

**Ohio Office of Budget  
and Management**

State of Ohio  
*Bob Taft*  
**Governor**



**OHIO**

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FOR THE FISCAL YEAR  
ENDED JUNE 30, 2002

# **INTRODUCTORY SECTION**



January 28, 2003

To the Governor, the Honorable Members of the General Assembly, and the Citizens of Ohio:

It is my privilege to issue the *Ohio Comprehensive Annual Financial Report* (CAFR) on the financial condition of the State of Ohio for the fiscal year ended June 30, 2002. The report is prepared in conformity with Generally Accepted Accounting Principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB).

The Ohio Office of Budget and Management pursuant to Section 126.21, Ohio Revised Code, which requires that an official financial report of the State be issued annually, prepared this report. The report includes the basic financial statements, which provide an overview of the State's financial position and the results of financial operations.

The Office of Budget and Management is responsible for the accuracy of the data presented and the completeness and fairness of its presentation, including all disclosures. To the best of our knowledge and belief, the enclosed data are accurate in all material respects and are reported in a manner designed to present fairly the financial position and results of operations of the State of Ohio. All disclosures necessary to enable the reader to gain an understanding of the State's financial activities have been included.

The State's basic financial statements include all funds that comprise the State's legal entity or primary government. The State's reporting entity is also comprised of its component units for which the elected officials of the State's primary government are financially accountable. We followed the criteria of GASB Statement No. 14, *The Financial Reporting Entity*, to determine the organizations for which the State is financially accountable. NOTE 1A. to the financial statements explains more fully which financial activities are included in the State's reporting entity.

The CAFR includes the following: introductory section; financial section that presents the management's discussion and analysis (MD&A), basic financial statements, required supplementary information, combining financial statements, supporting schedules, and fund descriptions; and a statistical section that presents financial, economic, and demographic data for Ohio.

The MD&A, which is required under GAAP to accompany the basic financial statements, provides a narrative, introduction, overview, and analysis.

The reporting format for our CAFR is significantly different from the way the State more typically presents its finances on a non-GAAP budgetary basis. The most obvious difference is that the "General Fund" in the CAFR includes more than just the State's General Revenue Fund (GRF). The General Fund also includes other funds such as the reimbursement-supported funds used for activities administered by state agencies and departments for which special revenue or proprietary fund classifications were considered to be inappropriate.

### **INDEPENDENT AUDIT RESULTS**

The basic financial statements have been audited by the Office of the Auditor of State. The outcome of the audit conducted by the Auditor of State, in accordance with generally accepted auditing standards, was an unqualified auditors' report. This opinion indicates there was no limitation on the scope of the auditors' examination and the financial statements were presented fairly, in all material respects, in conformity with GAAP.

### **PROFILE OF THE GOVERNMENT**

The State of Ohio's first constitution was adopted in 1802, and Ohio entered the union in 1803. Ohio's present constitution was modified by a state constitutional convention in 1851 and has since been amended on numerous occasions. The Constitution establishes a state governmental structure similar to the federal model, with three separate branches of government — executive, legislative, and judicial.

The executive branch consists of the Governor and Lieutenant Governor, who are jointly elected, and four additional statewide elected officials: the Attorney General, the Auditor of State, the Secretary of State, and the Treasurer of State. All of these officials are elected to four-year terms. More than 100 departments, agencies, boards, and commissions are part of the executive branch of government and receive appropriations from the legislature, along with three judicial and five legislative agencies. An organizational chart of state government can be found on page 12.

The state legislature in Ohio is referred to as the General Assembly and consists of two separate chambers, the Senate, a 33-member body, and the House of Representatives, a 99-member body. Each member of the General Assembly is elected to represent the residents of a geographical district for a specified term. Members of Ohio's General Assembly are subject to term-limits; senators are re-

stricted to serving two four-year terms, and representatives are restricted to serving four two-year terms. Each chamber has a presiding officer to call the chamber to order and direct the calendar of events. The presiding officer in the Senate is the President of the Senate, and the presiding officer of the House of Representatives is the Speaker of the House. A new General Assembly is convened in January of each odd-numbered year.

Along with the establishment of our state governmental structure, the Constitution requires Ohio to have a balanced budget. Ohio's budget is prepared for a period of two years – a biennium –, which begins on July 1 of odd-numbered years and ends 24 months later on June 30.

The State provides a wide range of services and support to its citizenry that are accounted for in the following functions or programs: primary, secondary and other education, higher education support, public assistance and Medicaid, health and human services, justice and public protection, environmental protection and natural resources, transportation, general government, community and economic development, workers' compensation, lottery, unemployment compensation, tuition credits, liquor control, and other business-type activities.

#### **ACCOUNTING SYSTEM AND BUDGETARY CONTROL**

The State's management is responsible for establishing and maintaining internal control designed to ensure that the State's assets are protected from loss, theft, or misuse and to ensure that adequate accounting data are compiled to allow for the preparation of financial statements in conformity with GAAP. Internal control is designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that: 1) the cost of a control should not exceed the benefits likely to be derived, and 2) the valuation of costs and benefits requires estimates and judgments by management.

In fiscal year 1992, an executive order initiated the Internal Accounting Control Program (IACP). The IACP establishes written guidelines for state agencies to follow during periodic management reviews of their accounting operations. Under the program, agencies are required to formally establish, maintain, and annually evaluate and report on internal accounting control.

The State's Central Accounting System (CAS) achieves budgetary control over the various accounts of the State's funds. The General Assembly, authorizes expenditures by appropriating funds in biennial and supplemental appropriation acts. The Office of Budget and Management uses the CAS to control departmental obligation and expenditure activity to ensure authorized appropriations are not exceeded.

The State's non-GAAP budgetary financial statements are prepared on a modified cash basis of accounting. This means that revenues are recognized when cash is received and expenditures are recognized when cash is paid. Encumbrances, reservations of appropriation authority as of June 30, the end of the State fiscal year, are reflected as expenditures on the budgetary basis of accounting.

Budget-to-actual comparisons can be found in this report for each governmental fund for which an appropriated annual budget has been adopted. For the General Fund and major special revenue funds, these comparisons are presented as part of the basic financial statements. For other budgeted governmental funds with appropriated annual budgets, budget-to-actual comparisons are in the nonmajor governmental funds section of the CAFR.

Additional discussion of the budgetary and GAAP bases of accounting is provided in NOTE 1 to the financial statements.

The CAS maintains all non-GAAP budgetary basis transactions and most GAAP basis adjustments. In addition to the information obtained from the CAS for financial reporting, selected financial information provided by the State's agencies and departments is compiled to complete the GAAP basis financial statements.

Differences between the two bases of accounting (GAAP vs. non-GAAP budgetary) include: 1) entity differences — the GAAP reporting entity may include organizations such as financing authorities and other component units that are not included in the State's budget; 2) basis differences — the GAAP basis results in the reporting of accruals while the non-GAAP budgetary basis results in the reporting of cash transactions; and 3) timing differences — for example, GAAP recognizes expenditures for payables for goods and services received, whereas the non-GAAP budgetary basis considers unliquidated encumbrances as expenditures. A reconciliation between the GAAP basis and non-GAAP budgetary basis fund balances is presented in NOTE 3 to the financial statements.

#### **CASH MANAGEMENT**

In Ohio, with the exception of certain organizations within the State's reporting entity that have independent powers to manage and invest their funds, the Treasurer of State is responsible for investing the State's cash and investments pool. During fiscal year 2002, cash management and investment transactions made by the Treasurer of State's Office, in accordance with the Uniform Depository Act, were limited to checking accounts and certificates of deposit with qualified public depositories, U.S. government and agency obligations, commercial paper, repurchase agreements, bankers' acceptances, bonds of foreign nations diplomatically recognized by the United States, and security lending agree-

ments. Legal requirements for the investment of funds maintained in the State's cash and investments pool are discussed in NOTE 4 to the financial statements.

Quarterly, the Office of Budget and Management allocates the investment income earned on the cash and investments pool to the various funds designated by law to receive the earnings. The allocation is calculated in accordance with a formula based on average daily cash balances invested over the quarter. The Ohio Lottery Commission's investment portfolio, which is dedicated to the payment of deferred lottery prizes and is accounted for as part of the cash and investments pool, however, is not part of the investment earnings allocation just described. Instead, the Treasurer of State credits the investment earnings from the dedicated portfolio directly to the credit of the fund that accounts for this activity.

### **RETIREMENT SYSTEMS**

Employees of the primary government or its component units may be eligible to participate in the Ohio Public Employees Retirement System, the State Teachers Retirement System of Ohio, the State Highway Patrol Retirement System, or the Alternative Retirement Plan. Further information on the State's participation in the different retirement systems can be found in NOTE 9 to the financial statements.

### **RISK MANAGEMENT**

As discussed in NOTE 10. to the financial statements, the State's primary government is self-insured for claims under its traditional healthcare plan (OhioMed Health Plan) and for vehicle liability while it has placed public official fidelity bonding with a private insurer. The State self-funds tort liability and most property losses on a pay-as-you-go basis; however, selected state agencies have acquired private insurance for their property losses. Also, the State's primary government and its component units participate in a public entity risk pool, which is accounted for in the Bureau of Workers' Compensation Enterprise Fund, for the financing of their workers' compensation liability.

### **ECONOMIC OVERVIEW AND OUTLOOK**

After several quarters of sub-par growth, the U.S. economy is slowly recovering. However, the current recovery is expected to be a "jobless recovery," similar to the 1991-1992 economic expansion. Expansionary fiscal and monetary policies will spur economic growth for the short-term, but with foreign economies weak and capital spending rising only moderately, the current recovery cannot gain momentum.

Consumer spending, which constitutes about two-thirds of the economic activity in the U.S., continues to be the main driver of economic growth. Consumers rarely retrench, but when jobs are scarce and debts are high, as is the case now, the rate of growth in consumer spending slows. Consumers

are stretched about as far as they can go, taking on large amounts of debt in the process. Debt-service payments are claiming a record share of disposable income despite the drop in interest rates. For the recovery to experience solid growth, investment spending and capital outlays must be revived.

The financial markets continue to reflect a combination of worries over the strength of the recovery, the war in the Middle East, and lack of confidence in the numbers that are released from corporate income statements. Even if the stock market has already hit bottom, the climb from the hole is expected to be very slow and gradual. Investors will once again demand a substantial risk premium on stocks and the temptation of profit taking to recover losses will keep a lid on the price of equities.

The forecast for inflation calls for moderate growth at the consumer level. Outside of the volatile food and energy component, producer prices for finished goods are rising at less than 0.5 percent a year. Core consumer prices are rising a bit faster because of the heavy weighting of services. But even with services, inflation as measured by the Consumer Price Index is predicted to increase about 2.0 to 2.5 percent a year.

The economic outlook for the State of Ohio is consistent with the forecast of slow and moderate growth at the national level. Real Gross Domestic Product, the total value of goods and services produced in the U.S. and adjusted for inflation, is expected to grow in the range of 2.5 to 3.5 percent annually over the next three years.

## **MAJOR INITIATIVES AND PROJECTS**

### **The State Operating Budget**

Due to the national economic slowdown, Ohio experienced its most serious budget crisis in a decade. As part of a balanced approach to this crisis, Governor Taft ordered six-percent cuts to most state agencies in fiscal year 2002. These cuts came on top of the \$181 million in cuts mandated in the previous fiscal year and another \$600 million in proposed state agency spending that was redirected from agencies to a school funding solution during the last biennial budget development process. To begin fiscal year 2003, Governor Taft issued even more cuts – 15 percent for most state agencies. Later, on January 22, 2003, the Governor ordered additional budget cuts of 2.5 percent. Overall, Ohio's state agencies have experienced significant budget cuts in the past two years. The challenge continues to be providing essential state services in an efficient, effective and cost conscious manner.

### **Primary and Secondary Education**

Governor Taft's highest priority is enabling every child to succeed. This is reflected in the fiscal year 2002-2003 budget in which 62.7 percent of all new GRF dollars are used to support education at all lev-

els and the implementation of a new school funding formula that guarantees that every school child in Ohio has access to the resources necessary for a quality education. State appropriations for primary and secondary education totaled \$7.4 billion in fiscal year 2002 (an eight-percent increase over fiscal year 2001) and \$7.8 billion in fiscal year 2003 (a five-percent increase over fiscal year 2002). Pursuant to the new school funding formula, per pupil spending increased to \$4,814 in 2002 (an increase of 12.1 percent over fiscal year 2001) and \$4,949 in 2003 (an increase of 2.8 percent over fiscal year 2002). Under the current plan, per pupil spending will rise to \$5,527 by fiscal year 2007. The funding model is based on successful 1999 local school districts and removes those districts that fall within the top and bottom five percent of districts with regard to income and property wealth.

As an outgrowth of legislation enacted in June 2001, the state has begun to develop and implement policies and programs to address academic standards and student assessment; to improve student learning; and to establish school accountability. In fiscal year 2002, the State Board of Education adopted language arts and mathematics standards; curriculum models in these two subject areas are under development and social studies and science standards are slated for completion at the end of this year. Additionally, in fiscal year 2002, the State appropriated \$23.7 million for the administration of 4<sup>th</sup>, 6<sup>th</sup>, and 9<sup>th</sup> grade proficiency tests and the development of new federally required achievement, graduation and diagnostic tests. The fiscal year 2002 budget also supported \$31.9 million for student intervention services and \$4.5 million for the development and distribution of school report cards.

Other areas supported by FY 2002 appropriations include:

- \$99.8 million of parity aid that provides funding for low-wealth school districts;
- \$360.1 million to support disadvantaged pupil impact aid for economically disadvantaged children;
- \$339.2 million for special education; and
- \$45.9 million to support gifted units and the identification of gifted children.

### **Primary and Secondary Education — Ohio Supreme Court Case Update**

Litigation, similar to that in other states, has been pending in Ohio courts since 1991 questioning the constitutionality of Ohio's system of school funding and compliance with the constitutional requirement that the State provide a "thorough and efficient system of common schools." On December 11, 2002, the Ohio Supreme Court, in a 4-3 decision on a motion to reconsider its own decision rendered in September 2001, concluded (as it had in its 1997 and

2000 opinions in that litigation) that the State did not comply with that requirement, even after again noting and crediting the significant steps it had taken in recent years. The Court directed the General Assembly "to enact a school-funding scheme that is thorough and efficient" — as explained in its prior decisions and accompanying concurrences — dismissed the case, and relinquished any further oversight of it.

It is not possible at this time to state what or when the General Assembly's further responses will be, or what effect they or any related actions may have on the State's overall financial condition (particularly in the current biennium) or on specific state operations.

### **Rebuilding Ohio's Schools**

Governor Taft, through the Rebuild Ohio Plan, has proposed spending over \$10.2 billion in state funding, matched by \$12.9 billion in local funding, in a 12-year plan to address the facility needs of all Ohio school districts. The plan will allow every Ohio school child to learn in safe, modern facilities and give school districts the capability to create customized classrooms and instruction tailored to meet students' needs. The School Facilities Commission (SFC), charged with providing funding to public school districts and overseeing the construction and renovation of school facilities, has disbursed over \$2.5 billion, and spends over \$2 million a day. SFC currently administers school facility projects in 130 districts with over 300 buildings at a value of over \$4 billion in design, construction, or completion. At the end of calendar year 2001, SFC had completed 21 district-wide projects and finished the construction or renovation of 60 buildings. By the end of calendar year 2002, SFC estimates it will complete an additional 23 district-wide projects and an additional 83 buildings.

A major undertaking in fiscal year 2002 was the creation of the Accelerated Urban Assistance Initiative. The SFC conducted facility assessments and developed master facility plans to modernize Ohio's largest urban schools including Akron City, Dayton City, Columbus City, Cincinnati City, Cleveland Municipal and Toledo City schools. These school districts, which include over 500 buildings, house approximately 16 percent of Ohio's student population. The total projected cost for the six plans is \$5.74 billion, of which \$2.95 billion will be paid by the State. Funding for the construction portion of the program will begin in fiscal year 2003.

No other state in the nation has adopted such a comprehensive and ambitious building program. In fact, during the five years that SFC has been in existence (since May 1997), Ohio has appropriated nearly 20 percent more for school facility programs than the neighboring states of Michigan, Indiana, Pennsylvania, Kentucky, and West Virginia combined.

### Third Frontier Project

The Third Frontier Project is the state's largest commitment ever to expanding Ohio's high-tech research capabilities and promoting start-up companies to build high-wage jobs for generations to come. The Third Frontier Project will make Ohio a leader in high-tech, high-paying jobs by

- Committing \$500 million over the next 10 years through the Technology Action Fund and the Biomedical Research and Technology Transfer Fund.
- Proposing a new, ten-year, \$500 million capital improvement program to improve research facilities. These funds will finance buildings and provide equipment for globally competitive centers of innovation that will be named after the Wright Brothers.
- Initiating a \$500 million bond program to provide much-needed resources to recruit world-class researchers and bring state-of-the-art products to market.
- Creating a \$100 million Innovation Ohio Fund to help finance targeted industries with high-growth, high-wage potential consistent with regional priorities. The fund will support advanced manufacturing technologies to help existing industries become more productive, competitive and profitable.

Through the Third Frontier Project, federal and private sector support could boost the total investment to more than \$6 billion, and make Ohio a leader in high-tech, high-wage jobs over the next decade.

### Ohio Homeland Security

In response to the terrorist attacks of September 11, 2001, Governor Taft established the State of Ohio Security Task Force to develop a coordinated, comprehensive strategy to address security issues. The Task Force is organized into committees covering law enforcement, transportation security, technology research and development, medical and health preparedness, emergency preparedness, and funding and legislation. The Task Force shares information and discusses time-sensitive issues affecting Ohio and works proactively to enhance the state's security efforts. The Ohio Security Task Force has worked with federal, county and local Emergency Management Agency (EMA) officials, law enforcement and other agencies to complete a three-year domestic preparedness assessment, making it possible for Ohio to qualify for additional federal dollars to support security efforts across the state.

In September 2002, the U.S. Department of Justice approved Ohio's plan to allocate \$9.9 million in federal homeland security funds among Ohio's 88 counties and five state agencies. Ohio's share of

this national program is seventh largest among the country's states and territories and will be used to help finance local homeland security drills and exercises and purchase emergency response equipment as determined by comprehensive ongoing threat, risk and needs assessments from each county. In addition, federal funds will support:

- The State Fire Marshal to purchase first responder supplies and equipment;
- The Ohio Department of Agriculture to buy testing and verification equipment for its laboratory; and
- The Ohio EMA to purchase trailers stocked with medical items for first responders.

### CERTIFICATE OF ACHIEVEMENT

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the State of Ohio for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2001. This was the 12th consecutive year that the State has achieved this prestigious award.

To be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized CAFR. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current report continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to GFOA to determine its eligibility for another certificate.

### ADDITIONAL INFORMATION

The Ohio Office of Budget and Management provides access to the fiscal year 2002 *Ohio Comprehensive Annual Financial Report*, fiscal year 2002 *Ohio Budgetary Financial Report*, and other State-related financial data and information on the Internet at <http://www.state.oh.us/obm/>.

### ACKNOWLEDGMENTS

In conclusion, I wish to express my appreciation to the staffs of the various State agencies whose time and dedicated efforts made this report possible.

Sincerely,



Thomas W. Johnson  
Director

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

## State of Ohio

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2001

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



*William Patrick Pate*  
President

*Jeffrey L. Esser*  
Executive Director



# STATE OF OHIO OFFICIALS

## EXECUTIVE

Bob Taft  
Governor

Maureen O'Connor  
Lieutenant Governor

Betty D. Montgomery  
Attorney General

Jim Petro  
Auditor of State

Joseph T. Deters  
Treasurer of State

J. Kenneth Blackwell  
Secretary of State

## LEGISLATIVE

Richard H. Finan  
President of the Senate

Larry Householder  
Speaker of the House

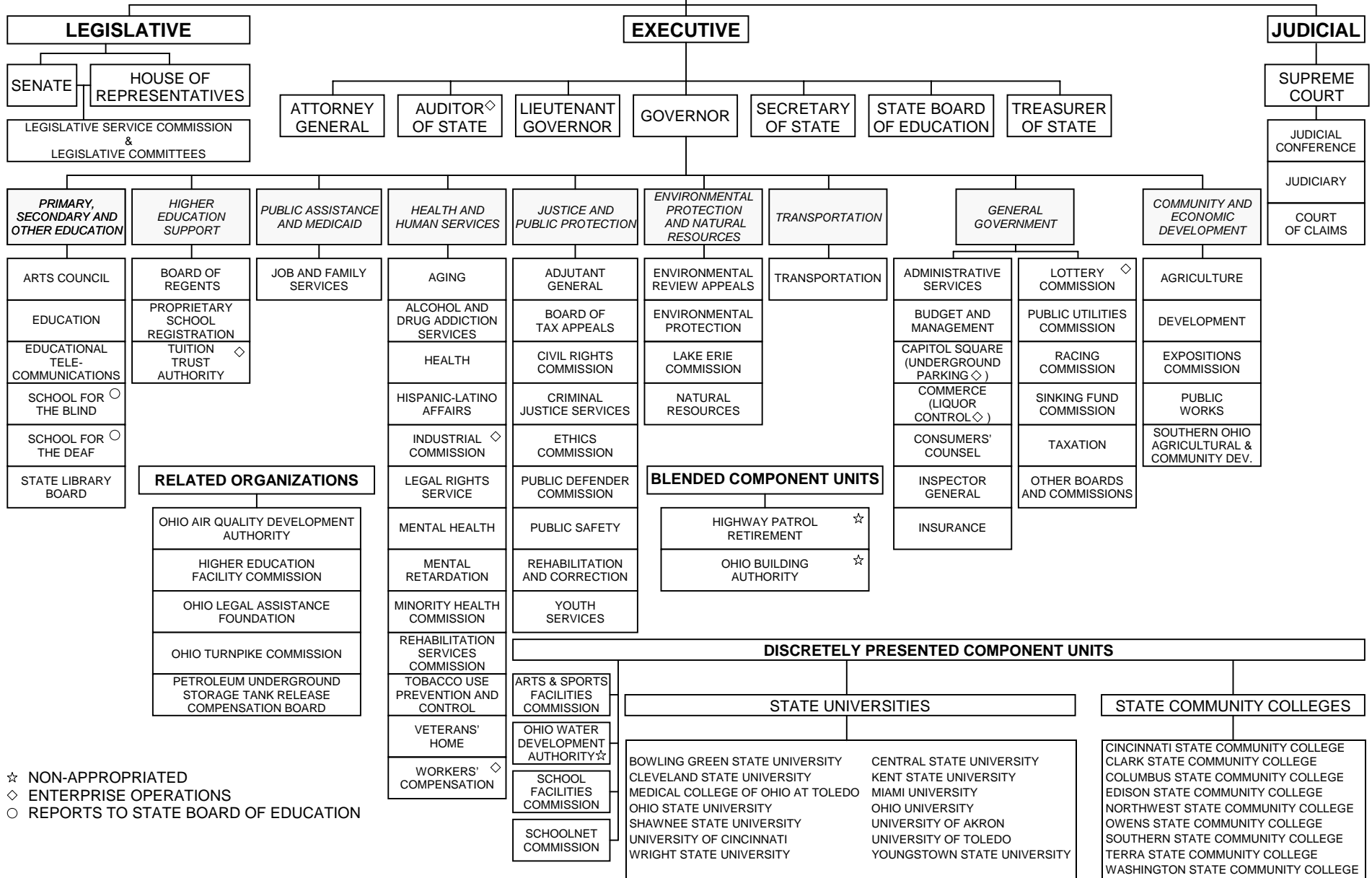
## JUDICIAL

Thomas J. Moyer  
Chief Justice  
Supreme Court

# STATE OF OHIO ORGANIZATION CHART

THE CITIZENS OF OHIO

PRIMARY GOVERNMENT



- ☆ NON-APPROPRIATED
- ◇ ENTERPRISE OPERATIONS
- REPORTS TO STATE BOARD OF EDUCATION