

Defining the indicators

According to Ohio law, the Auditor of State must “develop guidelines for identifying fiscal practices and budgetary conditions, amongst municipal corporations, counties, and townships that, if uncorrected, could result in a future declaration of fiscal watch or emergency.”



Pursuant to Ohio Revised Code Section 118.025, the Auditor of State may declare an entity in fiscal caution for engaging in certain fiscal practices or budgetary conditions. In addition to these fiscal caution guidelines, the Auditor of State has developed Financial Health Indicators (FHI). FHI are a collection of financial information, percentages and ratios gathered from annual financial statements filed by the local governments and their audit reports, which are useful in predicting financial stability.

The Auditor of State will use these FHI to recognize early signs of fiscal stress at specific local governments and, where requested, take a proactive approach to monitoring or assisting these local governments.

Seventeen FHI have been identified as useful in determining signs of fiscal stress. The FHI are based on information derived from the annual financial statement data submitted to the Auditor of State by local governments and their audit reports.

From the financial statement data, our staff gathers information as it relates to:

Governmental Type Activities (GTA)

The financial information for Governmental Type Activities is from the government-wide financial statements — Statement of Net Assets/Position and Statement of Activities.

General Fund and All Governmental Funds

General Fund and All Governmental Fund information is from the govern-

mental fund type financial statements — Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balances.

From the audit reports, the Auditor’s staff gathers information as to whether the entity is complying with Ohio budgetary law and/or proper accounting methods.

The Auditor of State has evaluated the 17 FHI as useful in identifying fiscal stress in local governments that report financial statements prepared in conformity with Generally Accepted Accounting Principles (GAAP). For local governments that choose to present their financial statements on cash or modified cash basis of accounting, it has been determined that at least 15 of the FHI are useful in identifying fiscal stress.

Using historical data, the Auditor of State has determined that entities reporting on a **GAAP basis** have higher financial stress if they have at least six FHI with a “critical outlook” or if they have a combination of eight negative indicators, either “critical” and “cautionary. The higher the number of “critical” indicators, the higher the level of stress.

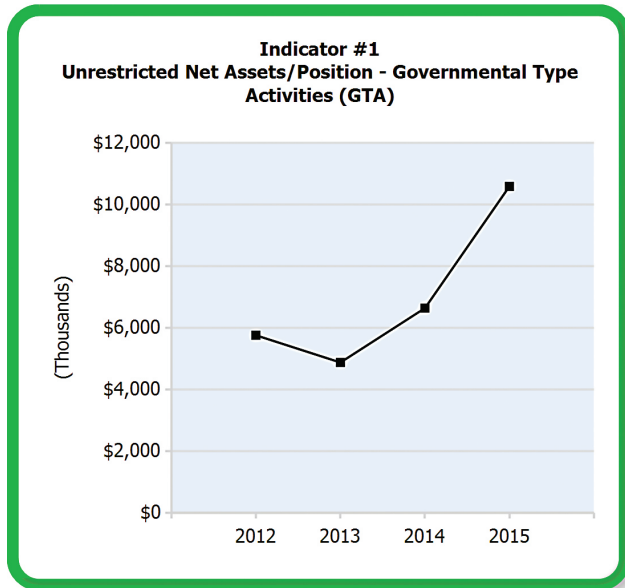
Using the same data, the Auditor of State determined entities reporting on a **cash or modified cash basis** of accounting are at an elevated risk of financial stress if they have at least four “critical” indicators or a combination of at least six “critical” and “cautionary” indicators. The stress is higher as the number of “critical” indicators increases.

FINANCIAL HEALTH INDICATORS

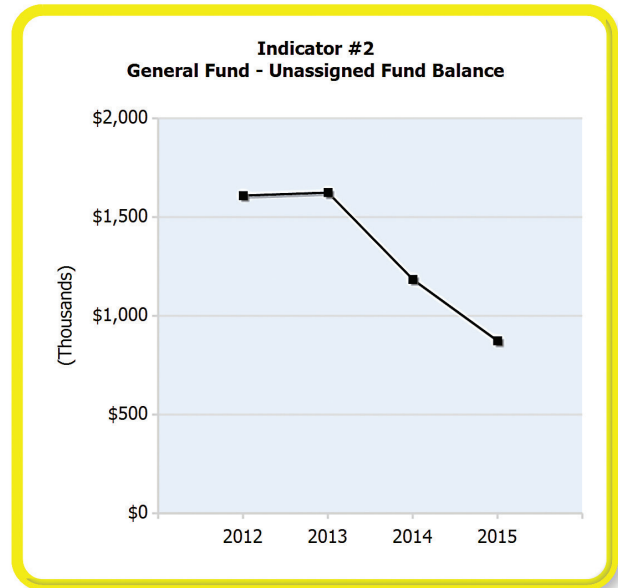
Description of indicators

The 17 FHI, including the description, meaning, and importance of each indicator, are:

Indicator #1 - Positive Outlook



Indicator #2 - Cautionary Outlook



1 Unrestricted Net Assets/Position of Governmental Type Activities (GTA)

- There are three (3) major components to net assets/position (equity) - Net investment in capital assets, restricted net assets/position, and unrestricted net assets/position.

- Unrestricted net assets/position represents the portion of net position that has no related liabilities or restriction as to use.

- Negative unrestricted net assets/position occurs primarily if liabilities exceed assets.

What it means: This indicator identifies when an entity has declining or negative unrestricted net assets/position.

Why it is important: This indicator identifies if net assets/position is available for unrestricted purposes. Although unrestricted net assets/position may not be in liquid form, it is important to have net assets/position available and unrestricted as to use. If an entity's unrestricted net assets/position is declining or is negative, it leaves little or no room for unexpected expenses; and therefore, is a sign of fiscal stress.

Critical Outlook – Zero or negative amounts

Cautionary Outlook – Decline between the current and prior year by more than 1%.

2 Unassigned Fund Balance of the General Fund

- A component of equity

- There are five components of fund equity – nonspendable, restricted, committed, assigned, and unassigned. Unassigned fund balance is the portion of fund balance that has no related liabilities or has not otherwise been obligated.

What it means: This indicator identifies when an entity has declining or negative unassigned fund balance.

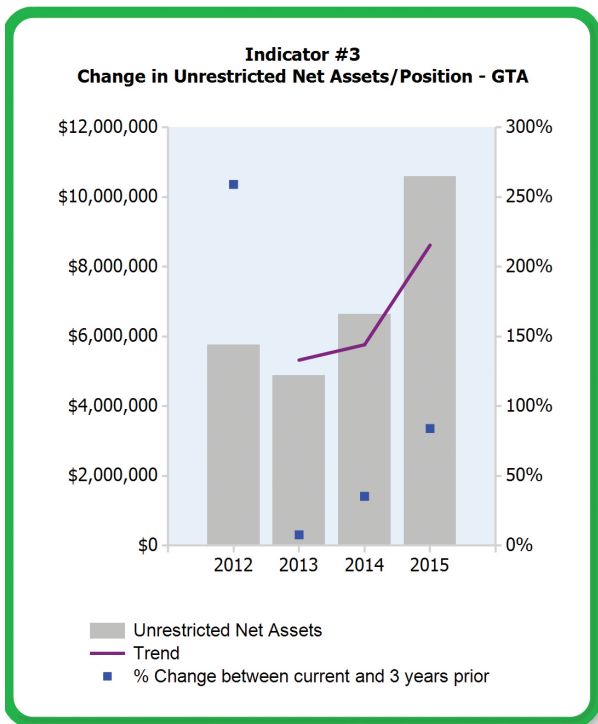
Why it is important: This indicator identifies if fund balance is available for unrestricted purposes. Although unassigned fund balance may not be in liquid form, it is important to have fund balance available without restrictions as to use. If an entity's unassigned fund balance is declining or is negative, it leaves little or no room for unexpected expenses; and therefore, is a sign of fiscal stress.

Critical Outlook – Zero or negative amounts

Cautionary Outlook – Decline between the current and prior year by more than 1%.

Description of indicators

Indicator #3 - Positive Outlook



3 Change in Unrestricted Net Assets/Position for GTA

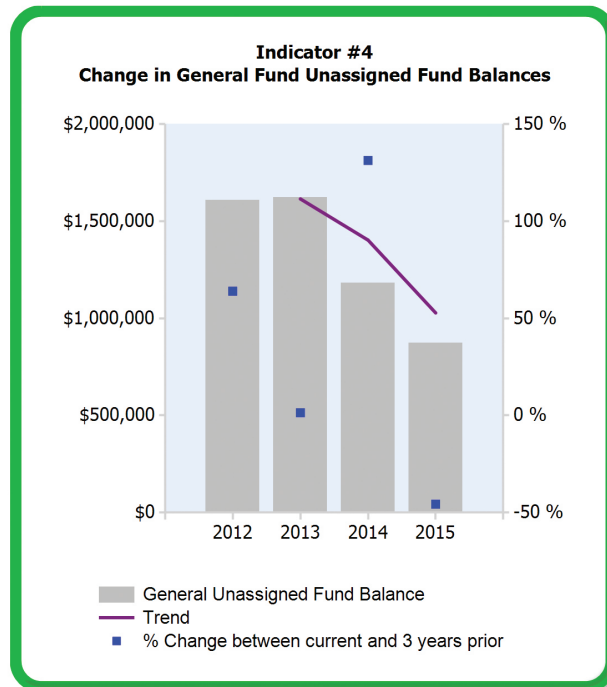
What it means: This indicator identifies changes (increases or decreases) in unrestricted net assets/position from the prior year to the current year and will be useful in identifying local governments whose unrestricted net assets/position is deteriorating.

Why it is important: A declining unrestricted net assets/position can be a sign of fiscal stress. This indicator is important in identifying a trend of deteriorating unrestricted net assets/position as well as how rapidly it is deteriorating.

Critical Outlook – The current period and at least two of the previous three periods reflecting a zero or negative amount OR a rapidly declining trend defined as a decline in each of the last three periods with a drop of greater than 20%.

Cautionary Outlook – Declining trend defined as a decline in each of the last three periods with a drop of 10% to 20%.

Indicator #4 - Positive Outlook



4 Change in General Fund Unassigned Fund Balance

What it means: This indicator identifies changes (increases or decreases) in unassigned fund balance from the prior year to the current year and is useful in identifying local governments whose unassigned fund balance is deteriorating.

Why it is important: A declining unassigned fund balance can be a sign of fiscal stress. This indicator is important in identifying a trend of a deteriorating unassigned fund balance as well as how rapidly it is deteriorating.

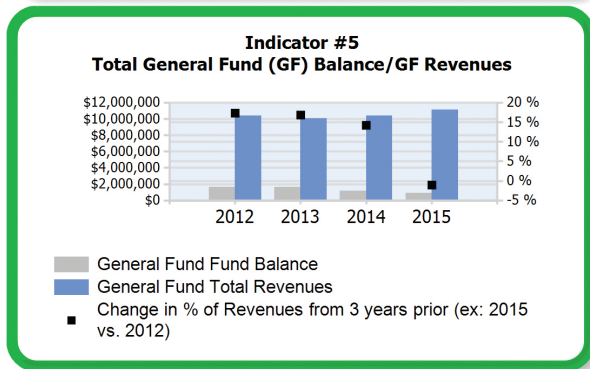
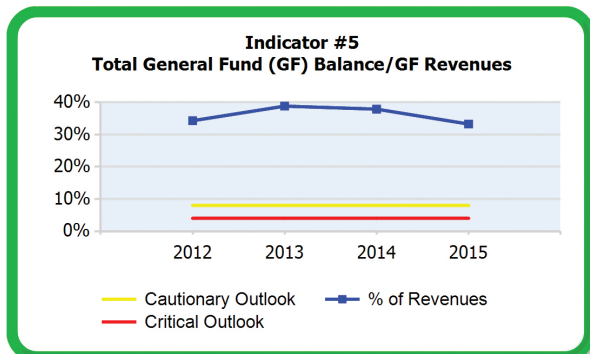
Critical Outlook – The current period and at least two of the previous three periods reflecting a zero or negative amount OR a rapidly declining trend defined as a decline in each of the last three periods with a drop of greater than 20%.

Cautionary Outlook – Declining trend defined as a decline in each of the last three periods with a drop of 10% to 20%.

FINANCIAL HEALTH INDICATORS

Description of indicators

Indicator #5 - Positive Outlook



5 Total General Fund (GF) Balance / GF Revenues

What it means: This indicator identifies reserves available in the General Fund. The larger the reserve the better the entity is able to absorb, in the short term, the impact of sudden revenue loss or significant increases in operating costs, and begin planning financial adjustments.

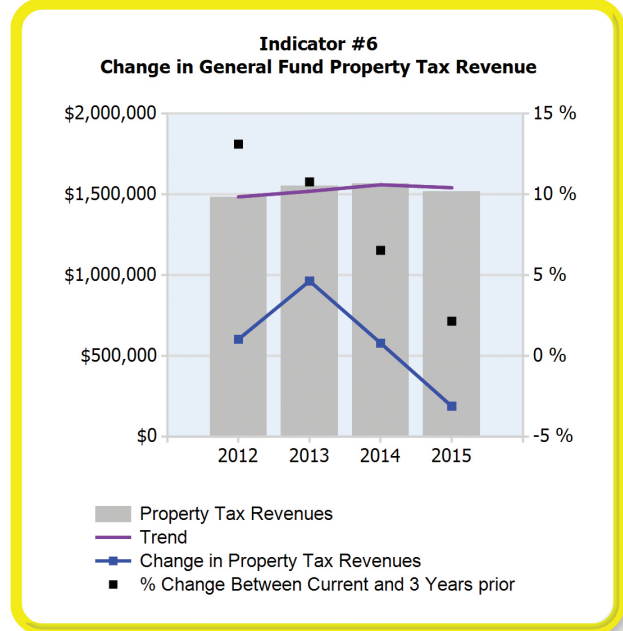
This indicator is calculated by taking the total General Fund balance divided by total General Fund revenues. This will determine the percentage of total General Fund revenues (or the current year budget) that has been reserved or available for carry over to the following year.

Why it is important: This indicator identifies a low reserve of fund balance even if Indicators 1 through 4 do not indicate negative unrestricted net assets/position or unassigned fund balance.

Critical Outlook – Negative percentage, very low percentage (< 1/24 or 4%), OR if fund balance is less than a two month carryover (17%), a rapidly declining trend defined as a drop of 10% or greater over a three year period.

Cautionary Outlook – Low percentage (< 1/12th or 8%) OR if fund balance is less than a two month carry-over (17%), a declining trend defined as a drop of 5%-10% over a three year period, OR if the fund balance represents less than 6 months (50%) of current year revenues, a decline in each of the last three periods.

Indicator #6 - Cautionary Outlook



6 Decline in General Fund Property Tax Revenue

What it means: This indicator reflects the percentage change from year to year for property tax revenue.

Why it is important: This indicator reflects declines in property tax revenue and is an indication that an entity may be facing financial hardship due to declines in significant revenue sources. It will also reflect the need for additional sources of revenue to maintain stability.

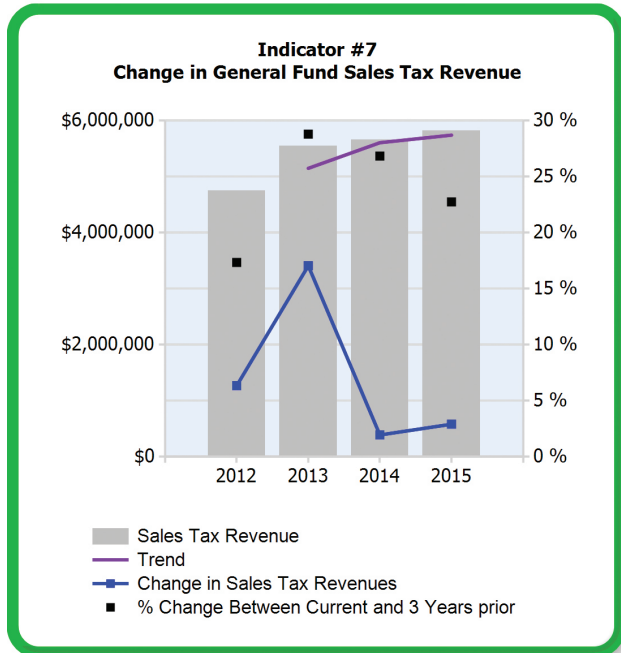
Critical Outlook – If property tax revenues represent 7-20% of total General Fund revenues, a trend of declining tax revenue over the last three years in excess of 20% OR if property tax revenues represent greater than 20% of total revenues, a trend of declining tax revenue over the last 3 years in excess of 10%.

Cautionary Outlook – Decrease in tax revenue from the current to the prior year by more than 1%.

FINANCIAL HEALTH INDICATORS

Description of indicators

Indicator #7 - Positive Outlook



7 Decline in General Fund Tax Revenue (Income Tax/Cities, Sales Tax/Counties)

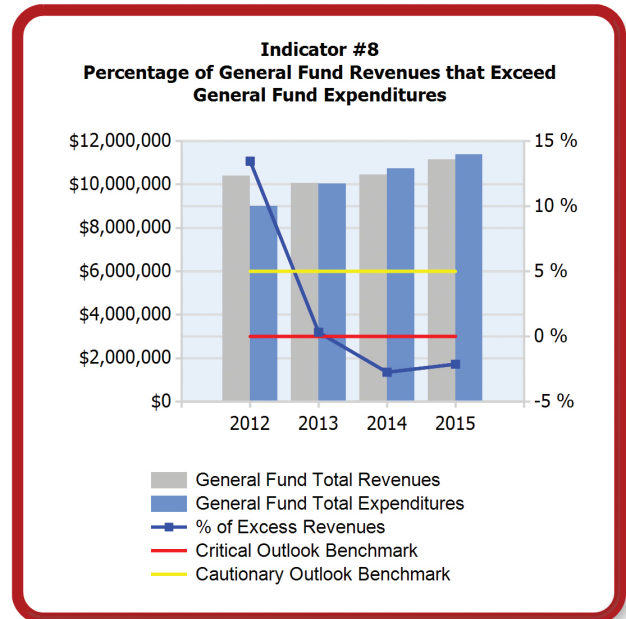
What it means: This indicator reflects the percentage change from year to year for sales tax revenue for counties and income tax revenue for cities.

Why it is important: This indicator reflects declines in these revenue types and is an indication that an entity may be facing financial hardship due to declines in significant revenue sources. It will also reflect the need for additional sources of revenue to maintain stability.

Critical Outlook – If income tax or sales tax revenues represent 7-20% of total General Fund revenues, a trend of declining tax revenue over a three year period in excess of 20% OR if income tax or sales tax revenues represent greater than 20% of total general fund revenues, a trend of declining tax revenue over the last 3 years in excess of 10%.

Cautionary Outlook – Decrease in tax revenue from the current to the prior year by more than 1%.

Indicator #8 - Critical Outlook



8 Percentage of General Fund Revenues that Exceed General Fund Expenditures

What it means: This indicator is calculated as total General Fund revenues less total General Fund expenditures, divided by total General Fund revenues. It will provide an indication of operating deficits and the size of the operating deficit compared to the current year budget. An operating deficit is the difference between revenues and expenditures. If expenditures exceed revenues, an operating deficit exists.

Why it is important: This indicator is important because it reflects if an operating deficit exists but also emphasizes the size of the deficit as compared to the current year's budget. This is an indication of the shortage in the current budget. A trend of operating deficits indicates potential financial hardship.

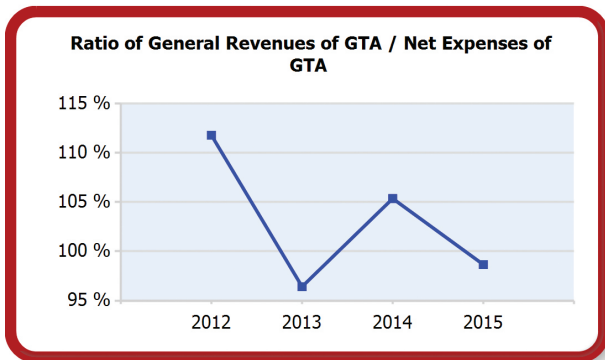
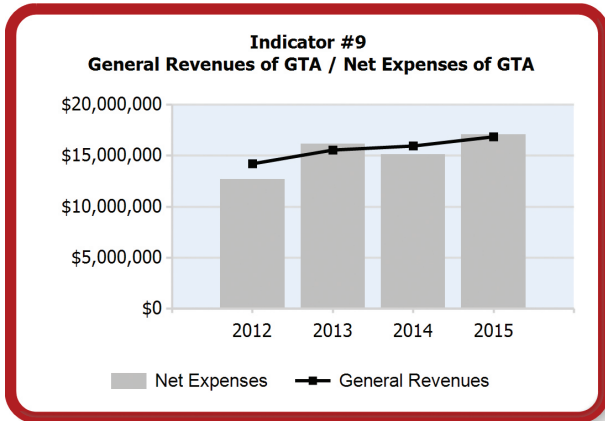
Critical Outlook – Negative percentage

Cautionary Outlook – Low percentage (<1/20th or 5%)

FINANCIAL HEALTH INDICATORS

Description of indicators

Indicator #9 - Critical Outlook



9 General Revenues of GTA / Net Expenses of GTA

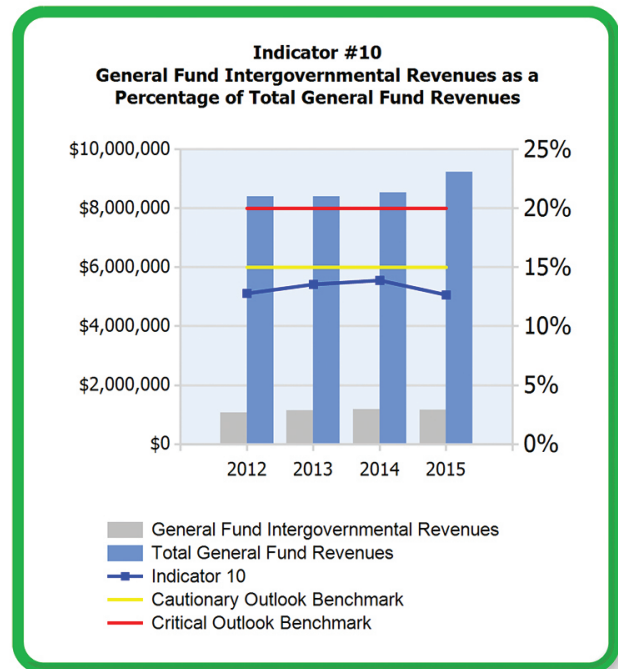
What it means: The ratio of this indicator reflects coverage of net expenses by general revenues. This indicator determines if, on a government-wide basis, expenses are exceeding revenues. For example, local taxes, unrestricted revenues (e.g. investment earnings) and unrestricted grants should be sufficient to meet expenses not covered by program revenues. Net expense is total expense less program revenues. Program revenues include charges for services (e.g. fees and fines), operating grants and capital grants.

Why it is important: This indicator is important to be aware if a shortage in revenues to cover expenses exists. A declining trend would indicate fiscal stress.

Critical Outlook – Ratio less than 100%

Cautionary Outlook – Declining trend of at least three years

Indicator #10 - Positive Outlook



10 General Fund Intergovernmental Revenues as a Percentage of Total General Fund Revenues

What it means: This indicator will reflect an over-reliance on intergovernmental revenues which are subject to state and federal budget cuts. A high percentage suggests the entity is heavily reliant on external governmental organizations for grants, entitlements, or shared revenues; and therefore, vulnerable to decreases in these revenue sources.

Why it is important: It is important to be aware of the percentage of total revenues that are not considered “own-source,” or local sources, of revenue. Understanding the percentage of total revenues derived from intergovernmental sources is important when trying to maintain fiscal stability, while dealing with an economic downturn.

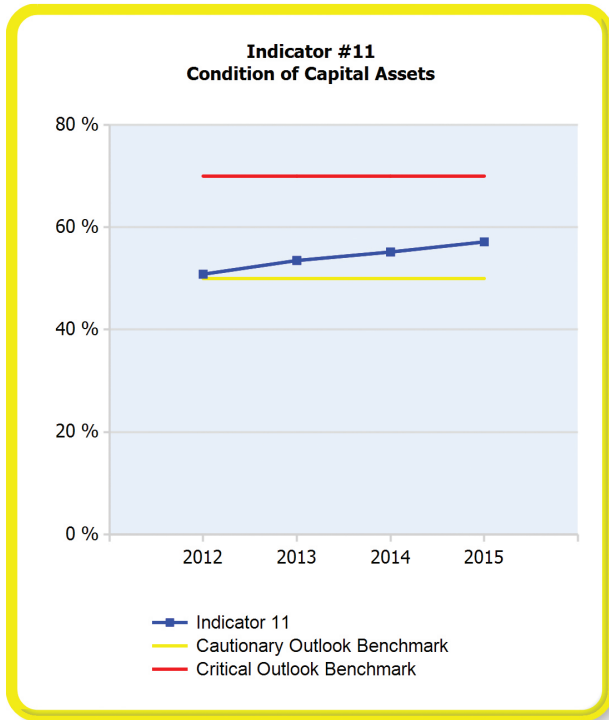
Critical Outlook – Ratio greater than 20%

Cautionary Outlook – Ratio between 15% - 20%

FINANCIAL HEALTH INDICATORS

Description of indicators

Indicator #11 - Cautionary Outlook



11 Condition of Capital Assets*

What it means: This indicator is accumulated depreciation as a percentage of depreciable capital assets. This indicator will identify situations in which repair or replacement of the local government's assets will be necessary. A high percentage indicates assets replacement is imminent and the entity may be delaying replacement of assets or significant repairs for cash flow purposes.

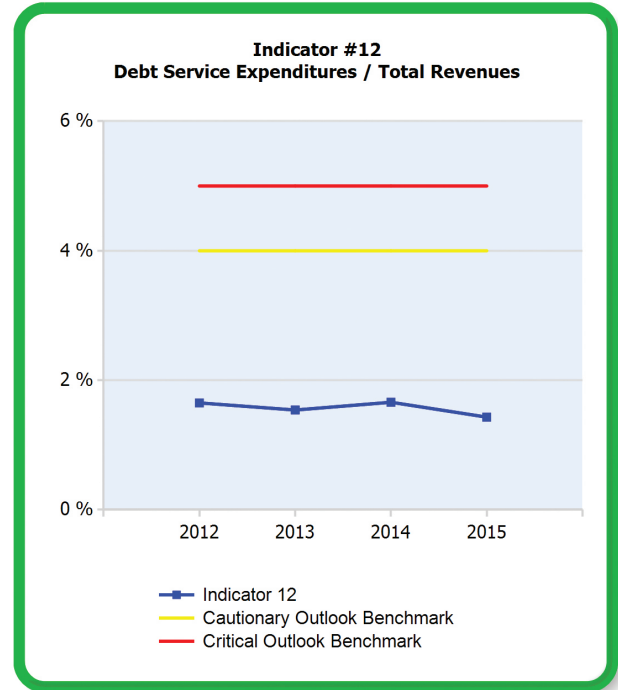
Why it is important: When entities delay improving or replacing assets in order to maintain cash flows for other purposes, improvements and replacements become absolutely necessary and may contribute to financial hardship on an already strained budget.

Critical Outlook – Ratio greater than 70%

Cautionary Outlook – Ratio between 50% - 70%

*This FHI is only applicable to local governments reporting on a GAAP basis of accounting

Indicator #12 - Positive Outlook



12 Debt Service Expenditures / Total Revenues

What it means: This indicator is total debt service expenditures divided by total revenues (for all governmental funds). This indicator identifies the percentage of the budget used/needed for repayment of debt.

Why it is important: Higher debt service expenditures to total revenues is unfavorable since the entity spends more of its current budget on debt repayment. An increasing trend of debt service expenditures to total revenues may mean the percentage of budget dedicated to debt payments is increasing; and therefore, less revenue will be available for asset repair/replacement or meeting current service demands.

For Cities:

Critical Outlook – Ratio greater than 15%

Cautionary Outlook – Ratio between 12% - 15%

For Counties:

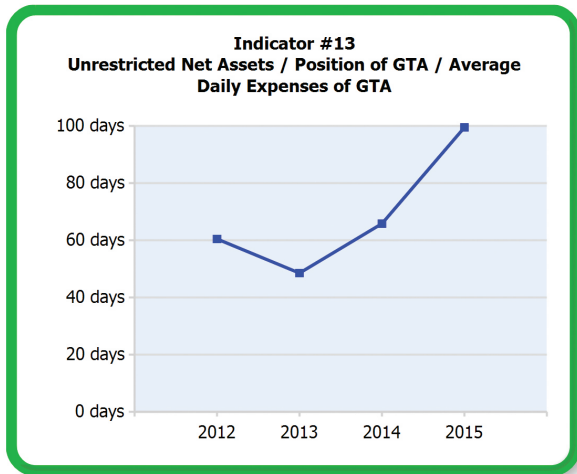
Critical Outlook – Ratio greater than 5%

Cautionary Outlook – Ratio between 4% - 5%

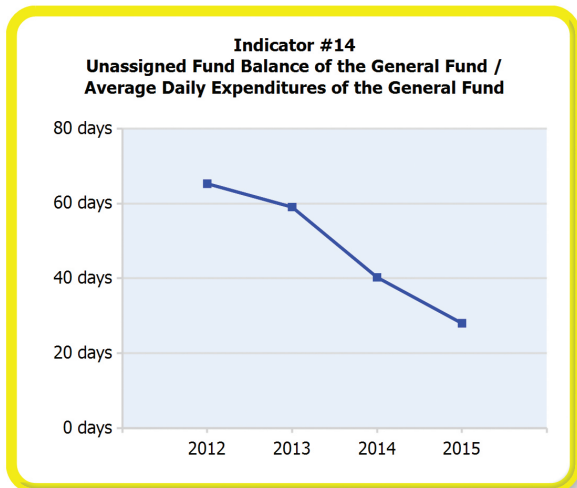
FINANCIAL HEALTH INDICATORS

Description of indicators

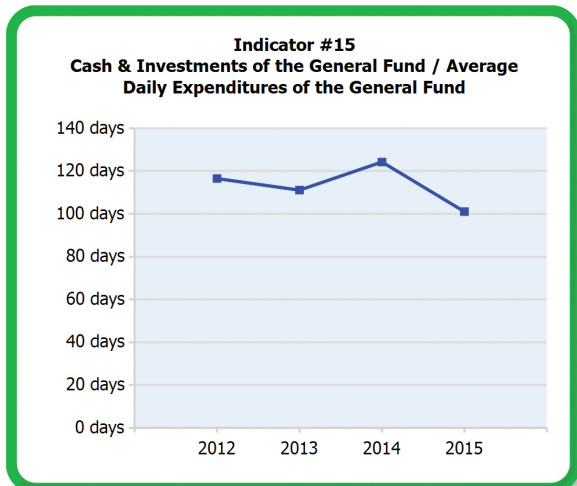
Indicator #13 - Positive Outlook



Indicator #14 - Cautionary Outlook



Indicator #15 - Positive Outlook



13-15. Average Daily Expenses or Expenditures Ratio (Indicators 13, 14 & 15):

13. Unrestricted Net Assets/Position of GTA/Average Daily Expenses of GTA

14. Unassigned Fund Balance of the General Fund/Average Daily Expenditures of the General Fund

15. Cash & Investments of the General Fund/Average Daily Expenditures of the General Fund

What they mean: Indicators 13, 14 and 15 identify the number of days the local government’s unrestricted net assets/position, unassigned fund balance, and cash and investments will sustain the entity. The indicators are based on the daily average expenses/expenditures.

Why it is important: These indicators are important because they identify the number days the entity may operate using their unrestricted net assets/position, unassigned fund balance, and cash and investments. The fewer days the entity can operate, the more financial stress they are under. It provides an early indication of an entity’s need to adjust their financial/expenditure planning.

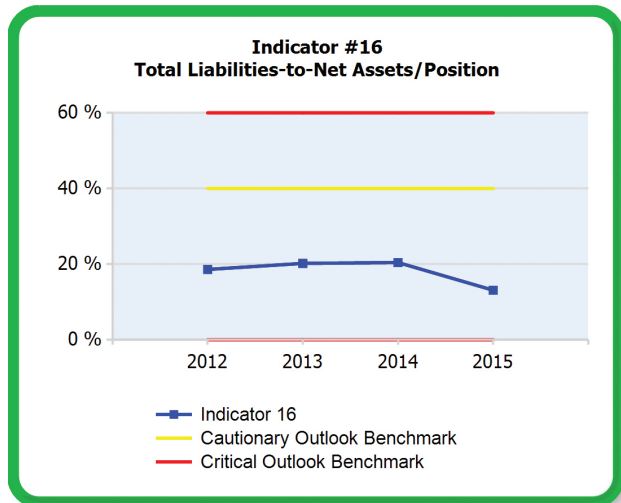
Critical Outlook – Zero days or below

Cautionary Outlook – Less than 30 days

FINANCIAL HEALTH INDICATORS

Description of indicators

Indicator #16 - Positive Outlook



16 Total Liabilities-to-Net Assets/Position*

What it means: This indicator is the ratio of total liabilities of GTA divided by total net assets/position of GTA and indicates the percentage of every dollar of resources, available for providing public services, that is owed by the entity.

Why it is important: This indicator identifies entities that are over-extended in terms of the percentage of every dollar which is owed to others.

For Cities:

Critical Outlook – Negative ratio (representing negative net assets) OR ratio greater than 70%

Cautionary Outlook – Ratio between 50% - 70%

For Counties:

Critical Outlook – Negative ratio (representing negative net assets) OR ratio greater than 60%

Cautionary Outlook – Ratio between 40% - 60%

* This FHI is only applicable to local governments reporting on a GAAP basis of accounting

Indicator #17 - Positive Outlook

| Indicator #17 Budgetary Non-Compliance and/or Unreconciled/Unauditable Financial Records? | |
|--|------------|
| Audited Year End | Applicable |
| 2015 | No |
| 2014 | No |
| 2013 | No |
| 2012 | No |

17 Budgetary Non-Compliance and/or Unreconciled/Unauditable Financial Records

What it means: This indicator identifies if an entity's recent audit reports include budgetary non-compliance and/or unreconciled/unauditable financial records. The Indicator 17 determination is based on the current and prior two (2) audited years.

Why it is important: This indicator will reflect if an entity is not complying with Ohio budgetary law and/or proper accounting methods. Maintaining accurate, reconciled accounting records and adherence to Ohio budgetary law is a significant factor in maintaining fiscal stability.

Critical Outlook – Direct and material audit finding(s) described above for the current and prior two audit years.

Cautionary Outlook – Direct and material audit finding(s) described above for the current audited year.