(585,469)
Total Revenues	19,982,832,369	19,984,229,581	20,473,793,237	489,563,656
<b>EXPENDITURES</b>				
Contracted Services	19,466,337	23,882,523	8,430,272	15,452,251
Personal Services	73,840,841	69,623,523	62,548,189	7,075,334
Employee Benefits	26,253,318	25,208,979	23,175,757	2,033,222
Supplies and Materials	788,246	1,173,179	1,033,416	139,763
Travel	1,435,395	1,668,025	1,381,800	286,225
Communication	4,359,863	3,327,875	3,048,867	279,008
Utilities	186,195	184,579	141,255	43,324
Data Processing Services	7,918,460	5,229,118	4,115,609	1,113,509
Claims and Benefits	14,323	70,911	70,908	3
Other Services	4,573,964	4,463,936	4,039,374	424,562
Other Fixed Charges	8,329,016	8,292,413	7,212,278	1,080,135
Expenditures to Other State Agencies		299,500	184,500	115,000
Capital Outlay	7,498,989	9,917,694	6,918,732	2,998,962
Insurance	42,889	41,971	35,933	6,038
Other Expenditures	3,742,682	4,262,094	4,047,233	214,861
Total Expenditures	158,450,518	157,646,320	126,384,123	31,262,197
Excess of Revenues Over Expenditures	19,824,381,851	19,826,583,261	20,347,409,114	520,825,853
<b>OTHER FINANCING SOURCES (USES)</b>				
State Appropriations	80,398,150	80,398,150	80,074,647	(323,503)
Sale of Capital Assets	1,000	1,000	1,000	
Transfers from Other Departments or Funds	1,224,153	1,224,153	1,781,919	557,766
Transfers to the State's General Fund <sup>1</sup>	(19,972,560,000)	(19,972,560,000)	(20,431,128,234)	(458,568,234)
Total Other Financing Sources (Uses)	(19,890,936,697)	(19,890,936,697)	(20,349,270,668)	(458,333,971)
Net Change in Fund Balance	(66,554,846)	(64,353,436)	(1,861,554)	62,491,882
Fund Balance July 1, 2014	89,035,503	89,035,503	89,035,503	
Fund Balance June 30, 2015	\$ 22,480,657	\$ 24,682,067	\$ 87,173,949	\$ 62,491,882

The accompanying notes to the required supplementary information are an integral part of this schedule.

<sup>1</sup> The Department of Revenue is required to transfer net tax revenue to the State's general fund. Tax revenues are greater than the transfer to the State's general fund primarily due to the cost for the maintenance of information systems and the 20 percent collection assistance fee which the Department uses to offset the costs of collecting and reducing the incidence of overdue tax debts.

**SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE-BUDGET AND ACTUAL (BUDGETARY BASIS-NON-GAAP) – GENERAL FUND**

**A. BUDGETARY PROCESS**

The State's annual budget is prepared principally on the cash basis. The 1985 General Assembly enacted certain special provisions which state that the budget as certified in the appropriations act is the legal budget for all agencies. These special provisions also state that agencies may spend more than was certified in various line items provided the over-expenditure meets certain criteria and is authorized by the Director of the Budget. The process of approving these over-expenditures results in the authorized budget amounts.

**B. RECONCILIATION OF BUDGET/GAAP REPORTING DIFFERENCES**

*The Schedule of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual (Budgetary Basis – Non-GAAP) – General Funds and Special Revenue, presents comparisons of legally adopted budget with actual data on a budgetary basis. Accounting principles applied to develop data on a budgetary basis differ significantly from those principles used to present financial statements in conformity with generally accepted accounting principles (GAAP). The following describes the major differences between budgetary financial data and GAAP financial data.*

**Basis differences:** Budgetary fund balance is accounted for on the cash basis of accounting while GAAP fund balance is accounted for on the modified accrual basis of accounting. Accrued revenues and expenditures are recognized in the GAAP financial statements.

**Timing differences:** A significant variance between budgetary practices and GAAP is the authorized carry forward of appropriated funds.

	General Fund
Fund Balance (budgetary basis) June 30, 2015	\$ 87,173,949
<u>Reconciling Adjustments:</u>	
<b>Basis Differences:</b>	
<b>Accrued revenues:</b>	
Accounts Receivable	755,608
Intergovernmental Receivable	13,681,635
Due from Other Funds	49,254
Taxes Receivable	1,891,381,837
Other Receivables	
Less:	
Unearned revenue	(387,800,000)
Total Accrued Revenues	<u>1,518,068,334</u>
<b>Accrued expenditures:</b>	
Accounts Payable	(1,901,526)
Tax Refund Payable	(965,641,906)
Accrued Payroll	(9,851)
Intergovernmental Payables	(131,633,293)
Total Accrued Expenditures	<u>(1,099,186,576)</u>
<b>Other adjustments:</b>	
Inventories	1,972,450
Securities Held in Trust (Sureties)	392,600
Due to NC Housing Finance Agency	(82,099,679)
Due to Fiduciary Funds	(26,986,670)
Funds Held for Others	(392,450)
Unavailable Revenue	(68,051,461)
<b>Timing Differences:</b>	
Undeposited Receipts	4,321,784
General Fund Tax Reserves	7,593,154
Authorized Carryforward for Specific Encumbrances	2,330,252
Fund Balance (GAAP basis) June 30, 2015	<u><u>345,135,687</u></u>



# SUPPLEMENTARY INFORMATION

**Department of Revenue  
Balance Sheet  
General Fund - Company 45  
As of June 30, 2015 and 2014**

**Exhibit C-1**

	<b>2015</b>	<b>2014</b>
<b>ASSETS</b>		
Cash and Cash Equivalents and Pooled Cash	\$ 90,216,976	\$ 91,239,160
Accounts Receivable	25,056	24,881
Securities Held in Trust (Sureties)	392,600	396,300
Due from Company 99	2,562,620	2,425,757
Due from Other Funds	49,254	54,686
Inventories	1,972,450	2,054,650
Total Assets	<u>95,218,956</u>	<u>96,195,434</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>		
Total Deferred Outflows of Resources	<u>0</u>	<u>0</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 95,218,956</u>	<u>\$ 96,195,434</u>
<b>LIABILITIES</b>		
Accounts Payable and Accrued Liabilities:		
Accounts Payable	\$ 1,827,748	\$ 1,319,756
Accrued Payroll	9,851	14,957
Intergovernmental Payables	2,810,753	1,976,549
Funds Held for Others	392,450	396,150
Total Liabilities	<u>5,040,802</u>	<u>3,707,412</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Total Deferred Inflows of Resources	<u>0</u>	<u>0</u>
<b>FUND BALANCE</b>		
Nonspendable	1,972,450	2,054,650
Committed	87,008,233	91,477,957
Assigned	2,330,252	
Unassigned	(1,132,781)	(1,044,585)
Total Fund Balance	<u>90,178,154</u>	<u>92,488,022</u>
Total Liabilities, Deferred Inflows, and Fund Balance	<u>\$ 95,218,956</u>	<u>\$ 96,195,434</u>

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

Company 45 General Fund is used to record the Department's general operations.

**Department of Revenue**  
**Statement of Revenues, Expenditures, and Changes in Fund Balance**  
**General Fund - Company 45**  
**For the Fiscal Year Ended June 30, 2015**  
**(With Comparative Totals for June 30, 2014)**

**Exhibit C-2**

	<b>2015</b>	<b>2014 (Unaudited)</b>
<b>REVENUES</b>		
Revenues from Other State Agencies	\$ 6,874,573	\$ 6,301,731
Revenues from Company 99	34,739,591	44,864,391
Sales and Services	307,128	73,319
Fees	2,118,213	1,647,938
Miscellaneous	6,124	1,638
Total Revenues	<u>44,045,629</u>	<u>52,889,017</u>
<b>EXPENDITURES</b>		
Contracted Services	8,673,562	14,863,222
Personal Services	62,646,996	62,513,718
Employee Benefits	22,872,463	22,455,343
Supplies and Materials	1,167,533	1,509,516
Travel	1,401,306	1,308,938
Communication	3,065,551	2,860,269
Utilities	143,026	132,457
Data Processing Services	4,205,676	4,632,232
Claims and Benefits	70,908	67,377
Other Services	4,033,094	3,396,631
Other Fixed Charges	7,216,767	4,462,242
Expenditures to Other State Agencies	184,500	259,000
Capital Outlay	7,248,975	2,259,613
Insurance	35,933	38,445
Other Expenditures	4,001,471	3,359,297
Total Expenditures	<u>126,967,761</u>	<u>124,118,300</u>
Deficit of Revenues Under Expenditures	<u>(82,922,132)</u>	<u>(71,229,283)</u>
<b>OTHER FINANCING SOURCES</b>		
State Appropriations	80,074,647	76,257,110
Sale of Capital Assets	522	662
Transfers In	537,095	567,937
Total Other Financing Sources	<u>80,612,264</u>	<u>76,825,709</u>
Net Change in Fund Balance	(2,309,868)	5,596,426
Fund Balance - July 1, as Restated	<u>92,488,022</u>	<u>86,891,596</u>
Fund Balance - June 30	<u>\$ 90,178,154</u>	<u>\$ 92,488,022</u>

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

Company 45 General Fund is used to record the Department's general operations.



**Department of Revenue  
Balance Sheet  
Special Revenue Fund - Company 45  
As of June 30, 2015 and 2014**

**Exhibit C-3**

	<b>2015</b>	<b>2014</b>
<b>ASSETS</b>		
Cash and Cash Equivalents and Pooled Cash	\$ 2,243,271	\$ 2,451,667
Receivables:		
Intergovernmental Receivables	5,453	5,453
Taxes Receivable, Net	4,451,250	4,061,686
Total Assets	<u>6,699,974</u>	<u>6,518,806</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>		
Total Deferred Outflows of Resources	<u>0</u>	<u>0</u>
Total Assets and Deferred Outflows of Resources	<u><u>\$ 6,699,974</u></u>	<u><u>\$ 6,518,806</u></u>
<b>LIABILITIES</b>		
Intergovernmental Payables	\$ 927,741	\$ 1,053,425
Total Liabilities	<u>927,741</u>	<u>1,053,425</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Unavailable Revenues	<u>4,180,445</u>	<u>3,805,637</u>
<b>FUND BALANCE</b>		
Committed	<u>1,591,788</u>	<u>1,659,744</u>
Total Fund Balance	<u>1,591,788</u>	<u>1,659,744</u>
Total Liabilities, Deferred Inflows, and Fund Balance	<u><u>\$ 6,699,974</u></u>	<u><u>\$ 6,518,806</u></u>

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

Company 45 Special Revenue Fund is used to record the excise taxes imposed on unauthorized substances.

**Department of Revenue**  
**Statement of Revenues, Expenditures, and Changes in Fund Balance**  
**Special Revenue Fund - Company 45**  
**For the Fiscal Year Ended June 30, 2015**  
**(With Comparative Totals for June 30, 2014)**

**Exhibit C-4**

	<b>2015</b>	<b>2014 (Unaudited)</b>
<b>REVENUES</b>		
Tax Revenues	\$ 5,894,562	\$ 7,257,201
Total Revenues	<u>5,894,562</u>	<u>7,257,201</u>
<b>EXPENDITURES</b>		
Other Services	36,820	45,797
Expenditures to Other Agencies	1,364,061	1,465,288
Statutory Tax Distributions	<u>4,024,542</u>	<u>4,385,202</u>
Total Expenditures	<u>5,425,423</u>	<u>5,896,287</u>
Excess of Revenues Over Expenditures	<u>469,139</u>	<u>1,360,914</u>
<b>OTHER FINANCING (USES)</b>		
Transfers Out	<u>(537,095)</u>	<u>(562,729)</u>
Total Other Financing (Uses)	<u>(537,095)</u>	<u>(562,729)</u>
Net Change in Fund Balance	(67,956)	798,185
Fund Balance - July 1, as Restated	<u>1,659,744</u>	<u>861,559</u>
Fund Balance - June 30	<u><u>\$ 1,591,788</u></u>	<u><u>\$ 1,659,744</u></u>

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

Company 45 Special Revenue Fund is used to record the excise taxes imposed on unauthorized substances.

**Department of Revenue  
Balance Sheet  
General Fund - Company 99  
As of June 30, 2015 and 2014**

**Exhibit C-5**

	<b>2015</b>	<b>2014</b>
<b>ASSETS</b>		
Cash and Cash Equivalents	\$ 11,202,163	\$ 7,003,631
Receivables:		
Accounts Receivable	730,552	747,594
Intergovernmental Receivables	13,681,635	10,321,484
Taxes Receivable, Net	1,891,381,837	1,841,264,615
<b>Total Assets</b>	<b>1,916,996,187</b>	<b>1,859,337,324</b>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>		
Total Deferred Outflows of Resources	0	0
<b>Total Assets and Deferred Outflows of Resources</b>	<b>\$ 1,916,996,187</b>	<b>\$ 1,859,337,324</b>
<b>LIABILITIES</b>		
Accounts Payable and Accrued Liabilities:		
Accounts Payable	\$ 73,778	\$ 563,986
Intergovernmental Payables	128,822,540	127,660,467
Due to NC Housing Finance Agency	82,099,679	71,618,378
Due to Fiduciary Funds	26,986,670	26,170,130
Due to Company 45	2,562,620	2,425,757
Tax Refunds Payable	965,641,906	1,181,509,228
Unearned Revenue	387,800,000	316,400,000
<b>Total Liabilities</b>	<b>1,593,987,193</b>	<b>1,726,347,946</b>
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Unavailable Revenues	68,051,461	55,916,349
<b>FUND BALANCE</b>		
Unassigned	254,957,533	77,073,029
<b>Total Fund Balance</b>	<b>254,957,533</b>	<b>77,073,029</b>
<b>Total Liabilities, Deferred Inflows, and Fund Balance</b>	<b>\$ 1,916,996,187</b>	<b>\$ 1,859,337,324</b>

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

Company 99 General Fund is used to record tax collections and distributions on behalf of the state.

**Department of Revenue**  
**Statement of Revenues, Expenditures, and Changes in Fund Balance**  
**General Fund - Company 99**  
**For the Fiscal Year Ended June 30, 2015**  
**(With Comparative Totals for June 30, 2014)**

**Exhibit C-6**

	<b>2015</b>	<b>2014</b> <b>(Unaudited)</b>
<b>REVENUES</b>		
Tax Revenues	\$ 21,320,118,118	\$ 19,957,571,715
Miscellaneous		10,052
Total Revenues	<u>21,320,118,118</u>	<u>19,957,581,767</u>
<b>EXPENDITURES</b>		
Statutory Tax Distributions	600,345,714	536,398,948
Expenditures to Company 45	34,739,591	44,864,391
Total Expenditures	<u>635,085,305</u>	<u>581,263,339</u>
Excess of Revenues Over Expenditures	<u>20,685,032,813</u>	<u>19,376,318,428</u>
<b>OTHER FINANCING (USES)</b>		
Transfers Out	<u>(20,507,148,309)</u>	<u>(19,139,297,425)</u>
Total Other Financing (Uses)	<u>(20,507,148,309)</u>	<u>(19,139,297,425)</u>
Net Change in Fund Balance	177,884,504	237,021,003
Fund Balance - July 1, as restated	<u>77,073,029</u>	<u>(159,947,974)</u>
Fund Balance - June 30	<u>\$ 254,957,533</u>	<u>\$ 77,073,029</u>

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

Company 99 General Fund is used to record tax collections and distributions on behalf of the state.

**Department of Revenue**  
**Statement of Collections (Cash Basis)**  
**General Fund - Company 99 and Special Revenue Fund - Company 45**  
**For the Fiscal Year Ended June 30, 2015**

**Exhibit D-1**

<b>Source of Revenue</b>	<b>Gross Revenue</b>	<b>Refunds</b>	<b>Reserves for Local Government</b>	<b>Other Transfers</b>	<b>Net Revenue</b>
Estate Tax	\$ 3,517,974	\$ 444,128	\$ 0	\$ 84,511	\$ 2,989,335
Privilege License Tax	45,801,820	4,242,634		492,587	41,066,599
Tobacco Products Tax	277,847,392	1,356,265		27,957,032	248,534,095
Franchise Tax	601,361,327	52,237,690		5,001,484	544,122,153
Individual Income Tax	12,302,270,205	1,077,995,161		145,752,612	11,078,522,432
Sales and Use Tax	10,131,781,884	536,890,524	2,732,696,807	610,171,377	6,252,023,176
Alcoholic Beverage Tax	358,563,120	155,951	39,525,134	152,201	318,729,834
Gift Tax	225,734	6,257		7,688	211,789
Freight Car Lines Tax	288,056			163	287,893
Insurance Tax	577,409,045	13,652,813		53,079,938	510,676,294
Piped Natural Gas Tax	6,116,901	6,116,901			
Corporate Income Tax	1,568,418,204	237,987,277		2,742,798	1,327,688,129
Real Estate Conveyance Tax	55,523,630	2,526			55,521,104
White Goods Disposal Tax	4,849,342	213,417	2,388,020	276,318	1,971,587
Scrap Tire Disposal Tax	18,061,718	(145,415)	12,462,677	403,309	5,341,147
Manufacturing Tax	41,609,565	253,891		240,481	41,115,193
Solid Waste Disposal Tax	18,527,842	22,578	6,924,320	9,272,838	2,308,106
Miscellaneous Tax Receipts	19,368				19,368
<b>Total General Fund Revenue</b>	<b>\$ 26,012,193,127</b>	<b>\$ 1,931,432,598</b>	<b>\$ 2,793,996,958</b>	<b>\$ 855,635,337</b>	<b>\$ 20,431,128,234</b>
Special Revenue Fund - Unauthorized Substances Tax	\$ 6,586,783	\$ 162,279	\$ 0	\$ 6,625,900	\$ (201,396)

**Department of Revenue**  
**Statement of Collections (Cash Basis)**  
**General Fund - Company 99 and Special Revenue Fund - Company 45**  
**For the Fiscal Year Ended June 30, 2014**

**Exhibit D-2**

<b>Source of Revenue</b>	<b>Gross Revenue</b>	<b>Refunds</b>	<b>Reserves for Local Government</b>	<b>Other Transfers</b>	<b>Net Revenue</b>
Estate Tax	\$ 28,410,868	\$ 9,073,682	\$ 0	\$ 61,618	\$ 19,275,568
Privilege License Tax	50,922,191	474,875		492,633	49,954,683
Tobacco Products Tax	283,438,549	1,588,119		26,318,110	255,532,320
Franchise Tax	915,894,648	11,791,384		207,090,771	697,012,493
Individual Income Tax	12,417,964,513	1,999,852,222		145,753,463	10,272,358,828
Sales and Use Tax	8,949,231,180	630,895,129	2,470,098,460	281,719,414	5,566,518,177
Alcoholic Beverage Tax	341,658,837	(255,324)	35,723,179	196,087	305,994,895
Gift Tax	648,264	6,794		116,579	524,891
Freight Car Lines Tax	296,230			1,432	294,798
Insurance Tax	543,503,003	34,000,086		68,580,803	440,922,114
Piped Natural Gas Tax	55,703,643	1,531		25,311,963	30,390,149
Corporate Income Tax	1,553,583,145	192,648,649		4,078,290	1,356,856,206
Real Estate Conveyance Tax	45,381,922	48,313			45,333,609
White Goods Disposal Tax	4,499,881	5,860	2,498,440	481,225	1,514,356
Scrap Tire Disposal Tax	17,374,495	201,170	11,774,566	352,516	5,046,243
Manufacturing Tax	37,352,859	1,664,026		166,504	35,522,329
Solid Waste Disposal Tax	17,242,381	5,407	6,450,201	8,641,392	2,145,381
Miscellaneous Tax Receipts	16,046			45	16,001
<b>Total General Fund Revenue</b>	<b>\$ 25,263,122,655</b>	<b>\$ 2,882,001,923</b>	<b>\$ 2,526,544,846</b>	<b>\$ 769,362,845</b>	<b>\$ 19,085,213,041</b>
Special Revenue Fund - Unauthorized Substances Tax	\$ 7,635,231	\$ 152,709	\$ 0	\$ 7,361,672	\$ 120,850

**Department of Revenue  
Schedule of Aging of the Taxes Receivable  
General Fund - Company 99  
For the Fiscal Year Ended June 30, 2015**

**Exhibit E-1**

Tax Type	Delinquent Receivables (in years)				Total
	Less than 1	1 to 5	5 to 10	More than 10	
Individual	\$ 355,839,588	\$ 398,523,529	\$ 102,628,261	\$ 10,211,117	\$ 867,202,495
Corporate	18,669,330	2,404,208	413,157	65,407	21,552,102
Sales & Use	45,469,571	83,949,490	22,819,054	1,187,393	153,425,508
Franchise	7,862,172	1,818,051	443,749	72,022	10,195,994
Scrap Tire	120,799	296,584	21,685	168	439,236
White Goods	306	236	38		580
Manufacturing	168,833	32,025	1,226		202,084
Solid Waste	21,206				21,206
License and Excise	631,867	776,919	123,191	13,849	1,545,826
	<u>\$ 428,783,672</u>	<u>\$ 487,801,042</u>	<u>\$ 126,450,361</u>	<u>\$ 11,549,956</u>	<u>1,054,585,030</u>

**Reconciling Adjustments:**

**Non-Aged Tax Receivable Balances in Enterprise Tax Management (ETM):**

Tobacco Products	\$ 12,887,003	
Estate	9,153,650	
License and Excise	2,551,268	
Alcoholic Beverage	897,562	
Gift	233,084	
<b>Total ETM Receivables Balance</b>		<u>25,722,567</u>

**Other Adjustments:**

Unposted Accrued Interest for June 30, 2015	22,049,991
July Adjustments	(13,558,348)

**Delinquent Receivables (Gross) - General Fund** \$ 1,088,799,239

**Department of Revenue  
Schedule of Aging of the Taxes Receivable  
General Fund - Company 99  
For the Fiscal Year Ended June 30, 2014**

**Exhibit E-2**

Tax Type	Delinquent Receivables (in years)				Total
	Less than 1	1 to 5	5 to 10	More than 10	
Individual	\$ 305,941,757	\$ 425,835,538	\$ 67,758,495	\$ 5,499,111	\$ 805,034,901
Corporate	7,606,120	2,195,187	241,589	735,396	10,778,292
Sales & Use	49,085,165	84,009,413	15,625,171	804,167	149,523,916
Franchise	4,081,556	1,672,754	340,851	171,835	6,266,996
Scrap Tire	109,316	309,819	60,640	297	480,072
White Goods	36,505	1,805			38,310
Manufacturing	109,065	42,449	956		152,470
Solid Waste	3,396				3,396
License and Excise	498,635	580,115	42,798	3,742	1,125,290
	<u>\$ 367,471,515</u>	<u>\$ 514,647,080</u>	<u>\$ 84,070,500</u>	<u>\$ 7,214,548</u>	<u>973,403,643</u>

**Reconciling Adjustments:**

**Non-Aged Tax Receivable Balances in Enterprise Tax Management (ETM):**

Tobacco Products	\$ 11,669,127	
Estate	10,194,621	
License and Excise	2,544,411	
Alcoholic Beverage	650,229	
Gift	250,167	
<b>Total ETM Receivables Balance</b>		<b>25,308,555</b>

**Other Adjustments:**

Unposted Accrued Interest for June 30, 2014	20,600,122
July Adjustments	(223,193)
<b>Delinquent Receivables (Gross) - General Fund</b>	<b><u>\$ 1,019,089,127</u></b>



**North Carolina Department of Revenue  
Schedule of Operating Expenditures by Purpose  
General Fund - Company 99 and Company 45  
For the Fiscal Year Ended June 30, 2015**

**Exhibit F-1  
Page 1 of 2**

	<b>2015</b>	<b>(Unaudited) 2014</b>
<b><u>Expenditures Paid for Department Operations and Administration:</u></b>		
Contracted Services:		
Other Information Technology Services	\$ 3,524,208	\$ 12,441,223
Temporary Agency and Administrative Services	3,290,597	1,061,207
IT Project Management and Analysis Services	164,437	10,563
Legal Services	223,330	175,006
Financial and Audit Services	147,500	135,000
Security Services	556,242	455,150
Janitorial and Waste Services	99,296	95,302
Miscellaneous Contractual Services	667,952	489,771
<b>Total Contracted Services</b>	<b>8,673,562</b>	<b>14,863,222</b>
Personal Services:		
Employee Salaries	60,349,651	59,344,985
Law Enforcement Salaries	1,337,144	1,471,580
Temporary Wages	750,621	1,471,853
Overtime Wages	83,679	86,856
Board Member Compensation	88,400	85,400
Other Salary Expenses	37,501	53,044
<b>Total Salaries and Wages</b>	<b>62,646,996</b>	<b>62,513,718</b>
Employee Benefits:		
Regular Retirement Contributions	9,576,490	9,111,929
Medical Insurance Contributions	6,684,848	6,628,692
Social Security Contributions	4,665,747	4,658,395
Longevity Pay	1,056,211	1,041,140
Employee Educational Expense	495,789	66,243
Unemployment Compensation Payments <sup>1</sup>	20,370	587,827
Workers Compensation Medical Payments	213,445	155,506
Flexible Spending Savings	102,402	99,324
Other Employee Benefits	57,161	106,287
<b>Total Employee Benefits</b>	<b>22,872,463</b>	<b>22,455,343</b>
Supplies and Materials:		
General Office Supplies	670,207	404,411
Data Processing Supplies	335,793	242,056
Other Supplies and Materials	161,533	863,049
<b>Total Supplies and Materials</b>	<b>1,167,533</b>	<b>1,509,516</b>
Travel:		
Ground Transportation	905,866	924,267
Air Transportation	86,027	70,832
Lodging	267,769	196,628
Meals	126,182	97,308
Other Travel	15,462	19,903
<b>Total Travel</b>	<b>1,401,306</b>	<b>1,308,938</b>
Communication:		
Telephone Service	1,744,474	1,610,366
Telecommunication Data Charges	1,034,710	977,100
Cellular Phone Services	248,183	232,634
Other Telephone Charges	38,184	40,169
<b>Total Communication</b>	<b>3,065,551</b>	<b>2,860,269</b>

<sup>1</sup> The 2015 balance is reported net of a \$123,231 prior-year overpayment refund.

**North Carolina Department of Revenue  
Schedule of Operating Expenditures by Purpose  
General Fund - Company 99 and Company 45  
For the Fiscal Year Ended June 30, 2015**

**Exhibit F-1  
Page 2 of 2**

	<b>2015</b>	<b>(Unaudited) 2014</b>
Utilities:		
Energy Services-Electrical	130,838	121,643
Other Utilities	12,188	10,814
Total Utilities	<u>143,026</u>	<u>132,457</u>
Data Processing Services	<u>4,205,676</u>	<u>4,632,232</u>
Claims and Benefits:		
Law Enforcement Separation Allowance	<u>70,908</u>	<u>67,377</u>
Other Services:		
Postage and Delivery	3,333,416	2,699,674
Printing and Binding	474,206	589,188
Other Services	225,472	107,769
Total Other Services	<u>4,033,094</u>	<u>3,396,631</u>
Other Fixed Charges:		
Computer Software Maintenance Agreements	5,894,586	3,110,900
Computer Hardware Maintenance Agreements	379,402	298,574
Duplication Equipment Maintenance Agreements	220,476	220,477
Other Equipment Maintenance Agreements	347,705	279,984
Membership Dues and Subscriptions	299,096	469,093
Other Fixed Charges	75,502	83,214
Total Other Fixed Charges	<u>7,216,767</u>	<u>4,462,242</u>
Expenditures to Other State Agencies (Note 12)	<u>184,500</u>	<u>259,000</u>
Capital Outlay:		
Computer Software	2,311,579	211,271
Computer Hardware	4,114,014	1,144,131
Office Furniture	495,211	171,775
Voice Communication Equipment	115,588	28,106
Office Equipment	68,846	594,217
Duplication Equipment	32,287	34,894
Other Capital Outlays	111,450	75,219
Total Capital Outlay	<u>7,248,975</u>	<u>2,259,613</u>
Insurance and Bonding	<u>35,933</u>	<u>38,445</u>
Other Expenditures:		
Office Building Rent	2,252,187	2,110,417
Office and Communication Equipment Rents and Leases	143,095	148,028
Other Rents and Leases	55,237	57,632
Electronic Payment Processing Fees <sup>2</sup>	1,550,556	1,043,218
Other Operating Expenses	396	2
Total Other Expenditures	<u>4,001,471</u>	<u>3,359,297</u>
Total Expenditures Paid for Department Operations and Administration	<u>126,967,761</u>	<u>124,118,300</u>
<b><u>Expenditures Paid by the Department Pursuant to Statutory Tax Allocations:</u></b>		
Expenditures Paid to Local Governments Pursuant to Statutory Tax Allocations	<u>600,345,714</u>	<u>536,398,948</u>
Total General Fund Expenditures	<u>\$ 727,313,475</u>	<u>\$ 660,517,248</u>

<sup>2</sup> The 2014 balance is reported net of a \$261,124 prior-year overpayment refund.



# **INDEPENDENT AUDITOR'S REPORT**

STATE OF NORTH CAROLINA  
**Office of the State Auditor**



**Beth A. Wood, CPA**  
State Auditor

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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**

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Secretary Jeffery M. Epstein  
and Management of the North Carolina Department of Revenue

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 governmental funds balance sheet of the North Carolina Department of Revenue, a department of the State of North Carolina, as of and for the year ended June 30, 2015 and 2014, and the governmental funds statement of revenues, expenditures, and changes in fund balance for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the Department's basic financial statements, and have issued our report thereon dated July 7, 2016.

As discussed in Note 1, the financial statements present only the Department of Revenue and are not intended to present fairly the financial position of the State of North Carolina, and the results of its operations in conformity with accounting principles generally accepted in the United States of America.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Department'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 Department'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 Department'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 Department's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Beth A. Wood, CPA  
State Auditor

Raleigh, North Carolina

July 7, 2016

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