

**Yellowstone County, Montana**  
**Comprehensive Annual Financial Report - Transmittal Letter (Unaudited)**  
**June 30, 2015**

*Yellowstone County*

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December 22, 2015

**Board of County Commissioners**  
**Citizens of Yellowstone County**  
**Billings, Montana**

The Comprehensive Annual Financial Report of Yellowstone County (the County) for the fiscal year ended June 30, 2015 is submitted herewith. State law requires that counties publish within six months of the close of each fiscal year a complete set of financial statements presented in conformity with accounting principles generally accepted in the United States of America (GAAP), and audited in accordance with generally accepted auditing standards by a firm of licensed certified public accountants. This comprehensive annual financial report meets all required criteria specified by the State, to report the Budgetary, Accounting and Financial Reporting System (BARS), prepared in conformance with the principles and standards for financial reporting as promulgated by the Governmental Accounting Standards Board (GASB). Pursuant to those requirements, the finance department hereby issues the comprehensive annual financial report of Yellowstone County for the fiscal year ended June 30, 2015.

This report consists of management's representations concerning the finances of Yellowstone County. Consequently, management assumes full responsibility for the completeness and reliability of all of the information presented in this report. To provide a reasonable basis for making these representations, management of Yellowstone County has established a comprehensive internal control framework that is designed to protect the government's assets from material loss, theft, or misuse; compile sufficient reliable information for the preparation of Yellowstone County's financial statements in conformity with GAAP; and ensure compliance with laws, regulations, and contracts. Because the cost of internal controls should not outweigh their benefits, Yellowstone County's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement. As management, we assert that, to the best of our knowledge and belief, this financial report is complete and reliable in all material respects.

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Yellowstone County's financial statements have been audited by Anderson, ZurMuehlen & Co., a firm of licensed certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of Yellowstone County for the fiscal year ended June 30, 2015, are free of material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts, and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unmodified opinion that Yellowstone County's financial statements for the fiscal year ended June 30, 2015 are fairly presented in conformity with GAAP. The independent auditor's report is presented as the first component of the financial section of this report.

The independent audit of the financial statements of Yellowstone County has usually been part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. However, for FY15 a Single Audit engagement did not take place, since the County did not meet the threshold for expenditures of Federal government awards of at least \$500,000. GAAP requires that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. Yellowstone County's MD&A can be found immediately following the report of the independent auditors.

**FINANCIAL STATEMENT PRESENTATION**

This Comprehensive Annual Financial Report includes all of the financial statements and reports as required by the Governmental Accounting Standards Board. Designed to meet the needs of a broad spectrum of financial statement readers, this Comprehensive Annual Financial Report is divided into four major sections.

1. **Introductory Section:** As the title indicates, this section introduces the reader to the report and includes the table of contents, transmittal letter, organization chart, and elected officials.
2. **Financial Section:** Includes the following subsections –
  - Independent Auditor's Report
  - Management's Discussion and Analysis (MD&A) – This report is a narrative providing information and analysis about the County's financial position, results of operations for the audited year, and significant changes from the prior year.
  - Basic Financial Statements – These include government-wide financial statements which report on both governmental and business-type activities on a full accrual (business-like) basis.
  - Notes to Basic Financial Statements – Explanatory narratives, details, and reconciliations that are critical to an understanding of the basic financial statements.
  - Required Supplementary Information
  - Fund Financial Statements – These statements provide additional reporting for the major and nonmajor funds.

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3. **Statistical Section:** Although this section contains substantial financial information, these tables differ from financial statements in that they present some nonaccounting data and are designed to reflect social and economic data, as well as the fiscal capacity of the County.

The diverse nature of governmental operations and the necessity of assuring legal compliance preclude recording and summarizing all governmental financial transactions and balances in a single accounting entity. Therefore, from an accounting and financial management viewpoint, a governmental unit is a combination of several distinctly different fiscal and accounting entities, each having a separate set of accounts and functioning independently of each other. Each accounting entity is accounted for in a separate "fund." A fund is defined as a fiscal accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations.

### **PROFILE OF THE COUNTY**

Yellowstone County (population 155,634), created by legislative enactment in 1883, is located in the south central section of Montana and includes the incorporated City of Billings, which is the County seat and most populous city in the state (population 109,059); and also includes the incorporated City of Laurel (population 7,036) and Town of Broadview (population 200). The County imposes tax levies for jurisdictions under the authority of the Board of County Commissioners, which includes county funds and some special districts, such as the Big Sky Economic Development (BSED). The Board of County Commissioners also approves levies requested by boards of special cemetery and fire districts. The County does bill, collect, and distribute property taxes on behalf of other taxing entities such as the State of Montana, schools and cities, but does not approve their levies.

The Board of County Commissioners is a commission form of government with a three member board comprised of officials elected at-large from three different district boundaries to six year terms on a staggered two year cycle. The County has the authority to cause actions that are statutorily permitted under Montana law. The Board of County Commissioners establishes budget authority and policies for County departments.

Budgetary control is maintained through an annual budget adopted by the County Commissioners. Public hearings are published and generally conducted in May or June of each year. The final budget must be adopted by the first Thursday in September or 30 days after receiving the certified taxable values from the State of Montana. Budgetary authority is flexible in that the Commissioners may make transfers among budget object lines within a fund and make budget amendments with statutory restrictions when considered necessary for proper administration of County government. Budget amendments may be passed by the Board of County Commissioners after conducting two published public hearings. The level of budgetary control is established at the fund level. Budget comparisons for the major governmental funds are presented as part of the basic financial statements. These statements also show the original budget that was adopted for the major funds. Generally the revisions made during the fiscal year are related to grant funding and associated expenditures.

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Yellowstone County provides a full range of services as mandated by Montana statutes, including general government, public works, public safety, public health, social and economic, culture and recreation, and community development. Some of the more significant departments and functions within these areas include:

**General Government** – County Commissioners, Treasurer, Finance, Elections, Records, Auditing, Facility Maintenance, Property and Liability Insurance, Planning, Geographical Information, and Clerk of District Court

**Public Safety** – Sheriff's departments including administration, patrol, detectives, civil, records, adult detention, and communications. Other public safety functions include youth detention, county attorney prosecution, disaster and emergency services and traffic safety programs.

**Public Works** – County road and bridge projects and maintenance, weed control, veteran's cemetery, and RSID construction and maintenance.

**Public Health** – Funding support for operations of the public health department (Riverstone Health), mental health treatment and involuntary commitment costs, animal control, and alcohol rehabilitation programs.

**Social and Economic Services** – Senior citizen program funding, extension & agricultural services, and low income medical and rent assistance programs.

**Culture and Recreation** – Library and museum funding, and county parks.

**Conservation of Natural Resources** – Soil Conservation programs and Air Quality Control funding

**Community Development** – Community Development Block Grant projects

The County also operates the METRA (Montana Exposition, Trade, and Recreation Arena) and adjacent buildings and grounds. This facility includes 3 large multi-purpose event centers, a 4,000 seat grandstand and track, and large adjacent parking, grounds, and ancillary buildings.

## **FACTORS AFFECTING FINANCIAL CONDITION**

### **General Operating Environment**

The information presented in the financial statements is perhaps best understood from the broader perspective when it is considered with the specific perspective in which the County operates.

Local business activity includes agricultural, medical, retail, industrial, petroleum refining, banking, mining, and utility enterprises; which contribute substantially to the County's economy and tax base. The County is home to three substantial oil refineries, two major hospitals, and is the major retailer to a large geographical area. Billings also is an important tourism and cultural center to the region. These businesses and industries have historically provided a stable economy for the community and have provided for steady population and economic growth.

Montana's tax structure predominately relies on income, mineral, property, gambling, and motor vehicle taxes. Counties directly levy property taxes and indirectly share in mineral, gambling and motor vehicle taxes by receiving revenue distribution from the State referred to as the entitlement share that is supported by the aforementioned taxes. The State has no general sales tax although some communities in the State are permitted to levy a local sales tax (referred to as the resort tax). Yellowstone County is not currently permitted to levy a local sales tax.

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Property taxing authority is statutorily determined and taxing authority above the allowed maximum level must be voter approved. The local governing bodies determine the amount of property tax revenue they wish to levy annually up to the maximum allowed. New property revenues are permitted for new construction valuation and a statutorily determined acceptable inflation growth indexed to 50% of the State's rate of inflation (1.20% for fiscal year 2013; 1.03% for fiscal year 2014; 1.03% for fiscal year 2015; and .67% for fiscal year 2016).

The Management Discussion and Analysis provides additional discussion of specific pending financial impacts on the County.

**Recent Events and Economic Conditions**

With the June 2015 defeat of the proposed levy to fund the expansion of the detention facility, the County will be considering options to address this ongoing overcrowding issue in the coming months. There is a strong possibility that a solution will involve significant expenditures out of the County's CIP funds, as well as fund reserves. Over time, this will also negatively impact interest earnings derived from these funds for other County uses.

Over the past decade, the Billings area has benefited greatly from its proximity to the Bakken oil fields in eastern Montana and western North Dakota. Our community provides a significant amount of manufacturing, transport, services, and support to companies doing business in that region. Our local economy has unquestionably benefited from these related activities. Housing in the area has seen strength from the influx of people wanting to live here while commuting to the oil fields. The recent prolonged drop in oil prices is curtailing new exploration and has begun to have a negative effect on some local businesses.

Local medical facilities continue to expand, and Billings continues to be a dominant regional medical center.

New residential and commercial construction has continued, but may be showing initial signs of slowing. New hotel development has continued.

Most of the County's large property tax protests from prior years have been settled with the Montana Department of Revenue. These settlements were distributed both to outside taxing jurisdictions and various county funds prior to the end of the fiscal year. The final resolution was distributed in early FY16, providing the County with slightly over \$500,000 from previously sequestered funds.

CHS, Inc. continues its protests, with almost \$3.1 million set aside from November 2015 collections alone. As the County's largest taxpayer, this continues to have a material impact on many local taxing entities. Phillips 66/Conoco has protested slightly more than \$1.4 million, with Verizon at \$248,000. In total, protests for the tax year of 2015 (FY16) stand materially more than estimated in the FY16 budget, on pace to exceed 6% in most County funds, while 4.1% was budgeted. Total protests for the November collection cycle of approximately \$5.4 million.

The unemployment rate for Yellowstone County is approximately 3%. Many employers have been challenged to find enough qualified workers and that has led to competitive wage growth. The diversity provided by local energy, retail, medical, and agriculture businesses help stabilize employment swings that much of the country experiences. Businesses are attracted by the educated workforce, reasonable cost-of-living, education system, and local amenities.

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**Internal Controls**

In developing and evaluating the County's accounting system, consideration is given to the adequacy of internal accounting controls. Internal accounting controls are designed to provide reasonable, but not absolute assurance regarding; (1) the safeguarding of assets against loss from unauthorized uses; (2) the reliability of financial records for preparing financial statements and maintaining accountability for assets; and (3) maintaining compliance with laws and regulations. The concept of reasonable assurance recognizes the costs of internal control should not exceed the benefits likely to be derived and the evaluation of costs and benefits requires estimates and judgments by management.

All internal control evaluations occur within the above framework. We believe the County's internal controls adequately safeguard assets, provide reasonable assurance of proper recording of financial transactions, and maintain compliance with laws and regulations.

As a recipient of Federal and State financial assistance, the County also is responsible for ensuring adequate internal control is in place to ensure compliance with applicable laws and regulations related to major programs. This internal control is subject to periodic evaluation by management and the internal audit staff of the County.

**Risk Management**

The County uses a self-funded Property and Liability Insurance Fund because the County considers it to be cost effective to self-insure for routine claims and reinsure for catastrophic losses. The County carries commercial liability coverage with a current deductible of \$250,000 and an aggregate limit of \$3,000,000 per year. Coverage of \$3 million per year is anticipated to provide a high degree of safety from catastrophic losses. The Property and Liability Insurance Fund has a fund balance of \$2,803,448, which is considered to be a sufficient reserve to fund the incurred claims against the County after establishing reasonably estimated loss reserves. See footnote 10 (page 69) for additional discussion on liability reinsurance. The County also carries \$173.7 million (FY15) in property damage coverage with a \$50,000 deductible on buildings and their contents.

See footnotes 10 and 11 (pages 69-72) for additional description of coverages related to worker's compensation and health insurance.

**Cash Management**

The County currently has an investment program agreement with the local schools, irrigation, cemetery, rural fire and other special districts to invest their funds as part of an investment pool. The County invests the funds at a fee of 1% of the interest proceeds received for the month. Currently the County invests in repurchase agreements; U.S. government securities; agencies of the U.S. government; and the Certificate of Deposit Account Registry Service (CDARS), which are time deposits issued through a local bank that are 100% FDIC insured. The rate of return for the investment pool is net of bank service fees incurred for the operational costs of the participating pool members. Investments are limited to a 5 year maturity. A comparison of previous years' investment results are as follows:

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**Cash Management continued:**

	<u>Total Interest Earned</u>	<u>Average Investment Balance</u>	<u>Rate of Return</u>
F.Y. 05-06	2,693,838	73,462,474	3.67%
F.Y. 06-07	3,963,897	83,597,321	4.74%
F.Y. 07-08	3,839,852	91,680,559	4.18%
F.Y. 08-09	2,727,239	101,596,016	2.68%
F.Y. 09-10	1,794,512	117,258,972	1.71%
F.Y. 10-11	1,164,351	105,370,634	1.11%
F.Y. 11-12	736,441	113,288,374	0.65%
F.Y. 12-13	518,708	139,604,003	0.37%
F.Y. 13-14	786,253	153,628,654	0.51%
F.Y. 14-15	1,104,073	148,673,700	0.75%

The rate of return for FY16 is expected to be higher than FY15's rate of return due to the increase in overall market rates. See footnote 4 (pages 52-56) for additional information on cash and cash investments.

**Debt**

At June 30, 2015 Yellowstone County has a number of debt issues outstanding. These issues include \$3,525,000 in limited tax general obligation bonds; and \$1,313,225 of rural special improvement district bonds for which the County has limited secondary responsibility. The County has no outstanding notes payable as of June 30, 2015.

See footnote 8 (pages 62-66) and the MD&A (pages 4-23) for additional information on long-term county debt.

**Pension and Other Post-Retirement Benefits and Obligations**

All county employees may elect participation in the Public Employees Retirement System (PERS) or Sheriff Retirement System (SRS) if they meet eligibility criteria. Employees exceeding 960 hours of work in a year must participate in PERS if they're in a covered position. Effective July 1, 2014 the current employer contribution rates are 8.17% of covered payroll for PERS and 10.115% for SRS. New employees have the option to elect membership in either a defined benefit (DB) plan or defined contribution (DC) plan. Employees hired before July 1, 2002 have had the opportunity to select their retirement option (DB or DC). Employees hired after July 1, 2002 have 12 months to select an irrevocable retirement option. Funding requirements and plan administration is the responsibility of the State of Montana. The PERS and SRS plans continue to be in poor fiscal condition. Legislation passed in the 2013 legislature added funding to the PERS pension system from the employer, the State, and the employee as well as reducing benefits for retirees in an attempt to improve the fiscal position of PERS. While certain portions of the legislation were recently upheld, the benefit reductions were overturned by the courts.

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**Pension and Other Post-Retirement Benefits and Obligations continued:**

The County allows retiring employees receiving a State pension the option to retain health insurance benefits on the County's plan. Eligible retirees and their dependents may maintain County coverage provided they pay the health insurance premium. Retirees and their dependents under 65 years old pay the same premium as active employees, except that retiree pays the coverage cost for themselves in addition to their dependents.

Retirees and their spouses over 65 pay a reduced premium, since the County becomes a secondary payer after Medicare. Effective July 1, 2008 the County began offering an option to Medicare eligible retirees to participate in Medicare advantage plans administered by third party companies. Medicare eligible retirees currently have an annual election to participate in the Medicare advantage plan or the county's health plan.

Terminating employees that do not elect or are not eligible for a pension may elect to retain County health coverage under the provisions of the Consolidated Omnibus Budget Reconciliation Act (COBRA). This coverage may be elected and paid for by the terminating employee for up to 18 months.

See footnotes 11E (pages 72-74) and 12 (pages 75-94) for additional information on pension and other post-retirement benefits and obligations.

**ACKNOWLEDGEMENTS**

This financial report is simply one method of reflecting efforts of all those who serve in County government. We are employed by our County's citizens, whom we endeavor to serve every day. Without our citizens and businesses providing the funding and direction for needed services and programs, the County government could not function. I appreciate and applaud the efforts of all community members who work to improve the community and its governments. The goal of this report is to provide useful information regarding the use of the resources provided to Yellowstone County government operations.

I would like to express my appreciation to the finance department staff and the staffs of all the County offices for providing excellent work and cooperation during the year. Although the finance department takes on the task of preparing the financial report, all county departments contribute to the cooperative effort required to maintain the financial system.

A special thanks is extended to Lisa Sticka and Jennifer Amundsen for their work in the preparation of the financial report, and assistance with the audit. As this is Lisa's last year in working with us, I want to extend to her a special thanks for her years of dedicated service to this department, the County, and the citizens whom we all serve. I would also like to thank Anderson ZurMuehlen & Company for their assistance, and for the auditing of this report.

Respectfully submitted,



Kevan Bryan, Finance Director