

## CHAPTER 1 DIRECT LAWS

AU-C 250 *Consideration of Laws and Regulations in an Audit of Financial Statements* clarifies the auditor’s responsibility regarding OCS tests:

“.02 . . . The provisions of some laws or regulations have a **direct** effect on the financial statements in that they **determine the reported amounts and [required] disclosures** in an entity’s financial statements. . .”

Conversely:

“.A13 Many laws and regulations relating principally to the operating aspects of the entity do not *directly* affect the financial statements (their financial statement effect is **indirect**) and are *not captured by the entity’s information systems relevant to financial reporting*. Their **indirect effect** may result from the need to disclose a contingent liability because of the allegation or determination of identified or suspected noncompliance.”

- Based on the above (and AU-C 250.A9 – .A11), “**direct** and material compliance” refers **only** to laws a government’s information system (which includes its accounting system) must “capture” to **determine financial statement amounts and required disclosures**<sup>1</sup>. Therefore, we have classified a law as **direct** in this OCS if noncompliance has the potential to materially misstate the financial statements. Chapter 1 of this compliance supplement includes “direct” laws.
  - As one example, GAAP requires governments to present budgetary comparisons as basic statements or as RSI.
  - GAAP also requires these presentations to follow the government’s legal budget basis.
    - In Ohio, a “5705 government’s” information system must capture information using the accounting basis Ohio Rev. Code Chapter 5705 (via GASB Cod. 2400) prescribes to compile budget and actual amounts and budget variances GAAP requires.
    - Ohio Rev. Code Chapter 5705 generally prescribes a cash + encumbrance accounting basis, which a compiler must understand and follow to satisfy GAAP.
- In addition to the discussion above from AU-C 250, the AICPA Audit and Accounting Guide *State and Local Governments*, sections 4.09 through 4.22, discusses legal requirements which might directly and materially affect determining financial statement amounts for a governmental entity. Material noncompliance (having a direct or indirect effect) would often:
  - Require adjusting amounts or revising disclosures.
    - Auditors should do the same regarding noncompliance **indirectly** affecting financial statement amounts or disclosures, if they become aware of it.
      - For example, AU-C 250.06 b.iii describes material penalties as an **indirect effect**, though they may require disclosure or even accrual as a contingent expense

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<sup>1</sup> Few Ohio GAAP governments’ have “formal” systems to compile most balance sheet assets or liabilities. Therefore, GAAP governments’ “information systems” include trial balances, other spreadsheets or any other material used to compile GAAP amounts or disclosures.

Cash / AOS basis governments’ *information systems* include documents used to prepare / support notes to the statements.

- Require reporting as a material GAGAS noncompliance finding.
- May represent significant / material violations of “finance-related legal and contractual provisions”
  - GASB Cod. 2300.106(h) require “notes to the financial statements should disclose significant material violations of finance-related legal and contractual provisions” and “actions taken to address significant violations”.
  - See [OCSImplementationGuide\\_2016.docx#Fin\\_Related\\_Legal\\_Contractual\\_Provisions](#).
- AAG SLG 4.12 lists examples of laws that may directly and materially affect the determination of financial statement amounts and disclosures. When preparing this edition of the OCS we considered the examples in 4.12. Each law in OCS Chapter 1 has potential for a direct effect. Laws with indirect classification per AU-C 250.06 b are included in Chapter 2.

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**Section A: Budgetary Requirements**  
**GENERAL REQUIREMENTS**

**1-1 Compliance Requirement:** Ohio Rev. Code §5705.38 Annual appropriation measure.

**Summary of Requirements:**

Ohio Rev. Code §5705.38(A) requires that on or about the first day of each fiscal year, an appropriation measure is to be passed. If the taxing authority wants to postpone the passage of the annual appropriation measure until an amended certificate is received from the county budget commission based upon the actual year end balances, it may pass a temporary appropriation measure for meeting the ordinary expenses until no later than April 1. This does not apply to school district appropriations.

Ohio Rev. Code §5705.38(B) provides that a board of education shall pass its annual appropriation measure by the first day of October. If a school district's annual appropriation measure is delayed as permitted by law (see below), the board may pass a temporary measure for meeting the ordinary expense of the school district until it passes an annual appropriation measure.

The taxing authority of a taxing unit that does not levy a tax must still appropriate at the minimum level of control prescribed by Ohio Rev. Code §5705.38(C) (or a lower level). No budget commission approval is required by 5705.28(B)(2)<sup>2</sup>.

As discussed in AOS Bulletin 1998-012 there are two circumstances when school district certificates/certifications would be issued after October 1:

- A certificate/certification would be issued after October 1 when a school district has borrowed against its spending reserve. This certificate/certification would not be issued until second half personal property taxes are settled.
- A certificate/certification would be issued after October 1 when the delivery of a tax duplicate is delayed under Ohio Rev. Code §323.17 because a subdivision in the county has placed a levy on the November ballot which, if approved, will go on the current tax list and duplicate.

If a school district is in either of these two situations, passage of the annual appropriation measure should be delayed until the necessary certificates/certifications are received.

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<sup>2</sup> For conservancy districts, auditors should additionally review the requirements of Ohio Rev. Code §6101.44 and tailor their compliance testing procedures accordingly, if necessary. For conservancy districts that levy taxes, we should cite to the budgetary requirements contained in Ohio Rev. Code § 6101.44 where they are similar to requirements contained in Ohio Rev. Code Chapter 5705. The more specific requirements contained in Ohio Rev. Code Chapter 6101 trump those contained in Chapter 5705. Auditors should apply the provisions of Ohio Rev. Code Chapter 5705 when Chapter 6101 does not address budgetary restrictions applicable to conservancy districts.

**Legal Level of Control: Minimum Requirements<sup>3</sup>**

- 1) Ohio Admin. Code §117-2-02(C)(1) states in part: “The legal level of control is the level (e.g., fund, program or function, department, or object) at which spending in excess of budgeted amounts would be a violation of law. This is established by the level at which the legislative body appropriates. For all local public offices subject to the provisions of Chapter 5705 of the Revised Code, except school districts and public libraries, the minimum legal level of control is described in section 5705.38 of the Revised Code (**see 2 below**). For school districts, the minimum legal level of control is prescribed in rule 117-6-02 of the Administrative Code (**see 3 below**). For public libraries, the minimum legal level of control is prescribed in rule 117-8-02 of the Administrative Code (**see 4 below**). The legal level of control is a discretionary decision to be made by the legislative authority, *unless otherwise prescribed by statute.*” (Emphasis added.)
2. Ohio Rev. Code §5705.38(C) requires the following minimum level of budgetary control for “subdivisions” other than schools: “Appropriation measures shall be classified so as to set forth separately the amounts appropriated for each office, department, and division, and, within each, the amount appropriated for personal services.”<sup>4</sup>
3. Ohio Admin. Code §117-6-02 prescribes the following for school districts’ legal level of control: “At a minimum, appropriation measures shall be classified to set forth separately the amounts appropriated by fund. The appropriation measure as passed by the school board shall be the legal level of control. This is the level at which compliance with statutory budgetary requirements will be determined.” **The AOS recommends that boards of education pass appropriations at a more detailed level. This is, however, a discretionary decision for the board of education based on the degree of control the board of education wishes to maintain over the financial activity of the school district.**
4. Ohio Admin. Code §117-8-02 requires the library's legislative body to adopt appropriation measures. These measures establish the legal level of control.

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<sup>3</sup> **We should not recommend that governments adopt the highest level of control the statutes allows.** Appropriating at lower levels than the minimums the Ohio Rev. Code or Ohio Admin. Code requires provides the legislative authority with more control over disbursements. However, appropriating at *very* low levels can significantly increase the volume of appropriation amendments requiring legislative approval as well as possibly requiring additional disbursement codes (more function, object codes, etc.). Conversely, appropriating at higher levels may simplify appropriation measures, but in doing so, the legislative authority effectively delegates more spending decisions to the fiscal officer. The legislative authority should choose the level of control it believes meets its needs to control expenditures. Also, the legislative authority may choose differing levels of control for different funds, *as long as they meet at least the minimum statutory requirements.*

<sup>4</sup> Staff should exercise judgment in determining whether to cite these governments. The following provides some guidance in determining this:

- Because Ohio Admin. Code §117-6-02 permits school districts to use the fund as their level of budgetary control, we presume noncompliance will not be an issue for school districts.

Because other facts and circumstances may arise regarding this matter, or if you are unsure whether citing a taxing district for this matter is fair, please consult with your regional chief auditor. If the regional chief is unsure, they can present the facts and circumstances to their Center for Audit Excellence Support representative.

5. Ohio Admin. Code §117-2-02(C)(1) also states in part: “All local public offices should integrate the budgetary accounts, at the legal level of control or lower, into the financial accounting system. This means designing an accounting system to provide ongoing and timely information on unrealized budgetary receipts and remaining uncommitted balances of appropriations.”

**Amounts / Funds Not Subject to Budgeting:**

- The nonexpendable principal of nonexpendable trust funds.<sup>5</sup> Appropriating nonexpendable principal would authorize the fiscal officer to spend the principal in violation of the trust agreement. [§5705.36(A)]
- Budget stabilization reserves [§5705.13, 5705.29(G)]
- The balance in a township reserve balance account established under Ohio Rev. Code §5705.132.
- For some time, AOS policy has been that agency funds do not require budgeting. Agency funds account for money a government holds in an agency capacity on behalf of another person or entity. Therefore, a government has minimal discretion in spending this money. Accordingly, the legislative body need not authorize a purpose for spending the money.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Accounting system capable of recording appropriations and comparing them to actual results</li> <li>• Reconciling appropriation totals to totals recorded in the accounting system.</li> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

<sup>5</sup> The ORC still refers to *nonexpendable trust funds*. GASB 54 amended GASB 34 and now requires classifying amounts legally or contractually required to be maintained (e.g., the principal of a Permanent Fund) as Non-expendable Fund Balances (and Restricted Net Assets in entity-wide statements). See AOS Bulletin 2011-004. Private-Purpose Trust Funds, on the other hand, are not subject to GASB 54 fund balance classifications. GASB 34 and 54 do not affect this ORC requirement. That is, these ORC requirements still apply to private purpose trust and permanent funds.

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Read the minutes and determine if the governing board adopted an annual appropriation measure by the required date.

If a school district has delayed adoption of an annual appropriation measure, inquire about the reasons for the delay.

Scan appropriation measures to determine whether they meet at least the minimum legal level of control 5705.38(C) prescribes.

Determine if the accounting system “integrates” budgetary data at the legal level of control. This means the accounting system should report appropriations, encumbrances, unencumbered cash balances, and estimated receipts, and should compare budgetary data to actual results. If the client uses a manual system (i.e. spreadsheets) determine if the manual system used by the client adequately tracks and compares budgetary data.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-2 Compliance Requirements:** Ohio Rev. Code Sections §5705.41 (D); and 5705.42 - Restrictions on appropriating and expending money.

**Summary of Requirements:**

The authorization of a bond issue is *deemed an appropriation* of the proceeds of the bond issue for the purpose for which such bonds were issued. No expenditure shall be made from any bond fund until first authorized by the taxing authority. [Ohio Rev. Code §5705.41(A)]

Similarly, Federal and State grants or loans are “*deemed appropriated*”<sup>6</sup> for such purpose by the taxing authority” as provided by law and shall be recorded as such by the fiscal officer of the subdivision, and is deemed in process of collection [Ohio Rev. Code §5705.42].

No orders or contracts involving the expenditure of money are to be made unless there is a certificate of the fiscal officer that the amount required for the order or contract has been lawfully appropriated and is in the treasury **or in the process of collection**<sup>7</sup> to the credit of an appropriate fund free from any previous encumbrances. [Ohio Rev. Code §5705.41(D)(1)]<sup>8 9</sup>

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<sup>6</sup> “Deemed an appropriation” under this section means the Federal or State government has already appropriated and established the purpose(s) for which a government can spend monies received from Federal or State grants and loans. The taxing authority cannot deviate from this purpose; the taxing authority can only resolve to spend the money for a purpose already prescribed in a contract, grant agreement, loan agreement, etc. Therefore, Federal and State grants and loans received under Ohio Rev. Code §5705.42 *do not* require formal appropriation by the legislative body. In other words, Ohio Rev. Code §5705.42 effectively eliminates an unnecessary appropriation action by the taxing authority. However, Ohio Rev. Code §5705.42 directs the fiscal officer to *record* the appropriation amount in the accounting system. The fiscal officer should also include the appropriated amounts on the (amended) certificate to properly monitor budget versus actual activity. *Note:* Amounts “deemed appropriated” are subject to inclusion in GAAP budgetary presentations (GASB Cod. 2400.102). The government has no legal authority to spend these resources unless they were either appropriated by the legislative authority or deemed appropriated by the Federal or State government. (2013-14 2015-1 GASB Comprehensive Implementation Guide Q&A 7.91.14.).

<sup>7</sup> It is permissible to certify a purchase without sufficient cash “in the bank” if a government is reasonably certain cash will be on hand in time to pay the invoice when due (i.e. is “**in the process of collection**”). For example, the Ohio EMA disburses Homeland Security grants only when the local government certifies to OEMA they have an invoice on hand requiring payment. Since the government will receive OEMA’s cash in time to pay the vendor, the CFO can certify the acquisition even if there is no cash in the fund at the time of the certification. (This assumes there is sufficient appropriation for the payment).

<sup>8</sup> Under Ohio Rev. Code §9.10, 9.11 and 1990 Op. Atty. Gen. No. 90-082, the fiscal officer need not manually sign each certification. Electronic or mechanical signatures are permissible. However, Ohio Rev. Code §9.10 expressly prohibits using rubber stamp signatures. (We likely would not deem using a rubber stamp to be material noncompliance.)

<sup>9</sup> Ohio Rev. Code §3315.20 permits schools to incur a fund cash deficit in certain circumstances.

If an entity levies taxes, Ohio Rev. Code §5705.41 applies. However, some entities with taxing authority do not levy taxes. When they do not levy taxes, Ohio Rev. Code §5705.28 (B)(2) permits a comparable, but somewhat streamlined budget process. Ohio Rev. Code §5705.28(B)(2) requires entities to follow §5705.41.<sup>10</sup>

Per 5705.41(D)(3), “Contract” as used in this section excludes current payrolls of regular employees and officers.

**Note:** See Appendix A-2 of the OCS Implementation Guide for examples of direct charges that do not require a certificate under 5705.41(D).

The statute provides the following exceptions to this basic requirement:

**Then and Now Certificate:** This exception provides that, if the fiscal officer can certify that both at the time that the contract<sup>11</sup> or order was made and at the time that he is completing his certification, sufficient funds were available or in the process of collection, to the credit of a proper fund, properly appropriated and free from any previous encumbrance, the taxing authority can authorize the drawing of a warrant. The taxing authority has 30 days from the receipt of such certificate to approve payment by resolution or ordinance. If approval is not made within 30 days, there is no legal liability on the part of the subdivision or taxing district.

Amounts of less than \$100 for counties, or less than \$3,000 for other political subdivisions, may be paid by the fiscal officer without such affirmation of the taxing authority upon completion of the "then and now" certificate, provided that the expenditure is otherwise lawful. This does not eliminate any otherwise applicable requirement for approval of expenditures by the taxing authority. [Ohio Rev. Code §5705.41(D)]

Fiscal officers may prepare "blanket" certificates for a sum not exceeding an amount established by resolution or ordinance<sup>12</sup> adopted by the members of the legislative authority against any specific line item account over a period not extending<sup>13</sup> beyond the end of the current fiscal year. The blanket

<sup>10</sup> For conservancy districts, auditors should additionally review the requirements of Ohio Rev. Code §6101.44 and tailor their compliance testing procedures accordingly, if necessary. For conservancy districts that levy taxes, we should cite to the budgetary requirements contained in Ohio Rev. Code § 6101.44 where they are similar to requirements contained in Ohio Rev. Code Chapter 5705. The more specific requirements contained in Ohio Rev. Code Chapter 6101 trump those contained in Chapter 5705. Auditors should apply the provisions of Ohio Rev. Code Chapter 5705 when Chapter 6101 does not address budgetary restrictions applicable to conservancy districts.

<sup>11</sup> 1987 Op. Atty. Gen. No. 87-069 concluded that when a government uses *Then and Now* certificates, they should charge the cost to the appropriation in effect at the time they incurred the obligation. For example, if a calendar-year government orders an item in December 2012, the government should charge the cost to 2012 appropriations, even if the fiscal officer signs a *Then and Now* Certificate in January 2013.

<sup>12</sup> The governing authority is only required to adopt one ordinance or resolution establishing the dollar limits for blanket certificates. A separate ordinance or resolution approving *each* individual blanket certificate is not necessary.

<sup>13</sup> We interpret the word “*extends*” in this context as the authority to certify commitments against a regular blanket certificate or super blanket certificate that expires at year end. However, the authority to pay against previously certified commitments continues until all outstanding commitments are paid. (In other words, the government should consider these unpaid year-end commitments similar to other outstanding commitments/encumbrances, and reduce next year’s opening unencumbered balances for these amounts.)

certificates may, but need not, be limited to a specific vendor. Only one blanket certificate may be outstanding at one particular time for any one particular line item<sup>14</sup> appropriation.

In addition to regular blanket certificates, a subdivision's fiscal officer may also issue so-called "super blanket" certificates for any amount for expenditures and contracts from a specific line-item appropriation account in a specified fund for most professional services, fuel, oil, food items and any other specific recurring and reasonably predictable operating expense. This certification is not to extend beyond the fiscal year or, in the case of counties, beyond the quarterly spending plan established by the county commissioners. More than one super blanket certificate may be outstanding at one particular time for a particular line-item appropriation account.

Continuing Contracts to be Performed in Whole or in Part in an Ensuing Fiscal Year: Where a continuing contract is to be performed in whole or in part in an ensuing fiscal year, only the amount required to meet those amounts in the fiscal year in which the contract is made needs to be certified. (1987 Op. Atty. Gen. 87-069)

Per Unit Contracts: Where contracts are entered into on a per unit basis, only the amount estimated to become due in the current fiscal year need be certified. (1987 Op. Atty. Gen. 87-069)

Contract or Lease Running Beyond the Termination of the Fiscal Year Made: Pursuant to §5705.44, Ohio Rev. Code, where a contract or lease runs beyond the termination of the fiscal year in which it is made, only the amount of the obligation maturing in the current fiscal year need be certified. The remaining amount is a fixed charge required to be provided for in the subsequent fiscal year's appropriations.

Payments made from the earnings of a public utility are exempted from the certification (and encumbering) requirements of Ohio Rev. Code section 5705.41(D). [Ohio Rev. Code §5705.44 and 1987 Op. Atty. Gen. No. 87- 069] However, these payments are still subject to the requirements of Ohio Rev. Code section 5705.41(B).

The Attorney General, in 1987 Op. Atty. Gen. No. 87-069, has clarified the application of the exceptions set forth above. In summary, he has indicated that:

If a government subject to Ohio Rev. Code §5705.41 (D) enters into a continuing contract under which no goods or services will be delivered during the current fiscal year and payment will not be due until delivery, no amount need be certified as available during the current fiscal year. Pursuant to Ohio Rev. Code §5705.44, the amount remaining unpaid at the end of a fiscal year to become due in the next fiscal year must be included in the annual appropriation measure for the next fiscal year as a fixed charge.

If under a continuing contract it cannot be determined whether delivery of goods or services and the obligation to make payment will take place in the current or an ensuing fiscal year, the total amount due under the contract must be certified as available during the current year.

If under a continuing contract delivery of goods or services is to occur in the current fiscal year with the obligation to make payment deferred until an ensuing fiscal year, the amount required to meet the

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<sup>14</sup> There is no additional legal explanation for what "line item appropriation" means in this context; therefore, AOS interprets "line item" to mean accounting line item, which is not necessarily the "legal level of control."

obligation for goods or services delivered during the current fiscal year must be certified as available in that fiscal year.

If a government subject to Ohio Rev. Code §5705.41 (D), enters into a contract that is not a continuing contract, the total amount due under the contract must be certified as available in the fiscal year in which the contract is made, regardless of when delivery of goods or services will be made or when payment will become due.

County Commissioner Authorization: A board of county commissioners, by resolution, may exempt purchases of \$1,000 or less from the prior certification requirement. The resolution must specify the dollar limit applicable to such purchases and whether it applies to all purchases, is limited to certain classes of purchases, or is limited to specific purchases. The board must notify the county auditor in writing of its intention to adopt such a resolution and the scope of the resolution. The county auditor has 15 days to comment on the resolution before it may be adopted by the board. Where such a resolution has been adopted, any person authorized to make purchases, within 3 business days (or other time limit the commissioners resolve) of making a purchase exempted under the resolution, must file with the county auditor a written or electronic document stating the purpose, amount, appropriation line item and date of the purchase, and the name of the vendor.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Review/Comparison/Recomputations of Purchase Documents</li> <li>• Budgetary/Purchasing Accounting/Monitoring System</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees – Policies and Procedures Manuals</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Search for material unrecorded liabilities and/or encumbrances at year end. Refer to minutes and records immediately following the fiscal year cutoff date.

During the search for material unrecorded liabilities and/or encumbrances at year end, compare the date of the fiscal certificates with invoice dates, noting whether or not the certificate date precedes the invoice/obligation date and was recorded as an encumbrance in the proper year.

Note:

- The obligation date may precede the invoice date. If separately identified, use the obligation date when determining compliance.
- As interpreted by AOS Bulletin 1997-012, if the government does not expect to complete the project in the current year, the remainder of the project must be appropriated immediately in the subsequent year(s).

Inspect a representative number of “regular blanket” certificates outstanding near year end and determine that:

- The amount is established by an ordinance or resolution passed by a majority of the legislative body. (If the legislative authority passed this in the prior years, agree to permanent file documentation.)
- They are not dated after the fiscal year end.
- They do not exceed the amount the legislative body established.
- Only one certificate is outstanding per line item appropriation.

For subdivisions using “super blanket” certificates, inspect the certification of the fiscal officer and determine whether:

- The certificates were for professional services, fuel, oil, food items or any other specific recurring and reasonably predictable operating expense and,
- They do not run beyond the fiscal year (or quarterly spending plan, if a county adopted a plan).

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-3 Compliance Requirement:** Ohio Rev. Code §5705.40 - Amending or supplementing appropriations, contingencies.

**Summary of Requirements:** Any appropriation measure may be amended or supplemented if the entity complies with the same laws used in making the original appropriation. However, no appropriation may be reduced below an amount sufficient to cover all unliquidated and outstanding contracts or obligations against them. “Transfers” \* may be made by resolution or ordinance from one appropriation item to another. Subject to certain limitations, the annual appropriation measure may contain an appropriation for contingencies.

Rulings filed in the case of *C. B. Transportation, Inc. v. Butler County Board of Mental Retardation*, 60 Ohio Misc. 71, 397 N.E.2d 781 (C.P. 1979), as well as in *Burkholder v. Lauber*, 6 Ohio Misc. 152, 216 N.E.2d 909 (C.P. 1965), held that a board or officer whose judgment and discretion is required, was chosen because they were deemed fit and competent to exercise that judgment and discretion and unless power to substitute another in their place has been given, such board or officer cannot delegate these duties to another. Following such reasoning, a local government’s governing board would be prohibited from delegating duties statutorily assigned to it, such as the ability to amend appropriations as provided for in Ohio Rev. Code §5705.40.

Per AOS Bulletin 1997-010, budgeted expenditures coincide with either the final appropriations the legislative body passed prior to fiscal year-end or the sum of those final appropriations plus encumbrances carried forward from the prior year. *That is, the AOS does not recognize appropriation amendments retroactive to the prior year.* The statutory budget process codifies what are or should be good management practices. These processes provide a framework that helps management and legislators reasonably control spending.

\* “Transfers” in this context mean reallocations of appropriations within a fund. These do not refer to transfers of cash between funds.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Accounting system capable of recording appropriations and comparing them to actual results.</li> <li>• Reconciling appropriation totals to totals recorded in the accounting system.</li> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Comparison of Outstanding Encumbrances and Balances to Proposed Amendments</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Inquire (or determine from reading the minutes) if amended or supplemental appropriation measures have been passed.

Inspect the government’s records to determine if selected appropriation amendments were accurately and timely posted into an accounting system that integrates budget and actual receipts and disbursements. If the client uses a manual system (i.e. spreadsheets) determine if the manual system used by the client adequately tracks and compares budgetary data. Base the extent of this testing on the control environment, especially the CFO’s competence and dedication to complying with Ohio Revised Code requirements, past errors noted, etc.

Match appropriations amendments, supplements and intrafund appropriation “transfers” recorded in the accounting system with resolutions or ordinances.

*Note:* We suggest you test the general and other major / large funds and perhaps rotate a few smaller funds each audit.

- However, normally scanning the fund-accounting records and listing noncompliance as of year end is not time consuming. This should be a reliable test if evidence suggests the auditee accurately records all budgetary amendments into its accounting system, and if the system reports negative variances.
- Also consider including funds for which we reported noncompliance in the prior audit.

There is rarely a need to “recreate” the budget in the working papers. That is, we do not require a spreadsheet listing all funds’ estimated resources, appropriations (and amendments thereto), receipts, disbursements, and encumbrances.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**REQUIREMENTS OF REVENUE, FUNDS, AND TRANSFERS**

**1-4 Compliance Requirement:** Ohio Rev. Code §5705.09 and 5705.12 - Establishing funds and Permission to establish funds.

**Summary of Requirements:** Each subdivision must establish the following funds:

- General fund;
- Sinking fund whenever the subdivision has outstanding bonds other than serial bonds;
- Bond retirement fund, for the retirement of serial bonds, notes, or certificates of indebtedness;
- A special fund for each special levy;
- A special bond fund for each bond issue;
- A special fund for each class of revenues derived from a source other than the general property tax, which the law requires to be used for a particular purpose;
- A special fund for each public utility operated by a subdivision;
- A trust fund for any amount received by a subdivision in trust.

Additionally subdivisions should establish the funds described in Ohio Rev. Code §5705.121, 5705.13, 5705.131, 5709.43, 5709.75, and 5709.80 when applicable. Establishing these funds (or other funds statutes mandate) does not require Auditor of State authorization.

However, should a taxing authority desire to establish other funds not authorized in the Ohio Revised Code, they must obtain *approval of the Auditor of State*. The subdivision may provide by ordinance or resolution that money derived from special sources other than the general property tax shall be paid directly into such funds.

It is necessary to request the Auditor of State's permission to establish any fund not specifically authorized by statute or when the purpose of the fund is not identified in the Ohio Rev. Code, such as (but not limited to) §5705.09 (A) - (H). Situations requiring Auditor of State approval include:

- When management wishes to create a new fund in order to capture additional financial information about a specific source of revenue or a specific activity;
- When the fund will account for restricted gifts or bequests that will not be held in trust; and
- When management wants to impose internal restrictions on the use of otherwise unrestricted resources.

In some circumstances, the AOS deems the use of additional funds unnecessary and will not approve the request. See AOS Bulletin 1999-006 for additional information.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Presence of Effective Accounting System</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Periodic Reviews of Fund Ledgers</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Compare funds on the subdivision’s chart of accounts with funds that existed in the prior audit period.

For any new funds, apply the following steps:

- Inspect authority (e.g., board resolution) to establish the fund.
  - *Note: The legislative body of a local government may always specify, for management purposes, how they want specific resources spent. Absent any statutory restrictions on such resources, an internal purpose restriction does not justify the creation of a separate fund. New funds must be created based on the guidelines in AOS Bulletin 1999-006.*
- Determine code section under which established.
- If not established under State statute, inspect Auditor of State approval letters for funds created during the current audit period.
  - If a fund is not authorized under Ohio Rev. Code §5705.09 or another Ohio Rev. Code section and the entity did not receive Auditor of State approval to establish the fund, propose findings for adjustment to remove the unauthorized fund(s) and place the activity in the General Fund or other appropriate fund. *(If the fund was set up properly for GAAP purposes a finding for adjustment may not be necessary. Additionally, we will not apply this retroactively to funds existing from prior audit periods.)*
- Read ordinances and resolutions regarding how monies derived from special sources are to be used. Trace a representative number of receipts into the funds or accounts required by the ordinances or resolutions.

For funds existing in prior years, review the fund activity to determine whether the fund is still being used for the statutorily approved purpose. Consider whether the government has:

- Funds where the government is no longer using the fund for the purpose for which it was originally established and approved
- Funds that do not meet any fund type definition and do not have statutory authority (sometimes a government will have a fund it just should not have)
- Funds with no restricted/committed revenue source (except for Debt Service sinking funds where governments must make transfers from the General Fund to satisfy a sinking fund requirement)

AOS auditors that identify any of the situations described above should consult with Center for Audit Excellence and AOS Legal Division to determine whether a potential noncompliance citation or finding for adjustment to reclassify the activity back to the General Fund, or some other appropriate fund based on the facts and circumstances, should be made.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-5 Compliance Requirement:** Ohio Rev. Code §5705.05-.06, 5705.10, 5705.14(E), 5731.48, and 3315.20(A) - Distributing revenue derived from tax levies, proceeds from sale of bond issue, proceeds from sale of permanent improvement, and depositing estate taxes into the general fund.

**Summary of Requirements:**

- All revenue derived from the following must be paid into the general fund [Ohio Rev. Code § 5705.10, unless otherwise indicated below]:
  - the general levy for current expense within the ten mill limitation,
  - any general levy for current expense authorized by vote in excess of the ten mill limitation, and from sources other than the general property tax, unless its use for a particular purpose is prescribed by law (see the circumstances requiring a separate fund in the preceding OCS Step)
    - Counties are precluded from using general levy revenue for current expenses for the construction, reconstruction, resurfacing, and repair of roads and bridges. [Ohio Rev. Code §5705.05 & .06]. Other entities (except counties) may transfer general levy revenue for current expenses to Road and Bridge Funds via a resolution passed by a simple majority of the governing authority [Ohio Rev. Code §5705.14(E)] or may pay for these expenses directly from the General Fund [Ohio Rev. Code §5705.05 & .06].
  - Estate taxes received by a township or municipal corporation under Ohio Rev. Code § 5731.48
    - **Exceptions:**
      - Villages: (A)(2) To the general revenue fund of a village or to the board of education of a village, for school purposes, as the village council by resolution may approve;
      - Townships: (A)(3) To the general revenue fund or to the board of education of the school district of which the township is a part, for school purposes, as the board of township trustees by resolution may approve, in the case of a township.
      - Municipal Corporations: (D) If a municipal corporation is in default with respect to the principal or interest of any outstanding notes or bonds, one half of the [estate] taxes distributed under this section shall be credited to the sinking or bond retirement fund of the municipal corporation, and the residue shall be credited to the general revenue fund.
- All revenue derived from general or special levies for debt charges which is levied for the debt charges on serial bonds, notes, or certificates of indebtedness having a life less than five years, must be paid into the bond retirement fund. All such revenue which is levied for the debt charges on all other bonds, notes, or certificates of indebtedness is to be paid into the sinking fund [Ohio Rev. Code § 5705.10(B)].
- All revenue derived from a special levy is to be credited to a special fund for the purpose for which the levy was made [Ohio Rev. Code §5705.10(C)].<sup>15</sup>

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<sup>15</sup> Townships receiving distributions from the Gasoline Excise Tax Fund in the state treasury are permitted to use that money to pay debt service on State Infrastructure Bank obligations. (Ohio Rev. Code §§5531.10 and 5735.27)

- All revenue derived from a source other than the general property tax and which the law prescribes, shall be used for a particular purpose is to be paid into a special fund (see Section 1-4 for a listing of possible “special” funds) for such purpose [Ohio Rev. Code §5705.10(D)].
- All proceeds from the sale of public obligations or fractionalized interests in public obligations as defined in Ohio Rev. Code §133.01, *except premium and accrued interest*, are to be paid into a special fund for the purpose of such issue. Any interest earned on money in the special fund may be used for the purposes for which the indebtedness was authorized, or may be credited and used for an authorized fund or account [Ohio Rev. Code § 5705.10(E)].
- The *premium and accrued interest* received from the sale of public obligations or fractionalized interests in public obligations as defined in Ohio Rev. Code §133.01 is to be paid into the subdivision's sinking fund or the bond retirement fund [Ohio Rev. Code § 5705.10(E)].

**Note:** We wish to emphasize to governments and to their auditors the importance of complying with this. We have seen recent instances where investors desire interest payments exceeding market rates. They are willing to exchange the necessary up-front payment (*premium*) to obtain these returns in the future. When this occurs, debt proceeds will include the premium, which may be a substantial amount. If the debt is restricted for a capital project (for example), governments should *not* deposit the premium into a capital project fund. Instead, Ohio Rev. Code § 5705.10(E) prudently requires governments to deposit the premium in a sinking / bond retirement / debt service fund, to set aside amounts for the above-market interest payable over the debt's duration.

Depositing premiums (or accrued interest) into a fund other than the sinking / bond retirement would violate the requirements above, and be subject to a finding for adjustment, see AOS Bulletin 2014-001 for more information.

- If a board of education of a school district disposes of real property under Ohio Rev. Code § 3313.41, the proceeds received on or after September 29, 2013, from the sale shall be used to either:
  - Retire any debt that was incurred by the district with respect to that real property. Proceeds in excess of the funds necessary to retire that debt may be paid into the school district's capital and maintenance fund and used only to pay for the costs of nonoperating capital expenses related to technology infrastructure and equipment to be used for instruction and assessment fund, or
  - Paid into a special fund for the construction or acquisition of permanent improvements [Ohio Rev. Code § 5705.10(H)].
- If a park district enters into an agreement for the sale or lease of mineral rights regarding a park within the district, the royalties or moneys from that sale or lease must be deposited into a special fund created by the board of park commissioners to be used exclusively for the maintenance of parks within the District or for acquisition of new park lands [Ohio Rev. Code § 1545.23].

- If a permanent improvement of the subdivision is sold, the amount received from it shall be paid into the sinking fund, the bond retirement fund, or into a special fund for the construction or acquisition of permanent improvements [Ohio Rev. Code § 5705.10(F)].<sup>16</sup> However, after a county home has been closed as provided by Ohio Rev. Code § 5155.31, the board of county commissioners may sell or lease any part of the county home farm, and all receipts from such sales or leases shall be paid to the county treasurer and credited to the general county fund, and shall be subject to appropriation for such purposes as the board decides [Ohio Rev. Code § 5155.33].
- Proceeds from the sale of a public utility are to be paid into the sinking fund or bond retirement fund to the extent necessary to provide for the retirement of the outstanding indebtedness incurred in the construction or acquisition of such utility [Ohio Rev. Code § 5705.10(F)].
- Proceeds from the sale of property other than a permanent improvement are to be paid into the fund from which such property was acquired or is maintained, or if there is no such fund, into the general fund [Ohio Rev. Code § 5705.10(F)].
- Monies collected under Ohio Rev. Code § 4501.04, 5735.23, and 5735.27 must be deposited into a special fund for the purpose of street construction and maintenance. This includes gas tax and license taxes distributed through the county. However, if the municipal corporation sits on the line of the state highway system as designated by the director of transportation as an extension or continuance of the state highway then 7.5% of the monies will be posted to a state highway fund. [Ohio Rev. Code § 5735.28]

*Note:* Also, the \$5 or \$10 license taxes that can be levied by a municipality under Ohio Rev. Code Chapter 4504 can be receipted directly into a Permissive MVL fund.

- Money paid into a fund must be used only for the purposes for which such fund has been established. As a result, a negative fund cash balance<sup>17</sup> indicates that money from one fund was used to cover the expenses of another fund [Ohio Rev. Code § 5705.10(I)]. However, Ohio Rev. Code § 3315.20 provides an allowable exception for school districts. A school district may have a deficit in any special fund (see Section 1-4 for a listing of possible “special” funds) of the school district, but only if all of the following conditions are satisfied:

<sup>16</sup> Ohio Rev. Code § 5705.10(F) & (G), include an exception for certain townships, with a population greater than 15,000, having used township tax increment financing (TIF) for real property in the township according to the most recent federal decennial census. These townships may pay proceeds from the sale of a permanent improvement of the township into its general fund if both of the following conditions are satisfied: (see bullets below or on next page)

- The Township fiscal officer determines that all foreseeable “public infrastructure improvements” to be made in the township in the 10 years immediately following the date the permanent improvement is sold will have been financed through township TIF on or before the date of the sale. Written certification of this determination must be made part of the township’s records.
- The permanent improvement being sold was financed entirely from moneys in the township’s general fund.

<sup>17</sup> There is no legal authority addressing whether encumbrances are to be included when analyzing fund balances. Ohio Rev. Code § 5705.10 does not explicitly prohibit an entity from having a negative fund balance. Instead, we cite to Ohio Rev. Code § 5705.10 because restricted funds were used for other purposes. Therefore, do not include encumbrances when analyzing compliance with Ohio Rev. Code § 5705.10.

- The school district has a request for payment pending with the state sufficient to cover the amount of the deficit [Ohio Rev. Code § 3315.20(A)]
- There is a reasonable likelihood that the payment will be made [Ohio Rev. Code § 3315.20(A)]
- The unspent and unencumbered balance in the school district’s general fund is greater than the aggregate of deficit amounts in all of the school district’s special funds. [Ohio Rev. Code § 3315.20(B)]

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Presence of Effective Accounting System</li> <li>• Periodic Reviews/Comparisons of Budgeted and Actual Revenues</li> <li>• Independent Inspection/Comparison of Revenues to Source Documents</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

1. Trace a representative number of receipts from tax levies, bond issues, and sales of permanent improvements, to the funds. *Note:* Because recording receipts to an incorrect opinion unit is a misstatement, auditors should test these transactions to the extent required to reasonably assure there was no material misstatement. Also, auditors should consider reporting noncompliance for misposting to incorrect funds (rather than opinion units) as described in the *Finding for Adjustment* guidance in the *Ohio Compliance Supplement Implementation Guide*.
2. Trace selected estate tax proceeds to the credit of the municipality’s or township’s general fund. If in default on bonds or notes, municipalities should apportion 50% of the net proceeds each to the debt service and general funds.
3. Trace significant interest earned on bond proceeds to the credit of (1) a fund used for purposes for which the debt was authorized, or (2) the general fund. [Ohio Rev. Code § 5705.10(E)] (*Note:* Proceeds exclude accrued interest and premiums, which the entity must credit to the sinking or bond retirement fund. Refer to AOS Bulletin 2014-001) Also note that this interest may be subject to Federal arbitrage regulations—AOS staff should refer to the arbitrage procedures in the specimen debt audit program.

4. Inspect accounting ledgers or month end reports as of fiscal year end and for selected periods during the year. Determine whether significant negative fund balances existed.

*Note: When a fund ends the year with negative cash, it is inappropriate to present an “advance” on the budgetary statement to eliminate the negative cash fund balance. Even though, in substance, the government has made an advance, it is not acceptable to “hide” noncompliance by creating an advance not properly authorized by the government. However, a government should post an interfund receivable and payable to eliminate the negative cash balance on the GAAP financial statements. The government should select the fund to report the receivable.*

5. If negative fund balances are identified for a school district, determine whether the school district met the allowable exception conditions above by:
- *Inspecting* the school district’s Project Cash Request (PCR) forms. In most cases, these forms will be available for viewing online in ODE’s Comprehensive Continuous Improvement Plan (CCIP) application at <https://ccip.ode.state.oh.us/default.aspx?ccipSessionKey=634588550645675891>.
  - *Computing* the unspent and unencumbered balance in the school district’s general fund and vouching whether it is greater than the aggregate of deficit amounts in all of the school district’s special funds.
6. If a school district disposed of real property, determine whether the school district used the proceeds received from the sale to retire any debt that was incurred by the district with respect to that real property.

*Note:* The proceeds received from the sale shall be used to retire any debt that was incurred by the district with respect to that real property. Proceeds in excess of the funds necessary to retire that debt may be paid into the school district's capital and maintenance fund and used only to pay for the costs of nonoperating capital expenses related to technology infrastructure and equipment to be used for instruction and assessment fund, or payment into a special fund for construction or acquisition of permanent improvements.

7. If a park district enters into an agreement for the sale or lease of mineral rights regarding a park within the district, confirm that the royalties or moneys from that sale or lease were deposited into a special fund created by the board of park commissioners.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-6 Compliance Requirements:** Ohio Rev. Code §5705.05-.06, 5705.14, 5705.15, and 5705.16 - Transfer of funds.

(Refer to Appendix A-1 in the OCS Implementation Guide for a more detailed discussion on what constitutes a “transfer” under Ohio Rev. Code §5705.14 - .16.)

**Summary of Requirements:** No transfer can be made from one fund of a subdivision to any other fund, except as follows:<sup>18</sup>

- The unexpended balance in a bond fund [i.e. a capital project fund financed with bond proceeds] that is no longer needed for the purpose for which such fund was created shall be transferred to the sinking fund or bond retirement fund from which such bonds are payable. [Ohio Rev. Code § 5705.14(A)]
- The unexpended balance in any specific permanent improvement fund, other than a bond fund, after the payment of all obligations incurred in the acquisition of such improvement, shall be transferred to the sinking fund or bond retirement fund of the subdivision. However, if such money is not required to meet the obligations payable from such funds, it may be transferred to a special fund for the acquisition of permanent improvements, or, with the approval of the court of common pleas of the county in which such subdivision is located, to the general fund of the subdivision. [Ohio Rev. Code § 5705.14(B)]
- Except as provided below, the unexpended balance in the sinking fund or bond retirement fund of a subdivision, after all indebtedness, interest, and other obligations for the payment of which such fund exists have been paid and retired, shall be transferred, in the case of the sinking fund, to the bond retirement fund, and in the case of the bond retirement fund, to the sinking fund. However, if the transfer is impossible by reason of the nonexistence of the fund to receive the transfer, the unexpended balance may be transferred to any other fund of the subdivision with the approval of the court of common pleas of the county in which such division is located. [Ohio Rev. Code § 5705.14(C)(1)]
  - Money in a bond fund or bond retirement fund of a city, local, exempted village, cooperative education, or joint vocational school district may be transferred to a specific permanent improvement fund provided that the county budget commission of the county in which the school district is located approves the transfer upon its determination that the money transferred will not be required to meet the obligations payable from the bond fund or bond retirement fund. In arriving at such a determination, the county budget commission shall consider the balance of the bond fund or bond retirement fund, the outstanding obligations payable from the fund, and the sources and timing of the fund's revenue. [Ohio Rev. Code § 5705.14(C)(2)]
- The unexpended balance in any special fund, other than an improvement fund, may be transferred to the general fund or to the sinking fund or bond retirement fund after the termination of the activity, service, or other undertaking for which such special fund existed, but only after the payment of all obligations incurred and payable from such special fund. [Ohio Rev. Code § 5705.14(D)]

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<sup>18</sup> GASB 2300.127 (and therefore OCBOA presentations) requires certain disclosures regarding the amounts and purposes of transfers in the notes to the financial statements.

- Money may be transferred from the general fund to any other fund of the subdivision [Ohio Rev. Code § 5705.14(E)]. *Note:* 1989 Op. Atty. Gen. No. 89-075 requires a governing board resolution passed by a simple majority of the board members to transfer funds.<sup>19</sup>
  - Counties are precluded from transferring general levy revenue for current expenses to other county funds for the construction, reconstruction, resurfacing, and repair of roads and bridges. [Ohio Rev. Code §5705.05 & .06]. Other entities (except counties) may transfer general levy revenue for current expenses to Road and Bridge Funds via a resolution passed by a simple majority of the governing authority [Ohio Rev. Code §5705.14(E)].
- Moneys retained by a county in accordance with Ohio Rev. Code § 4501.04 (auto registration distribution fund), or in accordance with Ohio Rev. Code § 5735.27 (gasoline excise tax fund), may be transferred from the fund into which they were deposited to the sinking fund or bond retirement fund from which any principal, interest, or charges for which such moneys may be used is payable. [Ohio Rev. Code § 5705.14(F)]
- Moneys retained or received by a municipal corporation under Ohio Rev. Code § 4501.04 (motor vehicle license tax), or division (A) (1) or (2) of Ohio Rev. Code § 5735.27 (motor vehicle fuel excise taxes), may be transferred from the fund into which they were deposited to the sinking fund or bond retirement fund from which any principal, interest, or charges for which such moneys may be used is payable. [Ohio Rev. Code § 5705.14(G)]
- After payment of the expenses of conducting and managing the water works, any surplus of a municipal corporation's water fund may be applied to the repairs, enlargement, or extension of the works or of the reservoirs, the payment of the interest of any loan made for their construction, or for the creation of a sinking fund for the liquidation of the debt. In those municipal corporations in which water works and sewerage systems are conducted as a single unit, under one operating management, a sum not to exceed ten per cent of the gross revenue of the water works for the preceding year may be taken from any surplus remaining after all of the preceding purposes have been cared for and may be used for the payment of the cost of maintenance, operation, and repair of the sewerage system and sewage pumping, treatment, and disposal works and for the enlargement or replacement thereof. Each year a sum equal to five per cent of the gross revenue of the preceding year shall be first retained from paid surplus as a reserve for waterworks purposes. The amount authorized to be levied and assessed for waterworks purposes shall be applied by the legislative authority to the creation of the sinking fund for payment of any indebtedness incurred for the construction and extension of water works and for no other purposes; provided, where such municipal corporation does not operate or maintain a water works or a sewage pumping, treatment, and disposal works, any or all such surplus may be transferred to the general fund of the municipal corporation in the manner provided for in sections 5705.15 and 5705.16 of the Revised Code<sup>20</sup>. [Ohio Rev. Code § 743.05]

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<sup>19</sup> AOS interprets this requirement to mean that a governing board may approve interfund transfers from the general fund to other funds of the subdivision within its annual appropriation measure provided that the measure was passed by a simple majority of the board members.

<sup>20</sup> In other words, if there is an excess in the water works fund and the municipality has its own water works operation, the excess can only be used for expenses related to the operation, maintenance, or expansion of the waterworks. Not all municipalities have their own waterworks system. Therefore, some municipalities may provide water to their residents by obtaining the water from another source. Where this is the case, if (after satisfying expenses related to furnishing water) there is an excess, the municipality may transfer the excess to its general fund.

- Money may be transferred from the County Developmental Disabilities general fund to the County Developmental Disabilities capital fund established under Ohio Rev. Code § 5705.091, or to any other fund created for purposes of the County Board of Developmental Disabilities so long as it is spent for the particular purpose of the transfer. An unexpended balance in an account may be transferred back to the County Developmental Disabilities general fund. Transfers shall be done by resolution of the Board of County Commissioners. [Ohio Rev. Code §5705.14(H)]
- Money may be transferred from the public assistance fund established under section 5101.161 of the Revised Code to either of the following funds, so long as the money to be transferred from the public assistance fund may be spent for the purposes for which money in the receiving fund may be used [Ohio Rev. Code §5705.14(I)]:
  - (1) The children services fund established under Ohio Rev. Code § 5101.144;
  - (2) The child support enforcement administrative fund established, as authorized under rules adopted by the director of job and family services, in the county treasury for use by any county family services agency.
- Money may be transferred among various funds and accounts from which a loss was directly attributable to allocate insurance and self-insurance program costs, including deductibles, under Ohio Rev. Code § 2744.08 and 2744.082. If a subdivision or joint self-insurance pool makes such an allocation or requires the payment of deductibles from specific funds or accounts, the subdivision's fiscal officer, pursuant to an ordinance or resolution of the subdivision's legislative authority, must transfer amounts equal to those costs or deductibles from the funds or accounts to the subdivision's general fund if both of the following apply:
  - (1) the subdivision requests payment from the employee responsible for the funds or accounts for those costs or deductibles [Ohio Rev. Code § 2744.082(A)(1)], and
  - (2) the employee receiving the request fails to remit payment within 45 days after the date the request is received [Ohio Rev. Code § 2744.082(A)(2)].
- Except in the case of transfers from the general fund, transfers can be made only by resolution of the taxing authority passed with the affirmative vote of two thirds of the members. Transfers from the general fund require a resolution passed by a simple majority of the board members (i.e., a two thirds vote is not required for general fund transfers though a resolution passed by a simple majority is required. A simple majority constitutes a quorum of greater than 50% of the members.) [Ohio Rev. Code § 5705.14 & .16]

Per Ohio Rev. Code § 5705.15 & .16: In addition to the transfers listed above, which Ohio Rev. Code § 5705.14 authorizes, the taxing authority of any political subdivision, with the approval of the Court of Common Pleas<sup>21</sup>, may transfer from one fund to another any public funds under its supervision, *except* the proceeds or balances of:

- loans,
- bond issues,
- special levies for the payment of loans or bond issues,
- the proceeds or balances of funds derived from any excise tax levied by law for a specified purpose, and
- the proceeds or balances of any license fees imposed by law for a specified purpose.

<sup>21</sup> Under Ohio Rev. Code § 5705.16, approval of the Tax Commissioner is also required in certain circumstances.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Periodic Reviews/Comparisons of Budgeted and Actual Transfers</li> <li>• Independent Inspection/Comparison of Transfers to Source Documents</li> <li>• Knowledge and Training of personnel</li> <li>• Presence of Effective Accounting System</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

*Note:* Except for “prior approval by the governing authority,” transfers fail the “existence” assertion unless they satisfy the aforementioned legal requirements. Therefore, noncompliant transfers (e.g., material transfers from the self-insurance fund that are unsupported or transfers that permit spending the transferred amount in violation of its restricted purpose) represent misstatements and may require findings for adjustment. See Appendix A-1 in the *OCS Implementation Guide* for more information on determining allowability for Transfers and Advances. Auditors should also refer to the finding for adjustment guidance in the Ohio Compliance Supplement *Implementation Guide*.

Inspect documents authorizing transfers during the audit period and determine that transfers involving balances described below met the requirements above:

- Unexpended bond balance;
- Permanent improvement balance;
- Bond retirement;
- Special fund;
- Auto registration;
- Resolution;
- Municipal corporation (motor vehicle license tax, motor vehicle fuel excise tax, water works);
- Public assistance;
- Developmental disabilities.

Determine if any material transfers were made from the proceeds or balances of:

- loans,

- bond issues,
- special levies for the payment of loans or bond issues,
- the proceeds or balances of funds derived from any excise tax levied by law for a specified purpose, or
- the proceeds or balances of any license fees imposed by law for a specified purpose.

Determine if selected transfers were authorized by vote of the governing board as described above.

If applicable, determine if selected transfers were authorized by the County Budget Commission, Court of Common Pleas, or Tax Commissioner as described above.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-7 Compliance Requirement:** AOS Bulletin 1997-003 and various ORC sections – Advances.

Though no statutory provisions directly address inter-fund *advances*, the following requirements are in part derived from Ohio Rev. Code §: 5705.10 (restriction on the purpose for which funds may be used); 5705.14, 5705.15, and 5705.16 (transfer of funds); 5705.39 (appropriations limited to estimated resources); 5705.41 (restriction on appropriation/ expenditure of money); and 5705.36 (certification of available revenue). AOS Bulletin 1997-003 sets forth the requirements for inter-fund advances and provides additional guidance for recording such transactions.

**Note:** This section applies when a subdivision purchases its own debt with its debt service fund cash, etc. pursuant to Ohio Rev. Code § 133.29 and accounts for it as *advances* and *interfund activity* in its financial statements. However, refer to OCS section 1-1645 if the subdivision accounts for a purchase of its own debt as an *investment* and *debt*. See AOS Bulletin 1997-001, Ohio Rev. Code § 133.03 and 133.29, and Appendix A-1 of the *OCS Implementation Guide* for additional guidance on legal requirements applicable to intra-entity borrowing. Ohio Compliance Supplement Chapter 1, section 1-1645 describes the legal compliance requirements for the issuance and retirement of manuscript debt.

**Summary of Requirements:** Inter-fund cash advances may be a desirable method of resolving cash flow problems without the necessity of incurring additional interest expense for short-term loans and to provide the necessary "seed" for grants that are allocated on a reimbursement basis. The intent for cash advances is to require repayment within the current or succeeding year. Inter-fund cash advances are subject to the following requirements:

- Any advance must be clearly labeled as such, and must be distinguished from a transfer. Transfers are intended to reallocate money permanently from one fund to another and may be made only as authorized in Ohio Rev. Code §§5705.14 to 5705.16. Advances, on the other hand, *temporarily* reallocate cash from one fund to another and involve an expectation of repayment;
- In order to advance cash from one fund to another, there must be statutory authority to use the money in the fund advancing the cash (the "creditor" fund) for the same purpose for which the fund receiving the cash (the "debtor" fund) was established;
- The debtor fund may repay advances from the creditor fund. That is, the AOS would not deem repaying advances to violate restrictions on use of the debtor's fund resources; and
- Advances must be approved by a formal resolution of the taxing authority of the subdivision which must include:
  - A specific statement that the transaction is an advance of cash, and
  - An indication of the money (fund) from which it is expected that repayment will be made.
- When a fund ends the year with negative cash, it is not appropriate to present an *advance* on the budgetary statement to eliminate the negative cash fund balance. Even though, in substance, the government has made an advance, it is not acceptable to "hide" noncompliance by creating an advance not properly authorized by the government. However, the government should post an interfund receivable and payable to eliminate the negative cash balance on the GAAP financial statements. The government should select the fund to report the receivable.

Other Budgetary Considerations

The advances-out (initial loan and repayment) in the creditor (loaning) and debtor (borrowing) funds do not require appropriation as advances represent temporary allocations of resources. However, an amended official certificate of estimated resources should be obtained to reflect the reduced fund balance in the creditor fund and the increased fund balance in the debtor fund. Creditor fund appropriations must be evaluated based on the reduced estimated resources, and appropriation reductions may be required. Prior to obligation of advanced funds, the debtor fund must have sufficient appropriations to cover the anticipated expenditures.

Additionally, when a cash advance is outstanding at the beginning of a fiscal year in which repayment is expected, an adjustment is required to the total resources available for expenditure in the creditor and debtor funds. The unencumbered cash balance of the creditor fund must be increased by the amount of repayment expected during the fiscal year to produce the “carryover balance available for appropriation.” Similarly, the unencumbered cash balance in the debtor fund must be reduced by the amount of repayment expected during the fiscal year to produce “carryover balance available for appropriation.” This adjustment is made on the “certificate of the total amount from all sources available for expenditures, and balances” filed with the County Budget Commission pursuant to Ohio Rev. Code § 5705.36.

The official certificate of estimated resources must be prepared and provided in cases in which the Budget Commission waives the requirement that the taxing authority of a subdivision adopt a tax budget. Ohio Rev. Code §5705.281(A) indicates the county budget commission by an affirmative vote of a majority of the commission, including an affirmative vote by the county auditor, may waive the requirement that the taxing authority of a subdivision or other taxing unit adopt a tax, but the taxing authority is still required to provide information to the commission in order for it to perform its duties, including dividing the rates of each of the subdivision’s or taxing unit’s tax levies. In addition, Ohio Rev. Code §5705.34 requires the budget commission to certify its action to the taxing authority. Ohio Rev. Code §5705.35(A) makes reference to “[t]he certification of the budget commission to the taxing authority of each subdivision or taxing unit, as set forth in section 5705.34 of the Revised Code...”, and indicates that “[t]here shall be attached to the certification a summary, which shall be known as the ‘official certificate of estimated resources,’ that shall state the total estimated resources of each fund of the subdivision that are available for appropriation in the fiscal year...”.

Conversion to a Transfer

If, after an advance is made, the taxing authority determines that the transaction should, in fact, be treated as a transfer (repayment is no longer expected) the following procedures should be followed retroactively:

- The necessary formal procedures for approval of the transfer should be completed including, if necessary, approval of the commissioner of tax equalization and of the court of common pleas (see Ohio Rev. Code §5705.14, 5705.15 and 5705.16);
- The transfer should be formally recorded on the records of the subdivision; and
- The entries recording the cash advance should be reversed.

Accounting for Manuscript Debt as an Advance and Interfund Activity

Before a taxing authority sells any securities of the subdivision to others, the taxing authority may offer the securities at their purchase price and accrued interest to the officer or officers who have charge of the bond retirement fund of the subdivision, or in the case of a municipal corporation, to the treasury investment board for investment under §731.56 of the Ohio Rev. Code, or an officer or similar treasury investment board having the authority under a charter. (Ohio Rev. Code §133.29(A)) This type of debt is often referred to as “manuscript debt”. See the Manuscript Debt section in chapter 1 for more information.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Presence of Effective Accounting System</li> <li>• Independent Inspection/Comparisons of Advances and Source Documentation</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

If advance transactions occurred, review authorizing legislation and accounting records. Determine whether the advance transactions were in amounts and between accounting funds approved in the authorizing legislation.

Based on knowledge of the entity’s operations and review of levy legislation or other appropriate documents, determine whether the creditor fund’s purpose was reasonably consistent with the debtor fund’s purpose.

Determine whether prior period advances are outstanding. If advances have not been repaid within a reasonable period or within the period specified (if any) in the authorizing legislation, determine through inquiry of appropriate client officials when the advance will be repaid.

If the client no longer intends for the advance to be repaid or repayment is unlikely, issue a finding for adjustment if the amounts are material and the client does not take appropriate steps to convert the advance to a transfer following the above procedures.

If advances have been converted to transfers, determine whether the transfer requirements summarized in Ohio Compliance Supplement Section 1-6 have been complied with retroactively.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-8 Compliance Requirement:** Ohio Rev. Code §5705.13 and 5705.132 - Reserve balance accounts and funds.

- Ohio Rev. Code §5705.13(A) - Reserve balance accounts and funds;
- Ohio Rev. Code §5705.13(B) – A special revenue fund may be established to accumulate cash for severance payments or salaries when the number of pay periods exceeds the usual and customary number for a year;
- Ohio Rev. Code § 5705.13(C) – capital projects fund(s) may be established to accumulate resources to acquire, construct, or improve fixed assets;

**Summary of Requirements:**

1. Ohio Rev. Code §5705.13(A) allows a taxing authority of a subdivision to establish, by resolution, a reserve balance account<sup>22</sup> for each of the three following purposes:
  - a) Budget stabilization: may be created in the general fund or in any special fund used for operating purposes. The amount reserved in the account in any fiscal year must not exceed 5% of the fund's revenue for the preceding fiscal year<sup>23</sup>. The reserve balance is excluded from the unencumbered balance when certifying available balances at year-end. The reserve for budget stabilization may be reduced or eliminated at any time by the taxing authority.
  - b) Self-insurance program: may be created in the general fund or in the internal service fund established to account for the operation of the program. The amount to be reserved must be based on actuarial principles and the taxing authority may rescind the reserve balance account at any time.
  - c) Retrospective Ratings Plan for Workers' Compensation<sup>24</sup>: may be created in the general fund or in the internal service fund established to account for the program. The amount to be reserved must be based on actuarial principles and the taxing authority may rescind the reserve balance account at any time.
2. Ohio Rev. Code § 5705.13(B) allows a taxing authority to establish a special revenue fund to accumulate cash to pay accumulated leave, or for paying salaries when the number of pay periods exceeds the usual and customary number for a year. This leave includes payments for accumulated sick leave and vacation leave, or for payments in lieu of taking compensatory time off, upon the termination of employment or retirement. Money may be transferred to this fund from any fund from which the termination or salary payments could lawfully be made. The

<sup>22</sup> Ohio Rev. Code §5705.13 refers to these accounts as "reserve" accounts. However, for the GASB 54 financial reporting AOS Bulletin 2011-004 describes, the criterion for using the budget stabilization is not specific enough to meet the *committed* criteria and it does not meet the *restricted* criteria as the budget stabilization is not mandated by State statute. Therefore, a budget stabilization/reserve account should be reported as *unassigned* in the general fund. While statute also gives the authority to have stabilization reserve accounts in other operating funds, the fund balance is reported as *restricted, committed, or assigned* and the reserve account does not change the fund balance classification. Entity wide statements should report these as part of *unrestricted* net assets.

<sup>23</sup> In the case of a reserve balance account of a county or of a township, the budget stabilization amount can be the greater of 5% of the fund's revenues from the preceding fiscal year or one-sixth of the expenditures during the preceding fiscal year from the fund in which the account is established. [Ohio Rev. Code § 5705.13 (A) (3)]

<sup>24</sup> Various plans to provide for the payment of claims, assessments, and deductibles are allowed. Plans allowed are: payments under a self-insurance program, individual retrospective ratings plan, group rating plan, group retrospective rating plan, medical only program, deductible plan, or large deductible plan for workers' compensation.

reserve must be established by resolution or ordinance and the taxing authority may rescind the fund at any time with the accumulated resources being returned to the fund from which they came. Amounts accumulated in this fund should be reasonable based on the taxing authority's estimated liability for benefits.

3. Ohio Rev. Code § 5705.13(C) provides that a taxing authority may create, by resolution, one or more capital projects funds<sup>25</sup> to accumulate resources for the acquisition, construction, or improvement of fixed assets, including motor vehicles. Each fund must be created by ordinance or resolution. The resolution or ordinance must identify the asset(s) to be acquired, the amount needed to be accumulated, the period over which the amount will be accumulated (with a limit of ten years from the date of the resolution or ordinance), and the source of the resources. Despite Ohio Rev. Code §5705.14 through .16, money may be transferred to the capital projects fund from any other fund that could acquire, construct or improve the fixed assets. If a contract for the fixed asset(s) has not been entered into before the ten-year period expires, the money is returned to the fund from which it was transferred or that was originally intended to receive it. The taxing authority may rescind a capital projects fund at any time with the accumulated resources being returned to the fund from which they came. Auditor of State approval is not required for this transfer.
4. Ohio Rev. Code §5705.132 permits *townships* to establish by resolution reserve balance accounts in addition to those described above to accumulate currently available resources for any purpose for which the board of township trustees may lawfully expend township money.<sup>26</sup> The resolution must state the:
  - Specific purpose for which a reserve balance account is established,
  - Fund within which it is established,
  - Fund or account from which money will be transferred to it,
  - Number of years it will exist [there is a five year cap on how long the account may be in existence]
  - Maximum total amount of money that may be credited to it during its existence; and
  - Maximum amount of money to be credited to it each fiscal year it exists

Reserve balance accounts established under this authority may exist for not more than five years beginning with the year in which money is first set aside. In addition, money in such an account can be expended only for the purpose for which the account is established.

Money may be transferred to these new reserve balance accounts from another township fund or account only if money in that fund or account may lawfully be expended for the purpose for which the new reserve balance account is created. Townships may create more than one reserve balance account under this section. However, the total amount of money credited to *all* of the reserve balance accounts established under this section cannot exceed, ***at any time in any fiscal***

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<sup>25</sup> Similar to the preceding note, governments should report these amounts as *committed, assigned, or restricted fund* balance as appropriate under the circumstances described in GASB 54 in governmental fund statements. Entity wide statements should report this equity as part of *unrestricted net assets*, because the restrictions are not externally imposed.

<sup>26</sup> Similar to reserve balance accounts created under existing law, reserves created under this section are not considered as an unencumbered balance or revenue of the township for purposes of annual budget reviews by the county budget commission. They are also not considered as an unencumbered balance or revenue for purposes of apportioning the county's undivided local government fund and the undivided local government revenue assistance fund.

year, 5% of the total of the township’s revenue from all sources for the preceding fiscal year, plus any unencumbered balances carried over to the current fiscal year from the preceding fiscal year. There are three important aspects of this restriction. First, be aware that it is based on revenues only. Other financing sources such as debt proceeds or transfers will not count toward the calculation of the limitation.<sup>27</sup> Second, recognize that this language has the effect of allowing the same dollars to be counted twice in calculating the limitations, first when they were received in the prior year and second to the extent they are carried over as unencumbered into the current year. Finally, notice that the amount of the limitation changes each year because it is based on the preceding year’s revenues.

If a township does not expect to spend the money set-aside in a reserve balance account in the upcoming year, the money in the reserve balance account need not be included in the certificate of year-end balances filed with the budget commission at the beginning of the year. If the township plans to spend the money that has been set aside, the township should include the money in the certificate of year-end balances. The money will then be included in the amended certificate of estimated resources and may be appropriated and spent during the year. Appropriations should be made to an account that reflects the purpose of the reserve. Appropriations should not be made to, nor expenditures made from, a reserve balance account. For example, assume in 2006 a township created a reserve balance account not to exceed \$40,000 in the motor vehicle license tax fund to purchase a new mower. \$10,000 is set aside each year from 2006 through 2009. In 2010, the \$40,000 is included in the certificate of year-end balances and appears as part of the amended certificate. The money is appropriated in the capital outlay account in the motor vehicle license tax fund and the new mower is purchased.<sup>28</sup>

Upon the expiration or rescission of a reserve balance account created under this section, any unexpended balance in the reserve account must be transferred to the fund or account from which money in the account was originally transferred. If money was transferred from multiple funds or accounts, a pro rata share of the unexpended balance must be transferred to each of them proportionate to the amount originally transferred from that fund or account.

Refer to AOS Bulletin 2007-002 for additional information regarding the authority for townships to create reserve balance accounts.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of</li> </ul>		

<sup>27</sup> Appendix IV-5 of the March ~~2015~~ 2014 Ohio Township Handbook lists all *Other Financing Sources*.

<sup>28</sup> For the purpose of setting aside money for the purchase of a capital asset, it may be easier and more convenient to create a separate capital projects fund under the provisions of Ohio Rev. Code § 5705.13.

changes in laws and regulations to employees		
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**Suggested Audit Procedures - Compliance (Substantive) Tests:**

If reserve balance accounts have been established:

- Determine through vouching, review of minutes, and inspection of accounting ledgers and authorizing legislation, whether reserve accounts were only established in the general fund, special fund used for operating purposes or appropriate internal service fund and for permitted purposes (budget stabilization, self-insurance program, or retrospective ratings program for worker’s compensation).
- Recalculate reserve percentages and inspect worksheets and accounting ledgers to determine whether the amount reserved exceeded the 5 % cap (budget stabilization account). In the case of Townships or Counties see footnote 23.
- For self-insurance and worker’s compensation reserve accounts, compare amounts reserved to estimates received from the entity’s actuary.

If a “severance payout reserve” or “capital improvement reserve” fund has been established:

- Review minutes, ordinances and resolutions to determine whether the fund has been established by resolution or ordinance.
- If a capital improvement reserve fund has been established, review the authorizing legislation to determine whether the assets; amount required; accumulation period (not to exceed ten years); and source of funding have been identified.
- Select a representative number of disbursement transactions from the fund. Through vouching, determine whether the transactions were only for related activities as indicated above, and in accordance with the purpose stated in the authorizing legislation.
- Trace a representative number of transfers to the reserve fund and determine whether the transfers were from funds permitted to make the disbursements for which the reserve fund was established.
- Determine through inspection of worksheets, ledgers and other such documents, whether records reasonably provide for the return of accumulated resources, to the fund from which they were originally transferred or the fund intended to receive them (If records do not reasonably provide for the proper return of resources, this situation would generally result in a recommendation; a noncompliance citation should not be made).

If the reserve fund was rescinded or if the ten-year period has elapsed prior to entering into a contract (capital improvement reserve fund), determine through inspection of worksheets and accounting ledgers whether the accumulated resources were returned to the fund from which they were originally transferred or the fund intended to receive them.

If a township has established an additional reserve balance account(s), determine whether the necessary resolution, stating the purpose of the reserve account, has been adopted by the board of trustees.

- Review monies transferred to the new township reserve balance accounts from other township funds or accounts and determine whether those monies may lawfully be expended for the purpose for which the new reserve balance account was created.
- Determine whether the total amount of money credited to *all* of the reserve balance accounts established under Ohio Rev. Code § 5705.132 exceeded 5% of the total of the township's revenue from all sources for the preceding fiscal year and any unencumbered balances carried over to the current fiscal year from the preceding fiscal year.
- Determine whether reserve accounts were only used for the purpose for which the account(s) was established.
- Determine that none of the additional reserve balance accounts have existed for more than five years.
- Upon the expiration or rescission of a reserve balance account created under Ohio Rev. Code § 5705.132, determine whether any remaining unexpended balance in the reserve account was transferred to the fund or account from which money in the account was originally transferred. If not, consider a finding for adjustment.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**ADDITIONAL COUNTY REQUIREMENTS**

**1-9 Compliance Requirement:** Ohio Rev. Code § 5101.144 - County Children Services Fund

**Summary of Requirements:** Requires that each county deposit all funds its public children services agency receives, regardless of source, into a special fund in the county treasury known as the children services fund.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

During revenue tests, trace a representative number of children services agency receipts to the fund.

<p><b>Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):</b></p>
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**BOARD OF EDUCATION (SCHOOLS)**

**1-10 Compliance Requirement:** Ohio Rev. Code § 3313.33 - **Board of Education** (schools) conveyances and contracts.

**Summary of Requirement:** The board president and treasurer shall execute any “Conveyances.” No contract is binding unless authorized at a regular or special board meeting. A “conveyance” is not a donation; it is a transfer *between two entities* with adequate consideration other than money.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Trace board approval from the minutes to the contracts or from the contracts to the minutes.

Inspect “conveyances” for board president and treasurer signatures.

<p><b>Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):</b></p>
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**Revised: HB 64, 131<sup>st</sup> GA**  
**Effective: 9/29/15**

**1-11 Compliance Requirement:** Ohio Rev. Code Chapter 3318 (Traditional School Districts) and section 501.10 Am. Sub. House Bill 64 (Community Schools) participating in classroom facilities assistance programs.

### Summary of the Program

#### Background:

Several programs provide financial assistance to construct or repair classroom facilities. The School Facilities Commission (Commission) administers these programs. The most common programs are the Classroom Facilities Assistance Program (CFAP), Community School Classroom Facilities Grant Project, Expedited Local Partnership Program, and Urban Initiative Program (i.e., applies to the following six city school districts: Akron, Cincinnati, Cleveland, Columbus, Dayton, and Toledo). Certain classroom assistance programs established by Ohio Rev. Code Chapter 3318 follow the basic guidelines of the CFAP.

#### Traditional School Districts:

#### Locally Funded Initiatives:

The Commission informed us that a school district board may elect to add to the scope of any project and separately fund a scope of work (“local initiative”), which involves improving all or part of a project the Commission funds. The school district board may request the Commission to approve the incorporation of design and construction of the local initiative into the overall project. Whenever a local initiative is interconnected with a project the commission funds, the district and the commission will execute a memorandum of understanding to specify the additional cost of the local initiative and the terms and conditions for accounting for the cost. *The district must account for the local initiative in a separate fund, NOT the project construction fund (USAS fund 010).*

The CFAP and related programs are discussed below.

#### CFAP Basics:

CFAP participation is based in part on the district’s relative wealth, the Commission’s determination of the district’s facility needs, and the time elapsed since prior CFAP participation.

Project commencement is contingent upon the district obtaining:

- The district’s share of project costs, funded by an additional bond levy, and /or certain local resources available for such purpose [Ohio Rev. Code §3318.084], or
- The proceeds of a property tax/income tax levy, or a combination of both [Ohio Rev. Code §3318.052], and

- The Board must levy an additional maintenance tax<sup>29</sup> of at least one-half mill [Ohio Rev. Code §3318.05 (B), 3318.06 (A)(2)(a) and (A)(3), and 3318.17], or
- The Board may elect, to satisfy its local maintenance requirement by earmarking from the proceeds of an existing permanent improvement tax levied under Ohio Rev. Code §5705.21, an amount equivalent to the amount of the additional tax described above or the District may elect to satisfy its local maintenance requirement by a combination of the half mill levy and the alternative funding source, or the district may elect to use a locally donated contribution under section 3318.084 of the Rev. Code. [Ohio Rev. Code § 3318.05 (B), and 3318.06 (A)(2)(b)]
  - A district may deposit into its maintenance fund, annually for 23 years, an amount from other district resources equal to 1/2 mill of the district's tax valuation<sup>30</sup>, instead of levying the maintenance tax<sup>31</sup>. The district's board must pass a resolution petitioning the Ohio School Facilities Commission to approve the arrangement. (Ohio Rev. Code § 3318.05, 3318.051, and 3318.084)
  - The district treasurer must annually certify to the Commission and the Auditor of State that the amount required for the year has been transferred<sup>32</sup> into the maintenance fund.

In order to satisfy the transfer certification requirement to the Auditor of State, districts can electronically submit the copy of the Auditor of State's certification to [OSFC@OhioAuditor.gov](mailto:OSFC@OhioAuditor.gov) or carbon copy the Auditor of State regional offices on their certification to the Commission. See the Auditor of State website [www.ohioauditor.gov](http://www.ohioauditor.gov) (Contact Us/Locations and Contacts) for regional office contact information.

<sup>29</sup> The original regulations required a ½ mill levy, all of which was remitted to the State to repay project funding received. Later regulations still required the levy (or other funding), but provided that all or a portion would be retained by the district, to be used for maintenance of project facilities. All such funding is referred to as "maintenance funding" in this OCS Section. Some districts have entered into supplemental agreements which subject the district to the amended regulations.

<sup>30</sup> Joint vocational school districts participating in a state facilities program, annually for 23 years, must deposit into a maintenance account an amount equal to 1.5% of the current insurance value of the acquired facilities (Ohio Re. Code § 3318.43).

<sup>31</sup> If a district board determines that it can no longer continue making the annual transfers, the act allows a district board to rescind its decision, but only if the district's voters approve the levy of a maintenance tax. The levy must be in effect for the remainder of the 23-year maintenance period (23 years minus the number of years that the district made transfers) and must be for not less than ½ mill for each dollar of district valuation. The act prescribes the ballot language to be used. A district electing to make the transfers authorized by the act is not relieved from its obligation to make annual deposits into its general "capital and maintenance fund," which applies to all districts under continuing law.

<sup>32</sup> Districts electing to make the transfers, instead of levying the maintenance tax, may not receive the new state maintenance equalization payments. (*Beginning in fiscal year 2007, the Ohio Department of Education is required to pay an equalized subsidy to city, exempted village, and local school districts participating in state-assisted facilities programs and have tax valuations per pupil below the statewide average. The subsidy equalizes to the statewide average the per pupil amount each eligible district raises from its 1/2-mill maintenance levy.*) (Ohio Rev. Code § 3318.18)

- The Auditor of State must “verify” the transfer as part of any audit of the district. If the Auditor of State finds that less than the required amount has been deposited, the Auditor must notify the district board in writing and require the board to deposit the necessary money within 90 days after the notice. If the district board fails to demonstrate to the Auditor's satisfaction that it has made the required deposit, the Auditor must notify the Ohio Department of Education. Upon that notice, the Ohio Department of Education must withhold 10% of the district's state operating funds for the current fiscal year, until the Auditor notifies the Ohio Department of Education that the Auditor is satisfied that the board has made the required transfer (Ohio Rev. Code §3318.051(B)).
  - *Note:* Auditors should consult with the Auditor of State’s Legal Division if noncompliance is identified. The Auditor of State Legal Division will prepare the written notification to the school district board and to the Ohio Department of Education, if necessary. IPA’s should notify the Auditor of State’s Center for Audit Excellence if noncompliance is identified. The Auditor of State Center for Audit Excellence will then consult with the Auditor of State Legal Division as appropriate.

Districts are to establish a project construction fund [Ohio Rev. Code § 3318.08] to account for project funding and expenditures (USAS fund 010),<sup>33</sup> and a project maintenance fund [Ohio Rev. Code § 3318.05] to account for maintenance funding and expenditures (USAS fund 034). ***Districts should not account for local funding initiatives in these funds. Rather, a separate fund should be established.***

The maintenance fund can only be used to maintain and repair completed facilities as identified in the approved maintenance plan, including preventative maintenance, periodic repairs, and the replacement of facility components. Routine janitorial and utility costs, equipment supplies and personnel costs associated with the day-to-day housekeeping and site upkeep are not allowable expenditures. No moneys other than costs associated with the development of the preventive maintenance plan may be expended out of fund 034 prior to the approval of the maintenance plan by the Commission. The construction manager is required to initiate the process of developing the plan at least six months prior to the completion of any facility for occupancy. [Legal criteria: The maintenance plan approved by the Commission, as evidenced by a signed Commission resolution]

#### **CFAP Written Agreement [Ohio Rev. Code §3318.08]:**

Prior to project commencement the Commission and school district enter into a written agreement (“Project Agreement”). The Project Agreement is the contract between the district and the Commission. There can be many attachments to the Project Agreement and amendments to the Project Agreement. Some of the common attachments include schedules of the alternative funding sources for both the local portion for construction and/or the maintenance levy, and a Memorandum of Understanding (MOU) which sets forth the specific terms and conditions of the Local Initiative. The agreement and the applicable attachments, in part, will provide for the following:

- Sale and issuance of bonds or bond anticipation notes for all or a portion of the district’s share of project costs (to be deposited into the district’s project construction fund (USAS

<sup>33</sup> AOS Bulletins 1999-004 and 2001-007 include USAS accounting and legal guidance for the CFAP program. The accounting guidance still applies, but auditors should not rely on the legal guidance of those bulletins because some of it is outdated.

- 010), and the transfer of approved local resources (if any) to the project construction fund. *(Note: the district's local share of the project costs is not the same as a "locally funded initiative". Locally funded initiatives should be accounted for in separate funds, not Fund 010.)*
- The funding source for project maintenance and the conditions, if any, under which a portion of maintenance funding will be paid to the State. Repaying the State is no longer required. As noted above, the money a one-half mill maintenance levy or an alternative funding source generates must be deposited into fund 034 and can only be used to maintain and repair facilities, including preventive maintenance, periodic repairs, and replacing facility components.
  - Authorization to advertise for, receive, and award construction bids for the project, subject to Commission approval.
  - Disbursement of moneys from the district's project construction fund after receiving Commission approval. Payments from the construction fund are restricted to: 1) professional design and administration services, 2) payments to contractors who have performed work, 3) purchases related to the Project, and 4) any transactions authorized necessary or appropriate for establishing and administering investment accounts. Occasionally, districts will receive approval from the Commission for reimbursement of items that should have been project costs. If this is the case, the District should have an approval letter on file from the Commission that should be presented to the auditor to substantiate the expenditure. All payments from fund 010 should evidence approval by the district treasurer or another board designee and by the Commission, as delegated to the construction manager. ***Locally Funded Initiatives should not be paid from fund 010, but from another fund identified by the district.***
  - The Commission will pay the construction manager from the State's share of the project. (These payments should be recorded in fund 010 as receipts of the State's share and as construction expenditures. When establishing budgets for the project, these amounts should be included in estimated receipts and appropriations.)
  - Disposition of any balance left in the project construction fund after completion of the project:
    - Regarding investment earnings attributable to the school's own contributions to the project, the school should either: retain them in its project construction fund for future projects, transfer them to its project maintenance fund,<sup>34</sup> or transfer them to its permanent improvement fund. [Ohio Rev. Code § 3318.12(C)(1)]
    - The school should transfer investment earnings attributable to the state's contribution to the School Facilities Commission [Ohio Rev. Code § 3318.12(C)(2)]
    - Any other surplus remaining in the school district's project construction fund after the project's completion shall be transferred to the commission and the school district board in proportion to their respective contributions to the fund. [Ohio Rev. Code § 3318.12(C)(3)]

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<sup>34</sup> These monies shall be used solely for maintaining the classroom facilities included in the project.

***Note:*** There are exceptions to some of these general requirements. Auditors should review the terms of the district's project agreement, and any attachments or amendments to the agreement, to determine requirements specific to the project.

**Related Programs:**

Other Ohio Revised. Code Chapter 3318 programs include the **School Building Assistance Expedited Local Partnership Program** [Ohio Rev. Code § 3318.36 and 3318.362], ~~and the **Exceptional Needs School Facilities Assistance Program** [Ohio Rev. Code § 3318.37] and the **Joint Science, Technology, Engineering, and Mathematics (STEM) Program** [Ohio Rev. Code §3318.71].~~ The Expedited program allows school districts to choose to fund a distinct portion of their Facilities Master Plan through local monies prior to the time their state funding becomes available. Once a district enters CFAP they receive credit against their required local contribution for the work completed under the Expedited program. None of the CFAP specific requirements related to the tracking and disposing of interest earnings apply to school districts participating in the Expedited Local Partnership Program. Since it is not a co-funded program, moneys related to that program should be accounted for in a fund other than fund 010. The Exceptional Needs program provides assistance to lower wealth districts with an exceptional need for immediate classroom facilities assistance, as determined by the Commission. The program is specifically designed for replacement as opposed to expansion or renovation.

Guidelines for the acquisition of classroom facilities for the STEM program are established by the Ohio School Facilities Commission. These guidelines can be found on the OFCC site at: <http://ofcc.ohio.gov/ServicesPrograms/K-12Schools/OtherK-12Programs.aspx>. The commission shall also provide funding to assist a qualifying partnership<sup>35</sup> in accordance with Ohio Rev. Code §3318.11. The qualified partnership's fiscal agent, a member district, may levy taxes in excess of the ten-mill limitation [Ohio Rev. Code §5705.2112] to use for all or part of the acquisition.

With the exception of the Expedited program identified above, these programs follow the basic CFAP requirements discussed above, though there are differences. Districts will enter into agreements with the Commission. If the district participates in these or other Ohio Rev. Code Chapter 3318 facility projects, auditors should review the terms of the agreement and identify those requirements which may be material. When making that determination, auditors should consider the requirements and procedures addressed in this Ohio Compliance Supplement Section for the CFAP program.

~~Note: Community schools may not participate in these programs, except: per Ohio Rev. Code § 3318.50, a community school may obtain a classroom facilities loan guarantee from the State, for up to 15 years.~~

**Interfund Activity:*****During the project***

Ohio Rev. Code § 3318.12 permits a school district board, by resolution, to use all or part of the interest attributable to the district's share of moneys in the project construction fund to pay the cost of local initiatives that are not included in the state-assisted project, but that are related to it. If a district board chooses to use some or all of the interest attributable to its share of the fund for local initiatives and, later, the cost of its state-assisted project exceeds the amount in the fund, the district must re-pay all of the interest used for those initiatives before further state funds will be released for the project.

<sup>35</sup> A qualifying partnership is a group of city, exempted village, or local school districts which meet the following criteria: (1) the districts are part of a career-technical education compact, the districts have entered into an agreement for joint or cooperative establishment and operation of a STEM education program under Ohio Rev. Code § 3313.842 , and (3) the aggregate territory of the districts is located in two adjacent counties, each having a population greater than 40,000 but less than 50,000, and at least one of which borders another state. (Ohio Rev. Code §3318.71)

***After the project is completed***

Ohio Rev. Code § 3318.12(B)(2) permits a school district board at its option, by resolution, to transfer the interest attributable to its local share in the project construction fund to its permanent improvement fund (where presumably it could be spent on any permanent improvement) or to leave that interest in the project construction fund to pay the cost of future projects. A district board also may choose to transfer the interest to the district's maintenance fund. In either case, interest attributable to the state's share of the project construction fund must be returned to the state.

**OSFC/OFCC Agreed-Upon Procedures (AUP) Engagements:**

OSFC/OFCC conducts AUP engagements on select school districts that are in the construction phase. All school districts participating in classroom facilities programs will receive an AUP engagement at least once during a project's lifetime. The firms of Kennedy Cottrell Richards and Julian & Grube, Inc. conduct these engagements and are in good standing with the Auditor of State's Office.

The focus of the AUP engagements is accountability and compliance with the terms of the OSFC/OFCC Project Agreement (including any amendments thereto) and Ohio Rev. Code Chapter 3318. The firms test the following areas, as applicable:

- deposit of project funds (both State and Local)
- spending of project funds
- interest earnings and allocation to the appropriate funds
- escrow accounting
- the closeout process

OSFC/OFCC forwards the results of the AUP engagements to the Auditor of State, who then distributes the reports to regional chief auditors and independent public accounting firms. Pursuant to *Government Auditing Standards* paragraph 4.05, "auditors should evaluate whether the audited entity has taken appropriate corrective action to address findings and recommendations from previous engagements that could have a material effect on the financial statements or other financial data significant to the audit objectives. When planning the audit, auditors should ask management of the audited entity to identify previous audits, attestation engagements, and other studies that directly relate to the objectives of the audit, including whether related recommendations have been implemented. Auditors should use this information in assessing risk and determining the nature, timing, and extent of current audit work, including determining the extent to which testing the implementation of the corrective actions is applicable to the current audit objectives."

**Community Schools:****Community School Classroom Facilities Grant Program**

Section 501.10 of Am. Sub. House Bill 64 authorized the creation of the Community School Classroom Facilities Grant Program. The act permits the Commission to provide grants for the purchase, construction, reconstruction, renovation, remodeling, or addition to classroom facilities to (1) "eligible high-performing community schools" and (2) newly established community schools that have a track record of high quality academic performance. Further details about this program can be found on the OFCC site: <http://ofcc.ohio.gov/ServicesPrograms/CommunitySchoolClassroomFacilitiesGrants.aspx>, or ODE

site: <http://education.ohio.gov/getattachment/Topics/Quality-School-Choice/Community-Schools/Community-School-Classroom-Facilities-Grants.pdf.aspx>.

Note: This is a new program and is likely to qualify as direct and material for any school that receives it. The OFCC is not requiring AUPs over these projects at this time. Therefore, include procedures as necessary in accordance with the grant agreement.

**POSSIBLE NONCOMPLIANCE RISK FACTORS:**

**Note: In assessing the risk of noncompliance, auditors should consider whether an AUP report that covered at least six months of the period under audit is available from OSFC/OFCC. If so, auditors should evaluate the results of the AUP to assess the risk of noncompliance.**

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

**Agreed-Upon Procedures (Traditional Schools ONLY):**

Per GAGAS 4.05, Inquire whether OSFC/OFCC conducted an AUP engagement over the district’s construction project. If so, obtain a copy of the AUP report, place it in the permanent file, and perform the following:

- Determine what period was covered by the AUP engagement procedures.
- Determine the extent of testing performed over the district’s construction activity. Auditors *may* rely on the AUP engagement to reduce the scope and extent of the audit steps enumerated below. *However, auditors should review the reported procedures to determine whether they apply: (1) only once during a project’s lifetime, or (2) if they are ongoing and should be tested annually. For example, we would expect tests of allowability of expenditures to be tested annually during the construction phase. However, the establishment of the appropriate project funds/special cost centers would only be applicable once, generally at the onset of the project. Therefore, testing of type (1) requirements (i.e., applicable one-time only) does not need to be repeated each year. Auditors may refer to prior year testing or an existing AUP engagement, regardless of the period covered, to satisfy these requirements. However, an AUP engagement may only be used to reduce testing of the steps below for type (2) requirements (i.e., applicable on an ongoing basis each year) if the period covered by the*

- AUP engagement included at least six months of the current period under audit. Auditors should carefully read the AUP procedures to ensure they obtain an appropriate understanding of the testing procedures performed when making this assessment.*
- Determine whether any significant findings or recommendations requiring corrective action or follow up were included in the results of the AUP report. If so, determine whether the district has corrected the noncompliance or can document satisfactory progress towards addressing the noncompliance. Auditors should *annually* evaluate the significance of uncorrected items for inclusion in the current audit report.
    - If the school is not adhering to agreed upon timetables for corrective action, etc., auditors should consider reporting noncompliance. Noncompliance findings should include the following: (1) a reference to the existing noncompliance such as, "... in a report dated XX, AOS or an accounting firm reported noncompliance with ORC 3318.YY", and (2) a description of the status of the noncompliance as of the date of the current audit report.

Review the project agreement between the district and Commission. Considering the requirements specific to the project, perform the following procedures (document specific requirements relevant to the following tests):

### **Project Funding:**

Scan the accounting records to determine if the proper activities are being recorded in the project activities fund (USAS 010). Determine if the District/STEM school is accounting for the following four revenue streams **separately**: (1) Local Revenue, (2) Interest on Local Funds, (3) State Revenue – aka "drawdowns", and (4) Interest on State Revenue.

Determine if the District/STEM school deposited the local share funds required by the Project Agreement into fund 010 for both the original contribution and any amendments.

Select contracts and related contract expenditures and determine through inspection, vouching, or other such means that contracts were awarded using competitive bidding procedures.

Vouch a few transactions from fund 010 for allowable cost as defined in the agreements. We are not opining on this program, so we do not require a high level of assurance. Testing high dollar transactions and scanning other selected transactions should suffice. Review the supporting documentation to determine if the expenditure was:

- a. allowed under the terms of the Project Agreement;
- b. if it was approved by the district treasurer or another board designee and the construction manager prior to payment;
- c. if it excludes any costs for a locally funded initiative;
- d. if the amount paid agrees with the invoice and
- e. if it is recorded in the correct amount in the correct fund.
- f. If the District did not properly segregate transactions into a project construction fund (i.e., did not establish fund 010), report noncompliance accordingly. Auditors should also consider reporting a finding for adjustment. See the OCS Implementation Guide for guidelines pertaining to Findings for Adjustments.

Scan interfund activity in fund 010. Determine whether material transfers or advances were properly approved and/or allowable under Ohio Rev. Code. If an advance is repaid out of fund 010, request the District/STEM school provide the approval letter from the Commission which authorized the reimbursement.

**Maintenance Funding:**

Inquire with the client or review capital asset records to determine if the District/STEM school ever had an OSFC/OFCC project. If so determine whether or not the project maintenance fund (USAS fund 034) has received the required ½ mill and expenditures were in accordance with the approved maintenance plan for the entire 23 years. **Note:** If they are using the alternate maintenance obligation see the section below.

Vouch a few disbursement transactions from fund 034. We are not opining on this program, so we do not require a high level of assurance. Testing high dollar transactions and scanning other selected transactions should suffice. Determine whether expenditures were only for maintenance of the funded project facilities in accordance with the district's approved maintenance plan. (If the District/STEM school did not segregate transactions related to project maintenance (i.e. did not establish fund 034), report noncompliance accordingly. As noted above, the only allowable expenditures out of fund 034 prior to the completion of the project are for the costs associated with the development of the maintenance plan.

**Locally Funded Initiative(LFI):**

If applicable, review accounting records and related documents and determine if the district/STEM school established a separate fund, or special cost center in a fund other than Fund 010, to track receipts and expenditures related to a locally funded initiative.

Vouch selected disbursement transactions from the LFI fund/special cost center. We are not opining on this program, so we do not require a high level of assurance. Testing high dollar transactions and scanning other selected transactions should suffice. Determine whether expenditures were: (1) approved by the district treasurer or another board designee and construction manager prior to payment, (2) in agreement with the vendor invoice, and (3) in compliance with the district's/STEM school's approved Memorandum of Understanding with the OSFC/OFCC. If the district/STEM school did not segregate transactions related to LFI (i.e. did not establish a separate fund or a separate special cost center in a fund other than Fund 010), report noncompliance accordingly.

**Alternate Maintenance Obligation:**

Determine whether the school district/STEM school has elected to use the new alternative mechanism for meeting its maintenance obligation. If so, obtain the district's annual certification<sup>36</sup> to the Commission and determine if the school district carbon copied the Auditor of State regional office that the amount required for the year has been transferred into the maintenance fund.

IPA's perform agreed-upon procedures reports to serve as certification. Obtain a copy of this AUP report from the district and review for noncompliance. If the school district has deposited less than the required amount, determine whether AOS sent the required written notification to the district board mandating the necessary deposit within 90 days of the notice.

**Interfund Activity:**

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<sup>36</sup> The following is sample annual certificate language: "The undersigned Treasurer of the Board of Education of the XYZ District, YYY County, Ohio hereby certifies that a resolution was duly passed by the Board of Education of said School District on MM/DD/YYYY to transfer \$xx,xxx from the General Fund to the OSFC/OFCC Facility Maintenance Special Revenue Fund.

Determine whether the district/STEM school transferred interest out of the Project Construction Fund (Fund 010) during the audit period. If so, determine whether:

- the district/STEM school board adopted a resolution approving the transfer
- the monies transferred represented only interest attributable to the district's local share of the project
- the monies were transferred to the appropriate funds and accounts. (*Note: the OSFC/OFCC recommends using the Transfer-Out appropriation and Transfer-In receipt accounts to record this activity*).

**Surplus Balance:**

If a surplus remained after project completion, inspect the district's records supporting the distribution of the surplus. Determine whether the proper amounts were returned to the Commission and transferred to the district's respective funds.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

*Section B: Contracts and Expenditures*

**NONE**

**Section C: Debt**  
**COMMUNITY SCHOOLS**

**1-12 Compliance Requirement:** Ohio Rev. Code §3314.08 - Foundation anticipation notes. *(MOVED FROM CHAPTER 3)*

**Summary of Requirement:** A community school may borrow money to pay any necessary and actual expenses in anticipation of State Foundation receipts. The school may issue notes to evidence such borrowing. The proceeds of the notes shall be used only for the purposes for which the school may lawfully expend the anticipated foundation receipts. [Ohio Rev. Code § 3314.08(G)(1)(a)]

A community school cannot issue debt secured by taxes. [Ohio Rev. Code §3314.08(E)]

A school may also borrow money for a term not to exceed fifteen years to acquire facilities. [Ohio Rev. Code §3314.08(G)(1)(b)]

**Suggested Audit Procedures – Compliance (Substantive) Tests:**

By reading the minutes, inspecting receipts journals, and by inquiry determine whether or not the School issued any type of debt.

Examine disbursements made of the proceeds to determine that they were used only for the purposes described in the debt agreement.

Determine that moneys borrowed were not collateralized by taxes.

Determine that moneys borrowed to acquire facilities are for a term of fifteen years or less.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**Revised: HB 64, 131<sup>st</sup> GA**  
**Effective: 9/29/15**

## ENTITIES OTHER THAN COMMUNITY SCHOOLS

**1-1312 Compliance Requirement:** Ohio Const. Art. XII, Section 11; Ohio Const. Art. XVIII, Section 12 Ohio Rev. Code §133.10, 133.22 133.24, 167.041, 321.34, 505.401, 5705.03, 5705.05, 5705.09 and 5705.10; 1981 Op. Atty. Gen. No. 81-035 – **Issuing or Retiring Bonds and Notes.**

### Summary of Requirements:

#### *Common Types of Debt*

**BACKGROUND INFORMATION:** Per Ohio Rev. Code §133.01(Q), *general obligation* securities are those collateralized by a pledge of taxing authority, up to the subdivision's available tax limit (sometimes described as a taxing authority's "full faith, credit and taxing authority.")

The following are examples of securities that are **not** general obligations:

Ohio Rev. Code §133.01(LL) defines *self-supporting securities* as securities, or portions of securities where the fiscal officer estimates that revenue sources, excluding taxes, are sufficient to pay for operating costs plus debt service. These are securities collateralized by pledged revenue,<sup>37</sup> without a pledge of taxes. Enterprise utility operations often issue self-supporting securities. Ohio Rev. Code §133.01(MM) lists the various subdivisions authorized to issue self-supporting securities; such as municipalities, townships, counties, school districts, and certain other districts. (See the statute for a complete list.) Ohio Rev. Code §133.01(MM) does not list community schools.

Ohio Rev. Code §133.08 (D) defines *revenue* securities as those a county issues, collateralized only by pledged revenue and which are not secured by a county's full faith, credit and taxing authority.

Ohio Const. Art. XVIII, Section 12, authorizes a municipality to issue bonds collateralized by pledged revenues or mortgages to acquire, construct, or extend public utilities. These bonds do not impose any liability on the municipality, except the creditor's right to the pledged revenue and / or mortgage. That is, this debt is not a general obligation.

#### *Issuance of Securities*

- Ohio Const. Art. XII, Section 11 states that "[n]o bonded indebtedness of the state, or any political subdivision thereof, shall be incurred or renewed unless, in the legislation under which such indebtedness is incurred or renewed, provision is made for levying and collecting annually by taxation an amount sufficient to pay the interest on said bonds, and to provide a sinking fund for their final redemption at maturity."
- Ohio Rev. Code §5705.03 provides that the taxing authority of each subdivision must levy sufficient taxes annually as are necessary to pay the interest and sinking fund on and retire at maturity the

<sup>37</sup> *Pledged revenue* is revenue the debt legislation or covenant provisions pledged as collateral to the debt owners.

bonds, notes and certificates of indebtedness of such subdivision subject to the limitations of applicable statutes.

- Ohio Rev. Code §133.23 describes the legislation required to authorize new securities. Per Ohio Rev. Code §133.23(C), legislation must identify the source(s) of repaying the bonds, which may be **any** moneys required by law to be used, or lawfully available, for the purpose authorized. If the bonds are general obligations, or a property tax otherwise must be levied for the debt service, the legislation shall provide for levying a property tax sufficient to pay the bonds' debt charges; but the tax amount levied or collected in any year may be reduced by the amount to be available from special assessments,<sup>38</sup> revenues and surplus funds of public utilities, any surplus in the funds from which such bonds are to be retired, or other moneys specifically assigned by law or by legislation of the taxing authority for payment of such debt charges.

We interpret Ohio Rev. Code §133.23(C) as follows:

- Revenue (tax or otherwise) pledged to repay debt must be used for debt service unless the debt is repaid from other sources.
- A government can use unrestricted money or restricted money for purposes consistent with the restriction to pay debt service. For example, a government might use restricted grant revenue<sup>39</sup> to pay revenue anticipation note debt service, if the debt proceeds were spent for allowable grant purposes, even if the debt legislation pledges taxes.
- Therefore, if these bonds are a general obligation, a government must **authorize** a levy, but need not levy the tax if it can use other resources to pay the debt service.

#### ***Debt Issuance for Board of Trustees for Fire Districts***

Pursuant to Ohio Rev. Code Chapter 133, Ohio Rev. Code §505.401 provides additional borrowing authority for the board of trustees for fire districts organized under Ohio Rev. Code §505.37(C). This section allows the fire district's board of trustees to issue bonds to acquire fire-fighting equipment, buildings and sites for the district or to construct or improve a building to house fire equipment.

#### ***Infrastructure Loans for Regional Councils of Government***

An educational service center serving as a fiscal agent for a regional council of governments can enter into agreements with the governing body of one or more member governments to lend money to improve infrastructure within the member's territory. [Ohio Rev. Code §167.041]

#### ***Retirement of Securities***

- Ohio Rev. Code §5705.09(C) requires each subdivision to establish a bond retirement fund into which it must pay sufficient revenues to retire serial bonds, notes and certificates of indebtedness at maturity.

<sup>38</sup> FYI: Special assessment anticipation notes issued per Ohio Rev. Code § 133.17 are collateralized by a pledge of special assessments, **and** as general obligations. However, notes issued per Ohio Rev. Code § 133.13, anticipating special assessments collected in one installment are collateralized only by the assessments and are **not** general obligations.

<sup>39</sup> Unless the grant regulations prohibit debt payments. For example, 2 C.F.R. 225 would generally permit using Federal grants to pay debt related to assets used in Federal programs, per Attachment B, item 23b. OMB issued the Uniform Guidance, implementing changes to the cost principles for new awards (and certain funding increments) signed by the federal agency on or after December 26, 2014, however, this provision (2 C.F.R. 200.449(a)) is the same.

- Ohio Rev. Code §5705.10 provides that all revenue derived from levies for debt charges on bonds, notes, or certificates of indebtedness must be paid into a [debt service] fund for that purpose.
- Ohio Rev. Code § 133.10(E) further provides that revenue anticipated (i.e. property taxes pledged to pay tax anticipation notes) may be appropriated for purposes other than paying debt charges only after deducting an amount sufficient to pay the debt. The amount (of anticipated revenues) to be applied to debt charges must be set aside in an account in the bond retirement fund. Ohio Rev. Code § 133.10(E) applies to certain other types of securities, for example in Ohio Rev. Code sections:
  - Ohio Rev. Code §133.13: Certain special assessments
  - Ohio Rev. Code §133.17: Securities anticipating special assessments
  - Ohio Rev. Code §133.32: All Ohio Rev. Code Chapter 133 securities
  - Ohio Rev. Code §6101.50: Conservancy district special assessments RAN

### *Issuance of Notes*

- Ohio Rev. Code §133.22(B) requires that when a subdivision issues notes, its financial officer must notify the county auditor that such notes have been sold. Per Ohio Rev. Code §321.34(B), when a county auditor *advances* tax revenue to a subdivision, the county auditor must allocate the advance between the subdivision's general and debt service fund, to provide sufficient tax revenue to pay the subdivision's outstanding G.O. indebtedness.
- Ohio Rev. Code §505.262(A) authorizes a board of township trustees to issue notes of the township to finance installment payment purchases of equipment, buildings, and sites for any lawful township purpose. All notes issues shall be pursuant to Ohio Rev. Code § 133.20. Furthermore, the Attorney General opined that Ohio Rev. Code § 505.262(A) does not grant explicitly or implicitly the authority of the township to grant a security interest in the property purchased by the installment contract. [1996 Op. Atty. Gen. No. 96-048]<sup>40</sup>

### *Special Features*

- Ohio Rev. Code Chapter 133 securities may include the following features:
  - Floating interest rates [Ohio Rev. Code § 133.26(A)]
  - Early redemption or call provisions [Ohio Rev. Code § 133.26(B)]
- Legislation authorizing a debt issuance may contain restrictions on the source of payment for debt charges.

### *Retiring Debt from Funds Other than a Debt Retirement Fund*

- ***Absent a specific requirement***, debt may be paid from any unrestricted monies held, segregated from restricted monies, in a fund which was established for a purpose not inconsistent with paying such debt. When evaluating compliance with the requirements in this section, place

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<sup>40</sup> For example, townships cannot take out a simple bank loan to purchase a truck for road purposes since “bank loans” are not a statutorily permitted form of debt for townships. However, townships do have authority to issue securities under Ohio Rev. Code Chapter 133 (e.g., anticipatory debt usually secured for infrastructure). However, Ohio Rev. Code § 505.262(A) and 1996 Op. Atty. Gen. No. 96-048 provide specific authority for townships to issue Chapter 133 securities for the purposes this paragraph describes.

emphasis on the source of monies used to repay debt. When a subdivision pays debt from a fund other than a debt retirement fund, consider the following:

- Ohio Rev. Code §5705.10 (I) provides that money paid into a fund shall be used only for the purpose for which such fund was established. Therefore, money in a fund may be used to pay debt charges provided the payment of such debt charges is consistent with the purpose for which the fund was established;
- With regard to tax anticipation notes, Ohio Rev. Code § 133.24(D) provides that, except for *capitalized interest*<sup>41</sup>, debt charges on tax anticipation notes are payable only from the revenue collected by the tax levy anticipated.
- Ohio Rev. Code § 5705.05 prohibits using taxes levied for current expenses to pay debt charges.
- Ohio Rev. Code § 5531.10(C) (issuing obligations for state infrastructure projects) provides that the holders or owners of such obligations shall have no right to have moneys raised by taxation by the state of Ohio obligated or pledged, and moneys so raised shall not be obligated or pledged, for the payment of bond service charges.<sup>42</sup>
  - Additionally, the section specifically permits townships receiving distributions from the Gasoline Excise Tax Fund in the state treasury to use that money to pay debt service on State Infrastructure Bank (SIB) obligations. (Ohio Rev. Code § 5531.10 and 5735.27)
- 1981 Op. Atty. Gen. No. 81-035 states:
 

Certain moneys paid into the general fund which are not derived from a general levy for current expenses are placed in the general fund precisely because their use is not restricted. (See Ohio Rev. Code §5705.10). Such monies may be used to pay debt charges provided that they have not been commingled with general fund monies which may not be used for debt payment. Where otherwise unrestricted monies have been paid into the general fund and have been commingled with restricted monies to the extent that the particular source from which the monies originated cannot be distinguished, such monies may be used to pay debt charges only after they have been transferred to an appropriate fund [pursuant to Ohio Rev. Code § 5705.14].
- Ohio Rev. Code §505.262(A) authorizes a board of township trustees to issue notes of the township to finance installment payment purchases of equipment, buildings, and sites for any

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<sup>41</sup> Ohio Rev. Code § 133.01(E) defines *capitalized interest* as interest received with the proceeds of a security. For example, this would include interest payable accruing between the security's issuance date and the date the security was sold. Since the government must pay this interest to the security owners, the government generally must set aside this interest for the first debt service payment and should not use it for the purpose for which the principal was issued. [EX133.16] Do not confuse this with *capitalized interest discussed in FASB 34 & 62 or GASB 34, 37, etc.*

<sup>42</sup> Ohio Rev. Code § 5531.10(C) is not a requirement to use a Debt Service Fund. Rather, this section describes statutory exceptions to the general rule that monies not otherwise restricted could be used to pay debt where the purposes of both were not inconsistent. In other words, governments with SIB loans cannot obligate or pledge State-levied taxes to pay bond service charges (except townships receiving distributions from the Gasoline Excise Tax Fund in the state treasury to use that money to pay debt service on State Infrastructure Bank (SIB) obligations).

lawful township purpose. All notes issues shall be pursuant to Ohio Rev. Code § 133.20. Furthermore, the Attorney General opined that Ohio Rev. Code § 505.262(A) does not grant explicitly or implicitly the authority of the township to grant a security interest in the property purchased by the installment contract. [1996 Op. Atty. Gen. No. 96-048]

- The Expedited Local Partnership Program provides a way for school districts to start approved school building projects using local funds while they wait for state funding under the “main” Classroom Facilities Assistance Program (CFAP) program. Once a district is eligible for CFAP, it may apply this advance expenditure of local resources toward its portion of the cost of its total CFAP project. If a district has spent more than its share of its CFAP project while proceeding under the Expedited Program, the School Facilities Commission must reimburse the district the amount of the over expenditure. Ohio Rev. Code § 3318.36(E)(2) provides that school districts may first deposit reimbursed money into either the district's general fund or a permanent improvement fund to replace local resources the district withdrew from those funds for constructing classroom facilities included in the district's CFAP project. The remaining reimbursement monies must be used to pay debt service on classroom facilities constructed under the Expedited Program. (Ohio Rev. Code § 3318.36(E)(2))

<b>In determining how the government ensures compliance, consider the following:</b>	<b>What control procedures address the compliance requirement?</b>	<b>W/P Ref.</b>
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Bond Counsel/Lender Involvement</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures – Compliance (Substantive) Tests**

For securities issued during the audit period, inspect the debt legislation and determine under which Rev. Code statute the debt was issued. If that section is not listed in this Ohio Compliance Supplement Chapter, read the specific statute and amend the testing steps to include tests to determine:

- The legality of the source of repayment and collateral. (We can normally rely on documents (such as an offering statement) bond counsel or the underwriter prepared describing the source of repayment and collateral, if they were involved with a debt issue. We should inspect their conclusions for reasonableness and summarize in the permanent file.)

- Whether the government properly segregated any revenue pledged for debt service or capitalized interest (i.e. interest accruing between the security's issuance date and the date the security was sold) and used that revenue for debt service. This will often require establishing a debt service fund.
- Whether the government used the proceeds for the purposes authorized.
- If the debt is still outstanding at the end of the audit period, include copies or summaries of the information related to the three bullet points above in the permanent file.
- If the debt includes features such as floating interest rates or early redemption or call provisions, determine if enabling legislation and the Ohio Rev. Code authorize those features. (For example, Ohio Rev. Code §133.22(D) describes features BAN can include.)

Inspect the county tax settlements and trace revenues to the funds indicated. If amounts from tax levies for bond retirement are being placed into funds other than bond retirement funds, inspect documentation that the government deducted an amount sufficient to pay the debt charges. (Ohio Rev. Code § 5705.10(B))

By reading the government's financial statements or inspecting its ledgers, determine where debt is paid from. If other than bond retirement funds, determine that:

- Debt paid from a restricted fund was paid from revenue which could be used for the same purpose for which the debt proceeds were spent [Ohio Rev. Code §5705.10 or 133.24(D)];
- Restrictions, if any, in the debt-authorizing legislation were followed;
- Revenue derived from a general levy for current expenses is not used to pay debt charges [Ohio Rev. Code §5705.05]; or
- Monies used to pay debt from the general fund have not been commingled with general fund monies which may not be used for debt payment [1981 Op. Atty. Gen. No. 81-035].

**Note:** Where bond counsel was involved with debt issues we are testing, we can usually rely on documents they have prepared or opined on, as evidence that legislation authorizing the securities complies with statute. However, bond counsel would not "audit" the government's *subsequent* compliance with requirements. For example, we would not expect bond counsel to determine how the government accounted for debt proceeds or whether the proceeds were spent for authorized purposes.

#### ***Board of Trustees for Fire Districts***

By reading the minutes, inspecting bond ledgers or other documents, or by inquiry, determine if the fire district used this type of borrowing.

If so,

- trace the bond issuance to the budget;
- inspect the resolution authorizing the bond issuance;
- determine whether the issuance is in accordance with Ohio Rev. Code Chapter 133 requirements; and

- determine whether the proceeds were used to acquire fire-fighting equipment, buildings or sites for the district or for the purpose of constructing or improving a building to house fire equipment.

**Council of Governments**

- Review the agreement and determine if they are following the requirements;
- Determine expenditures for the loans is for proper public purpose;
- Determine if the repayment for the loans is paid from the proper fund.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**Revised: HB 64, 131<sup>st</sup> GA**  
**Effective: 9/29/15**

**1-1413 Compliance Requirement:** Ohio Rev. Code § 133.10, 133.22, 133.24, and 4582.56(B) & (C) – Bond, Tax and Revenue Anticipation Notes (BAN, TAN and RAN).

**Summary of Requirements:** Per Appendix C-1 in the OCS Implementation Guide, several Ohio Rev. Code sections authorize TAN, RAN or BAN. Short-term TANs or RANs are generally subject to (1) below.<sup>43</sup> Long-term TAN are *generally* subject to (2) below.<sup>43</sup> Significant requirements related to BAN are described at the end of this step.

- 1) **Short-term** notes anticipating *current* revenues, most often current tax levies: A government cannot issue these notes for more than a defined percentage of the current-year's estimated revenue (for example, ½ the current annual estimated revenue from utility charges or grants [Ohio Rev. Code §133.10(B)], or approximately ½ of the next tax settlement, [Ohio Rev. Code § 133.10(A)]). These notes normally mature within six months, or the end of the fiscal year, whichever occurs first. Most Ohio Rev. Code sections authorizing these notes require them to comply with Ohio Rev. Code § 133.10. The remainder of this step refers to these notes as Ohio Rev. Code §133.10 *short-term notes*.
- 2) **Long-term** notes anticipating *future tax* revenues, from voted tax levies, usually of a limited life: A government cannot issue these notes for more than the amount the levy will generate over its life, or a portion of its life. These notes mature over the life of the levy or a shorter period Ohio Rev. Code specifies, such as 5 or 10 years. Most Ohio Rev. Code sections authorizing these notes require them to comply with Ohio Rev. Code § 133.24. The remainder of this step refers to these notes as Ohio Rev. Code §133.24 *long-term notes*.

### **RC 133.10 short-term TAN or RAN**

#### **TAN:**

- TAN must mature no later than the last day of the sixth month after the issue date, and in no case may they mature after the end of the fiscal year. The aggregate amount outstanding cannot exceed ½ of the amount anticipated for the next six months (typically the next settlement minus advances). [Ohio Rev. Code §133.10(A)]
- While Ohio Rev. Code §133.10(A) applies to subdivisions generally, §133.10(C) is specifically applicable to counties, municipalities, townships and school districts. If one of these entities issues TANs under Ohio Rev. Code §133.10(C), these TANs need not mature until the end of the year. (That is, they are not restricted to a six-month maturity.)
- Notes a school district issues anticipating a delayed property tax settlement may be for up to 90% of the amount estimated to be received by that settlement (other than taxes to be received for paying debt charges) minus advances, and may mature as late as the August 31 after the June 30 fiscal year end. [Ohio Rev. Code §133.10(D)]

<sup>43</sup> The references to *long-term* and *short-term* above refer to the legal requirements, not the classification of this debt under GAAP. Auditors should refer to GASB Codification B50 and GFOA CAFR checklist for guidance on GAAP debt classifications.

**RAN:**

- The notes issued cannot exceed ½ of the amount of the projected revenues remaining to be received during the fiscal year, minus advances and prior collections, as estimated by the fiscal officer. [Ohio Rev. Code § 133.10(B)]
- Notes issued anticipating current revenues in and for any fiscal year from any source or combination of sources, including distributions of any federal or state moneys, other than the proceeds of property taxes shall mature not later than the last day of the fiscal year for which the revenues are anticipated. [Ohio Rev. Code § 133.10(E)(2)]

**All Ohio Rev. Code § 133.10 short-term TAN or RAN**

- Pledged revenue (tax or otherwise) collected to retire these notes is considered appropriated for debt charges and financing costs. The government can appropriate this revenue for other purposes only after deducting sufficient amounts to pay debt service. The government must deposit pledged revenue sufficient to pay the debt in an account in a debt service fund. [Ohio Rev. Code § 133.10(E)(1)]
- These notes cannot be issued prior to the first day of the fiscal year. [Ohio Rev. Code § 133.10(E)(2)] (The only exception is that a board of education of a school district may issue notes as early as 10 days before the first day of the fiscal year (i.e., by June 21), provided that the proceeds of the notes can neither be spent nor considered available for appropriation prior to the first day of the fiscal year [i.e., July 1]). [Ohio Rev. Code § 133.10(H)]
- The government can spend note proceeds only for the purposes for which the related revenue can be spent. [Ohio Rev. Code § 133.10(E)(3)] For example, if a government issues RAN, anticipating Federal grant proceeds, the government can spend the note proceeds only for purposes the Federal grant permits.

**Ohio Rev. Code § 133.24 long-term TAN**

- The aggregate amount of principal outstanding may not exceed the anticipated levy proceeds provided in the applicable law by a statement of percentage or by a limitation on the amount of annual maturities. These TAN must mature by December 31 of the year authorized by statute, or by December 31 of the last year of the levy, whichever is earlier. [Ohio Rev. Code § 133.24(B)] Therefore, the duration of these notes should match the levy's life. (Unless another Ohio Revised Code section specifies a shorter period. See the Appendix C-1 in the OCS Implementation Guide for examples.) The estimated annual debt service should approximate the annual levy proceeds.
- Debt service is payable only from the levy proceeds. (Except the government should use capitalized interest collected with the debt proceeds to pay capitalized interest due with the first debt service payment.) The levy proceeds are deemed appropriated for debt service, and must be deposited into an account in the debt service fund. (The interest payable from capitalized interest should be paid with capitalized interest.) [Ohio Rev. Code § 133.24(D)]

--Any amount so deposited and not needed for the purpose in the particular fiscal year may, without compliance with any other law or approval by any other agency, be transferred to the special fund established for the proceeds of the tax levy [Ohio Rev. Code § 133.24(D)] (such as a capital projects fund, if the tax was levied for both debt service and for a specific capital project.)

**Requirements applicable to BAN**

- Per Ohio Rev. Code § 133.22, the legislative body must pass legislation authorizing:

- The purpose for (eventually) issuing the bonds (which is limited to one purpose) [(A)(1)(a)]
  - The maximum amount of BAN, which cannot exceed the bond amount [(A)(2)(a)]
  - The maximum maturity, which cannot exceed (C). (See 133.22(C) below).
  - If the bonds are eventually payable from a property tax, the legislation provides for the levy of property taxes while the BAN are outstanding;
- **(Note:** We can normally rely on bond counsel for assuring compliance with the following provisions. This requirement is listed as background information for you.) Per §133.22(C), BAN issued with a latest maturity of less than two hundred forty months may be renewed for up to two-hundred-forty months.
- Per (C)(2), five years after issuing the original BAN, a portion of the principal shall be paid annually, in amounts at least equal to, and payable not later than the payment dates of, the principal that would have been paid if the government issued bonds at the expiration of the initial five-year period.
  - Per (C)(3), the latest maturity of BAN may not exceed the maximum maturity of the bonds anticipated plus five years. (Bond maturities can range from 5 to 50 years, per Ohio Rev. Code § 133.20.)
  - **Note:** There are exceptions to these general rules, but they are too complex to summarize here. (Refer to Ohio Rev. Code § 133.22(C) for exceptions.)
- (These features are listed for your information.) Per §133.22(D), BAN may include the following features:
- Put options (D)(6)
  - Issue commercial paper in lieu of BAN (D)(7)
  - Floating interest rates (D)(8)
  - Interest rate swaps (D)(9)(b)

### **Lake Erie Shoreline Improvements**

- The board of county commissioners pledges all revenue from levies of an excise tax to Port authorities who are part of the Lakeshore Improvement project<sup>44</sup>. The revenue must be used to fund or pay debt charges related to the construction of port authority facilities under an agreement between the county and port authority. (Ohio Rev. Code §4582.56(B))
- The port authority may issue special obligation bonds, and notes anticipating the proceeds of the bonds (BAN). (Ohio Rev. Code §4582.56(C))

<sup>44</sup> The Lakeshore improvement project includes constructing a port authority facility within one mile of the Lake Erie shoreline in a County whose territory includes a part of the Lake Erie shoreline at least fifty percent of the linear length of the county's border with other counties. (Ohio Rev. Code §4582.56(A))

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Bond Counsel/Lender Involvement</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

For notes issued during the audit period, inspect the debt legislation and determine under which Rev. Code statute the debt was issued. If that section is not listed in this Ohio Compliance Supplement Chapter (including Appendix C-1 of the OCS Implementation Guide), read the specific statute and amend the testing steps to include tests for the 5 debt requirements below. If a note is outstanding at the end of the audit period, include copies or a summary of documentation addressing the 5 compliance tests below in the permanent file.

Determine whether:

**Note:** For Lake Erie Shoreline Improvements only steps 4 and 5 apply.

1. Note proceeds did not exceed Ohio Rev. Code limits, typically limited by the related revenue estimate (RAN or TAN) or bond proceed (BAN) estimates. (We can normally rely on the work of bond counsel or the underwriter, if they were involved with a debt issue. We should inspect their conclusions for reasonableness and summarize for the permanent file.)
2. Notes did not exceed limitations on the time to maturity. (*Usually*, notes issued for operating expenses must mature in one year. Notes used for capital improvements have longer maturities. BAN can mature up to the life of the eventual bonds.) (We can normally rely on the work of bond counsel or the underwriter, if they were involved with a debt issue. We should inspect their conclusions for reasonableness and summarize for the permanent file.)
3. The government repaid the debt with the pledged or other legal revenue (RAN and TAN), or refinanced BAN according to the BAN legislation.

4. The government properly segregated any revenue pledged for debt service and used that revenue for debt service.
5. The government used the note proceeds for the purposes authorized.

**Audit implications (adequacy of the system and controls, and the direct and material effects of Non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-1514 Compliance Requirement:** Ohio Rev. Code § 3375.404 - Additional borrowing authority for boards of library trustees.

**Summary of Requirements:** Ohio Rev. Code §3375.404 allows a board of library trustees of a public library that receives an allocation of the library fund to anticipate its portion of the proceeds of the library fund distribution and issue library fund facilities notes to pay the costs of financing the facilities (or certain other property), or to refund any refunding obligations.

A library board may issue such notes only if it projects that the annual note service charges (including interest, repayment of principal, and redemption premiums) are capable of being paid from the library’s annual Library and Local Government Support Fund (LLGSF) (also known as: “public library funds”) receipts.

The maximum annual debt service for these notes cannot exceed 30% of the average LLGSF funding (public library funds) the library received for the two years preceding the year the notes were issued.

The notes are payable from the LLGSF monies (public library funds) received by the library board issuing the notes, or from the proceeds of notes, refunding notes, or renewal anticipation notes which may be pledged for such payment in the authorizing resolution. The notes are payable solely from the funds pledged for their payment as authorized by Ohio Rev. Code §3375.404 and all notes must contain on their face a statement to that effect.

The maximum maturity, in the case of any anticipation notes, cannot exceed 10 years from the date of issue of the *original* anticipation notes.

For *refunding* notes or any notes that are not anticipation notes, the maximum maturity cannot exceed 25 years from the date of the original issue of notes.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Bond Counsel/Lender Involvement</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

By reading the minutes, inspecting bond ledgers or other documents, or by inquiry, determine if the library used this type of borrowing.

Calculate, or inspect the library's calculations, that the maximum annual note debt service charges does not exceed 30% of the average LLGSF funding (public library funds) for the two years preceding the year in which the notes are issued. (This step should only apply in the year notes were issued.)

Inspect the notes for the statement that the notes are payable solely from the ~~resources~~ funds pledged for their payment as authorized by Ohio Rev. Code §3375.404. In other words, ensure the debt service funds were allocated to the appropriate fund(s) based on the legal authority to retire the debt.

Inspect the notes for the maximum maturities of 10/25 years.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-1615 Compliance Requirement:** Ohio Rev. Code §133.29, 135.14, 731.56 - Governments investing in their own securities.

*Note:* Entities must have the legal authority to **both buy and sell** the debt. Ohio Rev. Code §133.29 authorizes entities to invest in their own securities; however, there must be a separate, specific authority to issue the debt before the Bond Retirement or other authorized Fund may purchase it.

### Summary of Requirement:

#### Manuscript and Treasury Debt in General

Before a taxing authority sells any securities of the subdivision to others, the taxing authority may offer the securities at their purchase price and accrued interest to the subdivision. The securities may be offered to the officer or officers who have charge of the bond retirement fund of the subdivision, or in the case of a municipal corporation, to the treasury investment board, or an officer or similar treasury investment board having the authority under a charter. (Ohio Rev. Code §133.29) Ohio Rev. Code §133.01(NN) defines a "taxing authority" to include a county's board of county commissioners, a municipal corporation's legislative authority, a school district's board of education, and a township's board of township trustees, among others defined in the Code.

This type of debt is often referred to as "manuscript debt" or "treasury debt". Manuscript or treasury debt can be outstanding for five years, unless it is matched to a specific obligation or debt of the subdivision (such as obligations of the debt retirement fund). [Ohio Rev. Code §135.14(D)]

Any securities sold under this section shall bear interest at a rate(s) that is a fair market rate(s) for such securities at the time of the sale, and a certificate of the fiscal officer that the interest rate(s) borne by the securities is the fair market rate(s) is binding as to the statements set forth. [Ohio Rev. Code §133.29(B)]

Interest earned on the principal of any special fund, regardless of the source or purpose of the principal, is revenue derived from a source other than the general property tax for which the law does not prescribe use for a particular purpose and shall be paid into the general fund. (1985 Op. Atty. Gen. No. 85-072)

In addition to a taxing authority's ability to direct the bond retirement fund of the subdivision to purchase its securities, certain taxing authorities have additional options for purchasing manuscript or treasury debt.

#### County

A County may invest its "inactive moneys" in bonds or other obligations of the County. (Ohio Rev. Code §135.35(A)(4)) Ohio Rev. Code §135.31 defines a county's "inactive moneys" as all public moneys in public depositories in excess of the amount determined to be needed as active moneys (which are the amount of public moneys in public depositories determined to be necessary to meet current demands upon a county treasury, and deposited in a commercial or money market account). There is no limit on what fund the inactive moneys must be drawn from, so there is more flexibility for purchasing manuscript or treasury debt.

#### Other Political Subdivisions in General

All other political subdivision investments are addressed in Ohio Rev. Code §135.14. The statute permits a political subdivision to invest "interim moneys" in a series of investment categories. "Interim moneys" are defined in Ohio Rev. Code §135.01(F) as public moneys in the treasury of the state or any subdivision after the award of inactive deposits has been made in accordance with Ohio Rev. Code §135.07, which moneys are in excess of the aggregate amount of the inactive deposits (a public deposit other than an interim deposit or an active deposit) as estimated by the governing board prior to the period of designation and which the treasurer or governing board finds should not be deposited as active or inactive deposits for the reason that such moneys will not be needed for immediate use but will be needed before the end of the depository period of designation. The depository period of designation is the period of time during which the governing board has designated a public depository for public moneys of the subdivision, a designation that must be made once every five years. (Ohio Rev. Code §135.12(B)) An "active deposit" is defined as a public deposit necessary to meet current demands on the treasury.

### **Municipal Corporation (City and Village)**

In addition to the bond retirement fund options provided in Ohio Rev. Code §133.29, a municipal corporation (city or village) may invest moneys in the treasury that will not be required to be used for a period of six months or more in the obligations of the municipal corporation (Ohio Rev. Code §731.56). For the purposes of this section, any "interim moneys" or "inactive deposits" that will not be needed within six months may be invested. Similar to the rules for a County, there is no prescription as to which fund the "interim moneys" or "inactive deposits" must be drawn from.

Ohio Rev. Code §731.57 and 731.58 add some extra qualifiers for manuscript or treasury debt investments. Before the investment is made, the auditor or chief fiscal officer must certify to the mayor or village solicitor/law director the probable requirements of money for the use of the municipal corporation for the next six months. The mayor or village solicitor/law director may then order the investments. It is not necessary to advertise bonds to make such an investment.

When a municipal corporation acts to convert such investments into cash, the obligations must first be offered to the sinking fund commission. If the sinking fund commission does not purchase the investments, they may then be sold in any manner authorized by law for the sale of investments by the sinking fund.

For as long as the treasury maintains these investments, they are held in a "treasury investment account". The chief accounting officer of the municipal corporation will enter all transactions relating to the investment of treasury funds in security obligations of the municipal corporation. When securities or interest coupons are due, the accounting officer shall collect them in the same manner as other receipts are collected.

~~Interest earned from the investment or deposit of tax revenues must be allocated to the fund to which the principal belongs. (1980 Op. Atty. Gen. No. 80-003)~~

### **Charter Municipal Corporations**

If a municipal corporation has adopted a charter, it may adopt its own set of investment principles that may be different from those expressed in the Ohio Revised Code. Ohio Rev. Code § 133.29 authorizes a municipal corporation that has a charter to authorize a treasury investment account that would operate in the same way as a municipal corporation treasury investment account under Ohio Rev. Code § 731.56. Beyond this provision, a municipal corporation may adopt a charter that

addresses its ability to invest in manuscript or treasury debt as long as it does not conflict with general laws. (Ohio Const. Art. XVIII, Section 3.).

### **School Districts**

School districts do not have any options for manuscript or treasury debt beyond using moneys in the bond retirement fund as discussed in Ohio Rev. Code § 133.29, 1955 Op. Atty. Gen. No. 55-5263). Such a transaction will be considered an investment of the sinking fund or bond retirement fund, and interest will be deposited and reinvested just like other investments of the sinking fund or bond retirement fund.

### **Townships**

Townships do not have any options for manuscript or treasury debt beyond using moneys in the bond retirement fund as discussed in Ohio Rev. Code §133.29.

### ***Accounting for Manuscript Debt***

There are two methods for recording manuscript debt in the accounting records:

#### *Investment Method*

Record proceeds from the sale of notes in the borrowing fund (often the general fund or project fund). Then record the amount received from the Bond Retirement Fund (or other authorized fund in the case of municipal corporations) as an investment on the investment record. Do not decrease the Bond Retirement or other authorized fund's balance. When preparing the bank reconciliation, outstanding securities should be included as an investment.

The county auditor, having been properly notified of the debt service requirements, should allocate property taxes on the tax settlement among the proper funds. The amount payable to the Bond Retirement or other authorized fund is the amount necessary to repay the principal plus interest on the outstanding securities. Debt service principal and interest, should be recorded in the Bond Retirement or other authorized fund. Upon payment of principal, a corresponding reduction of the investment should be recorded on the investment record.

#### *Advance/Interfund Method*

Record an advance-in in the debtor (borrowing) fund and a corresponding advance-out of the creditor (loaning) fund. Also, governments reporting under GAAP should record an interfund asset and offsetting interfund liability for both modified and full accrual bases. If the borrowing is between a governmental activity and a business type activity, the entity wide statements should also report this as an internal balance (GASB Cod. 1300.120 and 1800.102(a)).

Governments reporting under GAAP must use the Advance/Interfund method for financial statement reporting (2013-14 2015-1 GASB ~~Comprehensive~~ Implementation Guide Q&A 6.4.5). This means that if a GAAP entity uses the Investment Method for their accounting records, they must convert the transactions to the Advance/Interfund Method during the GAAP conversion.

GAAP, Cash, and OCBOA basis governments should disclose the fund liabilities, including interest rates and repayment schedules, in their notes under either accounting method.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Bond Counsel/Lender Involvement</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

Determine whether the entity issued manuscript debt during the audit period or has any manuscript debt outstanding as of fiscal year end.

If so, review the governing body’s ordinance or resolution approving the issuance and determine the legal authority under which such debt/investment was issued. If applicable, we may rely on an opinion from bond counsel to verify the entity’s legal authority for issuing such debt. A copy of the ordinance or resolution and bond counsel opinion should be placed in the permanent file.

Determine the issuance date<sup>45</sup> of the debt/investment and review the entity’s debt/investment schedules to determine whether the principal matured within five years.

Review the entity’s debt/investment schedules and determine whether the entity has charged interest at the proper rate and amount in the Bond Retirement or other authorized fund.

***For all entities other than municipal corporations,*** determine whether the amount of manuscript debt issued was limited to the available resources in the bond retirement fund.

***For counties and municipal corporations,*** determine whether the amount of manuscript debt issued was limited to the available resources in the general treasury or other authorized fund.

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<sup>45</sup> Issuance date isn’t always the sale date. If the “Obligation’s Closing Date” is the actual date of the issuance, this should be recorded as the issuance date.

Scan the entity's debt schedules, investment records, monthly bank reconciliations, and annual financial statements to determine whether the entity has properly accounted for all manuscript debt transactions (i.e., note proceeds, property tax and interest receipt allocations, debt service payments on principal and interest, and outstanding debt and investment amounts).

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

## Section D: Accounting and Reporting

### GENERAL

**1-1716 Compliance Requirements:** Ohio Admin. Code § 117-2-03(B) and 126:3-1-01(A)(2)(a) and Ohio Rev. Code § 117.38 ~~and~~ §1724.05 and §1726.11, and AOS Bulletin 2015-007 - Annual financial reporting.

#### Summary of Requirements:

**Note:** The Auditor of State (AOS) ~~is in the process of~~ has implemented the Hinkle Annual Financial Data Reporting System (Hinkle System – formerly AFDRS). ~~AFDRS~~ The Hinkle System is an Internet based application that allows certain financial statement, debt, and demographic data to be entered, uploaded and transmitted to the AOS to satisfy the filing requirements prescribed by the Ohio Revised Code (ORC) and the Ohio Administrative Code (OAC). All cities and counties were required to report via ~~the Hinkle System~~ AFDRS for periods ended December 31, 2013 and thereafter, and all schools, community schools and educational service centers were required to report via ~~the Hinkle System~~ AFDRS for periods ended June 30, 2014 and thereafter. All townships, villages and libraries ~~will be~~ were required to report via ~~AFDRS~~ the Hinkle System for periods ~~ending~~ ended December 31, 2014 and thereafter. All other entity types required to file with the AOS are required to report via the Hinkle System for periods ended in 2015 and thereafter ~~will be phased into AFDRS reporting.~~ Please refer to the AOS website at <https://ohioauditor.gov/financialreporting/default.html> and AOS Bulletin 2015-007 for additional information.

#### **Generally Accepted Accounting Principles (GAAP) Basis Entities**

Ohio Admin. Code §117-2-03(B) requires counties, cities, school districts, educational service centers, ~~and~~ community schools and government insurance pools (except those established under Ohio Rev. Code Chapter 167)<sup>46</sup> to report annually (but not necessarily account) on a GAAP basis.

Ohio Rev. Code §1724.05 and §1726.11 require community improvement corporations, including economic development corporations and county land reutilization corporations, and development corporations established under Ohio Rev. Code Chapter 1724 and 1726, respectively, and colleges and universities pursuant to Ohio Admin. Code §126:3-1-01(A)(2)(a) to report annually (but not necessarily account) on a GAAP basis.

<sup>46</sup> Ohio Admin. Code §117-2-0(B) was amended in 2015 to require government insurance pools to prepare their annual financial reports pursuant to GAAP. The new GAAP filing requirement is effective for annual financial report filings for periods ending December 31, 2016.

Per Ohio Rev. Code §117.38, entities filing on a GAAP-basis must file annual reports within 150 days of their fiscal year end (except Ohio Rev. Code §1724.05 and §1726.11 require community improvement corporations and development corporations to file within 120 days of their fiscal year end). Colleges and universities must file by October 31<sup>st</sup> per Ohio Admin. Code §126:3-1-01(A)(2)(a).<sup>47</sup>

Per AOS Bulletins ~~2006-002 and 2008-001~~2015-007, annual reports filed with AOS must be **complete** to avoid the application of a penalty of \$25 per day (\$750 maximum) permissible under Ohio Rev. Code §117.38. To be **complete**, GAAP entities must submit the basic financial statements, including the government-wide financial statements, fund financial statements, notes to the basic financial statements, Management’s Discussion & Analysis, and any other required supplementary information to be considered a complete filing.<sup>48</sup>

### **Cash Basis Entities**

Per Ohio Rev. Code §117.38, entities filing on a cash-basis<sup>49</sup> must file annual reports with the Auditor of State within 60 days of the fiscal year-end. The Auditor of State may prescribe by rule or guidelines the forms for these reports. However, if the Auditor of State has not prescribed a reporting form, the public office<sup>50</sup> shall submit its report on the form used by the public office. Any public office not filing the report by the required date shall pay a penalty of \$25 for each day the report remains unfiled, not to exceed \$750.<sup>48</sup> The AOS may waive these penalties, upon the filing of the past due financial report.

<sup>47</sup> We will cite noncompliance if a “GAAP mandated public office government” files special purpose framework (OCBOA) - cash, modified cash or regulatory cash financial statements. The following cite would apply:

“Ohio Admin. Code §117-2-03 (B) requires the County to prepare its annual financial report in accordance with generally accepted accounting principles. The County filed financial statements with the Auditor of State, but those statements followed a cash and investments accounting basis rather than generally accepted accounting principles. The accompanying financial statements and notes omit material assets, liabilities, fund equities, and disclosures. The County is subject to fines and various other administrative remedies.”

(For this finding we need not differentiate AOS Regulatory cash vs OCBOA cash/modified cash basis formatting or list the date the statements were filed, because it is irrelevant.)

<sup>48</sup> Failing to file an annual report could be a symptom of an inadequate accounting system, inadequate training of personnel in understanding the accounting and reporting process, unposted or unreconciled records or other significant issues affecting the control environment, or which may even pose fraud risks. It may also result in the entity being declared “unauditable” by the Auditor of State. This also applies for OCBOA cash, OCBOA modified cash and regulatory cash basis financial statements.

<sup>49</sup> Cash basis includes special purpose framework (OCBOA)-cash, OCBOA modified cash and regulatory cash basis.

<sup>50</sup> Ohio Rev. Code §117.01(D) states that, as used in Ohio Rev. Code Chapter 117, “*public office* means any state agency, public institution, political subdivision, or other organized body, office, agency, institution, or entity established by the laws of this state for the exercise of any function of government.” 1989 Op. Atty. Gen. No. 89-055 indicates the Auditor of State has discretion to interpret and apply the definition of “public office” used in Ohio Rev. Code §117.01(D). The Auditor of State has therefore determined that ~~charter~~ community schools qualify as public offices as defined under this section.

The report shall contain the amount of: (A) receipts, and amounts due from each source; (B) expenditures for each purpose; (C) income of any public service industry the entity owns or operates, as well as the costs of ownership or operation; and (D) **public debt** of each taxing district, the purpose of the debt, and how the debt will be repaid. *Note:* Using AOS shell reports will meet this requirement<sup>51</sup>.

*Note:* We normally would not deem a late filing to constitute “direct and material” noncompliance on the determination of financial statement amounts (i.e. the auditor would normally not report a late filing citation in the GAGAS compliance report, however the auditor should issue a management letter comment for late filings.)

Material noncompliance would exist if:

- An entity subject to GAAP did not follow GAAP in its annual report.
- An entity’s GAAP filing was significantly incomplete (see discussion of complete in the *GAAP Basis Entities and Cash Basis Entities* sections above).
- The filing was significantly misstated.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Presence of an Effective Accounting System</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

~~Inquire if the government files its financial reports with the Auditor of State on a GAAP basis.~~

Confirm whether the report was filed timely.

<sup>51</sup> For OCBOA-cash or OCBOA-modified cash basis, to be **complete**, the applicable basic financial statements, must include the government-wide financial statements, fund financial statements, notes to the basic financial statements, and Management’s Discussion & Analysis (optional). ~~For AOS Regulatory cash basis to be **complete**, the applicable basic financial statements include statement(s) or combined statement(s) of receipts, disbursements and changes in fund balance – governmental, proprietary and fiduciary, as applicable and notes to the basic financial statements.~~

*Note:* The ~~AFDRS~~Hinkle System tracker and/or GPIInfoSearch includes due dates and filing dates. Auditors should check the tracker to determine compliance with due dates. If an entity's report was not filed by the required due date or by an approved extension date, a management letter comment should be issued.<sup>52</sup>

Auditors should inspect the filed report (~~in most cases~~AOS auditors can obtain this report through ~~AFDRS~~the Hinkle System tracker and/or GPIInfoSearch. GPIInfoSearch information is available to contracted IPA firms for their clients via logging into the IPA Portal.) ~~if AFDRS access is unavailable obtain a copy of the filed report retained and available in the fiscal office) to determine whether a filing was substantially complete.~~

Trace selected totals from the filed report to the underlying accounting system. (*If we use the filed report as a trial balance, AOS auditors will satisfy this requirement by completing the mandatory Trial Balance steps from the financial audit program.*) If the report is significantly deficient, we should cite Ohio Rev. Code §117.38, ~~or~~ §1724.05, §1726.11 or Ohio Admin. Code §126:3-1-01(A)(2)(a), as appropriate, for filing an incomplete or misleading report.<sup>53</sup>

Determine whether the filed report includes the ~~financial statements, notes to the financial statements, disclosures~~ and required supplementary information (if applicable)<sup>54</sup> ~~required by GAAP~~ (i.e. determine if the filing was substantially *complete* as described above).

**Beginning with audits of financial periods ending in 2016,** the AOS (and any independent public accounting (IPA) firms contracted to perform audits for the AOS) will audit the financial statements uploaded and submitted to the AOS via the Hinkle System. At the commencement of the audit, the AOS or IPA must verify with the public office that the financial statements submitted via the Hinkle System are the final, unaudited financial statements for the audit period. If the public office or other entity required to file indicates the financial statements filed for the audit period require modification, the entity must contact the AOS at [HinkleSystem@ohioauditor.gov](mailto:HinkleSystem@ohioauditor.gov) in order to reset their Hinkle System filing status enabling the public office to re-file. The filing date and accounting basis of the re-filed annual financial report will then become the basis for determining compliance with the filing requirements<sup>55</sup>. Failure to file via the Hinkle System may result in the AOS declaring the public office "unauditable."

<sup>52</sup> Auditor judgement may be required to determine if a non-compliance citation should be issued.

<sup>53</sup> Auditors should evaluate and document, using professional judgment, whether the financial statements are significantly deficient requiring a citation and, if cited, the level of that citation (report, management letter, verbal). AOS auditors should evaluate the necessity of a control deficiency using guidance from AU-C 265 and AOSAM 38100 AOS specific guidelines.

<sup>54</sup> Reporting non-compliance for cash basis entities not including notes to the basic financial statements with their annual Hinkle System filing (AOS Bulletin 2015-007) will be considered for periods ending in 2016 and beyond. For periods ended in 2015, the auditor or IPA should verbally notify the entity of the requirement and document the notification in the work papers.

<sup>55</sup> For 2016 year end engagements, including biennial periods 2015-2016 or 2016-2017, if the public office or other entity required to file originally submitted timely but must refile in order for the AOS/IPA firm to audit the financial statements submitted via the Hinkle System, noncompliance with filing deadlines should be communicated verbally rather than including a citation in the management letter. However, GAAP mandated public offices should be cited if the final financial statements filed via the Hinkle System are not GAAP basis.

For subsequent periods, auditor judgment may be required to determine if a non-compliance citation should be issued.

If the government is not mandated to follow GAAP and presents AOS Basis Regulatory cash basis (“AOS basis”) ~~special purpose framework~~ financial statements (instead of rather than OCBOA cash or OCBOA modified cash financial statements ~~special purpose framework~~ (“GAAP look-alike”)):

- Follow AU-C 800.21 which retained the guidance from AOS Bulletin 2005-002 and applies when regulatory cash basis statements are available for general use (local government statements we or IPA’s audit are available for general use). AU-C 800.21 requires issuing a dual opinion:
  - An adverse opinion on conformance with GAAP.
  - A second opinion on the regulatory cash basis.

If a GAAP-mandated government does not follow GAAP or present OCBOA cash or OCBOA modified cash ~~special purpose framework~~ (“GAAP look alike”) basis financial statements but presents Regulatory cash basis (“AOS Basis”) ~~special purpose framework~~ financial statements:

- Issue adverse opinion on conformance with GAAP
  - These governments do not qualify for the “dual opinion.”
- Issue GAGAS noncompliance finding

If a GAAP-mandated government presents their financial statements using an OCBOA ~~special purpose framework~~ cash or OCBOA modified cash basis (“GAAP look-alike statements”):

- Follow AU-C 800.A25 which requires auditors to include an emphasis of matter paragraph following the opinion paragraph alerting the users of the auditor’s report that the financial statements are prepared in accordance with a special purpose framework (OCBOA) basis of accounting and that the basis of accounting is a basis of accounting other than GAAP.
- Issue GAGAS noncompliance finding

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-1817 Compliance Requirements:** Ohio Rev. Code § 1724.05 and 1726.11 - GAAP and annual financial reporting for community improvement corporations (CICs)<sup>56</sup> and development corporations (DCs).<sup>57</sup>

**Summary of Requirements:** Annual Reporting

- Corporations must submit (unaudited) annual GAAP financial reports to the Auditor of State. The corporation must file the annual report within 120 days of fiscal year end.<sup>58</sup> The Ohio Revised Code does not prescribe a fiscal year end for these corporations.

**Failure to Report/Present Auditable Records** (Ohio Rev. Code §1724.06- CICs and § 1726.12-DCs)

- Additionally, the Auditor of State must certify corporations to the Secretary of State in the following two circumstances:
  - If a Corporation files its annual report more than 90 days delinquent (i.e., does not file its annual GAAP financial statement report within 120 days of its fiscal year end).
  - If a Corporation does not present auditable records within 90 days of a determination by the Auditor of State that a corporation is unauditable.
- The certifications are issued by the Legal Division once the regional chief auditor receives approval from the Chief Deputy Auditor.
- Upon certification, the Secretary of State is to cancel the Corporation's articles of incorporation until the deficiency is remedied.
- For more information, see AOS Bulletin 2001-003.

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<sup>56</sup> Being non-profit under chapter 1702 is not enough to be a CIC. To be a CIC requiring an AOS audit, the entity must be incorporated under both 1702 & 1724. (A Development Corp. would only be incorporated under chapter 1726.) Read the articles and see if they refer to chapters 1724 or 1726. Merely titling an entity as an "improvement" or "development" corporation is not sufficient. The articles of incorporation must support that the entity falls under 1724 or 1726.

<sup>57</sup> Development corporations organized under Ohio Rev. Code Chapter 1726 are stock-issuing entities.

<sup>58</sup> CICs or DCs that do not file GAAP statements and notes (and required supplementary information, if any) within 120 days of its fiscal year end are *not* subject to AOS penalties prescribed in Ohio Rev. Code §117.38. "A community improvement corporation is, in essence, a private non-profit corporation which is bound by the general terms of Ohio Rev. Code Chapter 1702 (non-profit corporations). A privately organized entity that performs a public purpose occupies a status no different from that of countless other non-profit corporations, the private nature of which is indisputable. Nor is a community improvement corporation possessed of powers derived from statute. Although Ohio Rev. Code § 1724.02 provides that a community improvement corporation shall possess certain powers enumerated therein, the ultimate source of its power is not Ohio Rev. Code § 1724.02, but its articles of incorporation and code of regulations." [1979 Op. Atty. Gen. No. 79-061] Also, auditors should take note that CIC and DC are subject to a 120-day filing requirement rather than the 150-day requirement applicable to other GAAP entities.)

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Presence of an Effective Accounting System</li> <li>• Legislative and Management Monitoring</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Read the corporation’s annual report. Determine if it complies with GAAP in material respects.

If a corporation does not file its annual GAAP financial statement report, or does not present auditable records within 90 days of the Auditor of State’s determination of unauditability:

- The Chief Auditor will consult with the Chief Deputy Auditor. The Chief Deputy Auditor will determine whether to request the Legal Division to issue a subpoena for the accounting records.
- IPA firms should contact the Regional Chief Auditor regarding these matters

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

*Section E: Deposits and Investments*

**NONE**

## Section F: Other Laws and Regulations

### VARIOUS ENTITY TYPES

**1-1918 Compliance Requirement:** Ohio Rev. Code §9.833, and §305.172 - Health Care Self Insurance<sup>59 60</sup>

**Summary of Requirement:** Ohio Rev. Code §9.833 requires individual, self-insured governments or joint self-insured health-care programs to calculate (i.e., reserve<sup>61</sup>) amounts required to cover health care benefit liabilities. (Health care insurance includes, but is not limited to health care, prescription drugs, dental care and vision care.) It also requires programs to prepare a report, reflecting those reserves (i.e., liabilities) and the aggregate of disbursements made to pay self-insured claims, legal and consultant costs during the preceding fiscal year. This report is not filed with any office, including the Auditor of State; the government should make it available upon request. Programs must prepare (i.e. obtain) and maintain a certified audited financial statement and a report of amounts reserved for the program and disbursements made from such funds. The program administrator must provide the report to the Auditor of State. The program must include a contract with a certified public accountant and a member of the American Academy of Actuaries for the preparation of the written evaluations described in this paragraph. (See AOS Bulletin 2011-008)

The provisions regarding the self-insurance programs do not apply to an individual self-insurance program created solely by municipal corporations. For this purpose, *municipal corporation* means all municipal corporations, including those that have adopted a charter under the Ohio Constitution.

An actuary must certify that the amounts reserved are fairly stated in accordance with sound loss reserving principles. The actuary must be a member of the American Academy of Actuaries.

Individual governments subject to this requirement must establish an internal service fund to account for this activity.

Per Ohio Rev. Code §9.833(E), some of the aforementioned requirements do not apply to municipalities. **Note:** Auditors should refer to AOS Bulletin 2011-008 for additional guidance.

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<sup>59</sup> Ohio Rev. Code §9.833(D) also permits subdivisions to procure group life insurance for its employees in conjunction with an individual or joint self-insurance program. However, neither a government nor a pool can self-insure for life insurance. (That is, a government must purchase life policies from commercial insurers.)

<sup>60</sup> Ohio Rev. Code §305.172 and Ohio Rev. Code §9.833(B)(2), permit political subdivisions and boards of county commissioners that provide health care benefits for their officers or employees to establish and maintain an individual health savings account program as part of their self-insurance program. These accounts must be maintained in accordance with section 223 of the Internal Revenue Code [26 U.S.C. §223]. Public moneys may be used to pay for or fund federally qualified high deductible health plans that are linked to health savings accounts or to make contributions to health savings accounts. Auditors should not audit compliance with Internal Revenue Code regulations governing health care savings accounts. Rather, be aware that such accounts may be included in self-insurance activity accounted for in the internal service or other appropriate fund as permitted by statute.

<sup>61</sup> “Reserve” in this context means liabilities measured in accordance with accepted actuarial principles.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>	asdf	

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Subdivisions<sup>62</sup> (except municipalities) must establish an internal service fund to account for health self-insurance activity. Determine if the subdivision established the required fund.

Inspect the actuary’s certificate (i.e. opinion) that the amounts reserved conform to accepted loss reserving standards. (This requirement does not apply to municipalities.)

Test information the subdivision submitted **to the actuary** to determine this information is supported by the client’s accounting or other applicable records. Testing information the client provides to the actuary<sup>63</sup> when the actuary’s liability calculation is accrued as a GAAP liability<sup>64</sup> or presented in a cash-basis entity’s notes.

Determine whether the actuary’s opinion language (including the scope of the work) generally complied with the example described in the “Actuarial Opinions” section of AOS Bulletin 2001-005.

Consider whether any qualification in the actuary’s report affects the financial statement opinion or indicates noncompliance with Ohio Rev. Code § 9.833.

<sup>62</sup> Ohio Rev. Code §9.833 and § 2744.01 define a subdivision as any municipal corporation, township, county, school district, or other body corporate and politic responsible for governmental activities in a geographic area smaller than the State. As used in Ohio Rev. Code §9.833, a “political subdivision” also includes the entity types described in Ohio Rev. Code §3905.36.

<sup>63</sup> AU-C 620 clarifies that the *Specialist* standard only applies to a specialist the auditor employs or contracts with. Auditors are responsible for testing the liability an actuary computes on behalf of the auditee using the *Evidence* standard in AU-C 500.

<sup>64</sup> As AOS Bulletin 2001-005 describes, actuarial principles for measuring these liabilities are similar but not identical to GAAP requirements per GASB 10. A government can use the actuarially-computed liability in its financial statements if it does not materially differ from GAAP measurement requirements.

Determine if a cash-basis (or AOS basis) government's audited statements disclose self-insurance activity based on the example disclosure in AOS Bulletin 2001-005. (For cash-basis entities, an inability to adequately calculate and present the liability may constitute a qualification related to the adequacy of disclosure.)

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**1-2019 Compliance Requirement:** Ohio Rev. Code §2744.081 - Liability Self Insurance

**Summary of Requirement:** This section requires joint self-insurance programs (such as governmental self-insurance pools) insuring against judgments, settlement of claims, expense, loss and damages that arise, or are claimed to have arisen, from an act or omission of the subdivision or any of its employees and to indemnify or hold harmless the subdivision’s employees, to reserve <sup>65</sup> amounts to cover potential costs. It also requires the program to prepare a report, reflecting those reserves (i.e., liabilities) and the aggregate of disbursements made to pay self-insured claims, legal and consultant costs during the preceding fiscal year. This report is not filed with any office, including the Auditor of State; it should be retained by the government and be made available upon request.

An actuary must certify that the amounts reserved are fairly stated in accordance with sound loss reserving principles. The actuary must be a member of the American Academy of Actuaries.

The aforementioned requirements apply only to governmental risk pools or other joint governmental liability insurance programs.

**Note:** Auditors should refer to AOS Bulletin 2001-005 for additional guidance.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Determine whether a report presenting the actuarially-measured liabilities and disbursements during the year was obtained.

Inspect the actuary’s certificate that the amounts reserved conform to accepted loss reserving standards.

<sup>65</sup> “Reserve” means liabilities measured in accordance with accepted actuarial principles.

Test information the client submitted to the actuary to determine this information is supported by the client's accounting or other applicable records. Testing information the client provides to the actuary is necessary<sup>66</sup> when the actuary's liability calculation is accrued as a GAAP liability<sup>67</sup> or presented in a cash-basis entity's notes.

Determine whether the actuary's opinion language (including the scope of the work) generally complied with the example described in the "Actuarial Opinions" section of AOS Bulletin 2001-005.

Consider whether any qualification in the actuary's report affects the financial statement opinion or indicates noncompliance with Ohio Rev. Code §2744.081.

Determine if a cash-basis (or AOS basis) government's audited statements disclose self-insurance activity based on the example disclosure in AOS Bulletin 2001-005. (For cash-basis entities, an inability to adequately calculate and present the liability may constitute a qualification related to the adequacy of disclosure.)

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

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<sup>66</sup> AU-C 620 clarifies that the *Specialist* standard only applies to a specialist the auditor employs or contracts with. Auditors are responsible for testing the liability an actuary computes on behalf of the auditee using the *Evidence* standard in AU-C 500.

<sup>67</sup> As AOS Bulletin 2001-005 describes, actuarial principles for measuring these liabilities are similar but not identical to GAAP requirements per GASB 10. A government can use the actuarially-computed liability in its financial statements if it does not materially differ from GAAP measurement.

**1-2120 Compliance Requirement:** Ohio Rev. Code §117.13(C)(3) and 2CFR 200.425 – Allocating Audit Costs.

**Summary of Requirements:** Local governments can charge audit costs to funds other than the general fund only if the charges are properly allocated to those funds.

CAUTION: This may not be material; if this is immaterial you may reduce or eliminate testing.

**Ohio Rev. Code § 117.13(C)(3)** states the fiscal officer may distribute such total cost of the audit to each fund audited in accordance with its percentage of the total cost.

**AOS Bulletin 2009-011** includes the following guidance for allocating audit costs to funds:

The fiscal officer should determine which funds should be charged a percentage of the audit costs. The Auditor of State is of the opinion that most operating funds of a local government, including utility funds (i.e., water, sewer, electric, refuse), special levy funds, funds that receive gas taxes, and motor vehicle registration fees can be charged a portion of the audit costs.

Other funds of a local government that may be charged a percentage of the audit costs include bond and grant funds. The ability to charge bond funds will depend on the allowable uses defined in the bond legislation. Trust and other funds that receive donations restricted to specific purposes will require analysis by the fiscal officer of the restrictions imposed by the donor and/or trust agreement to determine if any audit costs may be charged to those funds. Agency funds, because of their custodial nature, should not be charged for any share of the cost of an audit for the fiscal officer's role as the fiscal agent.

In determining a percentage of total cost that may be charged to a fund, any reasonable and rational method such as a percentage of the fund's revenue or expenditures compared to the total revenue or expenditures for all funds, excluding agency funds, would be acceptable. A local government's indirect cost allocation plan may also be an acceptable method for allocating audit costs.

**Effective for Federal awards made ON OR BEFORE December 26, 2014.** For grant funds, the costs of audits are allowable if the audits were required by and performed in accordance with the Single Audit Act and Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." (Also see 31 USC 7505(b), A-133.230 and 2CFR 225, Appendix B, item 4). Generally, the percentage of costs charged to Federal awards for a single audit shall not exceed the percentage derived by dividing Federal funds expended by total funds expended by the recipient or sub-recipient (including program matching funds) during the fiscal year. The percentage may be exceeded only if appropriate documentation demonstrates higher actual costs. Other audit costs are allowable if specifically approved by the awarding or cognizant agency as a direct cost to an award or included as an indirect cost in a cost allocation plan or rate.

**Effective for new Federal awards and certain incremental funding to existing awards made AFTER December 26, 2014.** For grant funds, a reasonably proportionate share of the costs of audits required by, and performed in accordance with the Single Audit Act and Uniform Guidance (UG), "Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards" are allowable. See 2CFR 200.425 for further explanation of allowable and unallowable audit costs and UG FAQ.425.1-5 for guidance when the auditee charges non-single, internal, legislative or performance audit costs.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Time summaries / timecards</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Determine if the government charges funds other than the general fund for audit costs. If so, review documentation supporting how the government determines a reasonable basis for allocating audit costs to funds other than the general fund. (Lack of formal documentation should not result in a citation or finding for adjustment if the allocation is reasonable.)

Determine if the government allocates audit costs to grant funds. If so, review documentation supporting the government ~~received a Single Audit and~~ allocated the audit costs to grant funds in accordance with Federal guidelines.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**If the compliance attributes listed in 1-22 below were tested during payroll substantive testing, no additional tests are needed.**

**1-2221 Compliance Requirements:** Various ORC Sections - Vacation and sick leave.

**Vacation leave:**

Ohio Rev. Code § 325.19 and § 3319.084 prescribe vacation benefits for **county** and **school non-teaching employees**, respectively. See tables below.

The governing authorities of other local governments set vacation policy by statute, ordinance or charter. However, collective bargaining agreements supersede local statutes, ordinances or charters.

**Ohio Rev. Code § 325.19 —County vacation leave**

<b>Ohio Rev. Code § 325.19 <u>Years of service</u></b>	<b><u>Vacation leave earned</u></b>
<1	0
≥1 but <8	80 hrs. per year
≥8 but <15	120
≥15 but <25	160
≥25	200

*Note:* Employees of county departments of jobs and family services accrue vacation pursuant to Ohio Rev. Code § 124.13. However, this Section prescribes the same vacation accruals as does Ohio Rev. Code § 325.19, above. Additionally, if a separation from county service occurs in connection with the lease, sale, or other transfer of all or substantially all the business and assets of a county hospital organized under Ohio Rev. Code Chapter 339 to a private corporation or other entity, the county shall have no obligation to pay any compensation with respect to unused vacation leave accrued to the credit of an employee who accepts employment with the acquiring corporation or other entity, if at the effective time of separation the acquiring corporation or other entity expressly assumes such unused vacation leave accrued to the employee's credit.

**Ohio Rev. Code § 3319.084 - School nonteaching employee vacation leave**

<b>Ohio Rev. Code §3319.084 <u>Years of service</u></b>	<b><u>Minimum vacation leave earned</u></b>
<1	0
≥1 but <10	2 weeks
≥10 but <20	3 weeks
≥20	4 weeks

**Ohio Rev. Code §9.44** generally requires an Ohio local government to include an employee’s prior service with the State or other Ohio local governments when computing vacation leave. However,

there are exceptions to this general rule. While this would rarely, if ever, be significant, if this applies to an employee’s leave you are testing, see Ohio Rev. Code §9.44 regarding the exceptions.

**Sick leave:**

Ohio Rev. Code § 124.38 prescribes 4.6 hours of sick leave for each 80 hours of completed service (120 hours / year), applicable to **county** (except for superintendent and management employees of County Boards of Development Disabilities defined in Ohio Rev. Code § 5126.20), **city, and civil service township service**. Ohio Rev. Code § 124.38 also applies to employees of any **state college or university**, and **certain board of education employees** (board of education employees for whom sick leave is not provided by Ohio Rev. Code § 3319.141).

Ohio Rev. Code § 3319.141- Sick leave for **school employees**: Earn 1¼ days per month (15 days / year), accumulating to a maximum of 120 days. However, a school board may adopt a policy permitting accumulations > 120 days. The requirements of Ohio Rev. Code § 3319.141 do not apply to substitutes, adult education instructors who are scheduled to work the full-time equivalent of less than one hundred twenty days per school year, or persons who are employed on an as-needed, seasonal, or intermittent basis.

Per Ohio Rev. Code § 124.39, employees governed by Ohio Rev. Code § 124.38 and employed for ≥ 10 years, are eligible for payment of 25% of their unused sick leave balance, up to a maximum of 30 days, upon retirement.

**Note:** These sections describe minimum vacation and sick leave. Governments generally may provide more than the minimum. These sections also prescribe procedures for paying the employees’ accumulated leave balances upon separation from service.

**POSSIBLE NONCOMPLIANCE RISK FACTORS:**

**Note:** Auditors should consider whether governments have vacation and sick leave policies placed in operation and have historically demonstrated effective internal controls over payroll and related compliance requirement. Additionally, adequate training of payroll personnel and supervisory monitoring controls can help mitigate the risk of noncompliance with vacation and sick leave compliance requirements.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Time summaries / timecards</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> </ul>		

<ul style="list-style-type: none"><li>• Management’s communication of changes in laws and regulations to employees</li></ul>		
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**Suggested Audit Procedures - Compliance (Substantive) Tests:**

**For GAAP entities, it is usually efficient to include these procedures when testing the financial statement liability for compensated absences.**

1. Obtain a copy of resolutions, ordinances or collective bargaining agreements setting vacation leave. Maintain an up to date copy in the permanent file.
2. Determine the procedures followed for recording the accrual and use of sick leave and vacation. (If leave accrual is automated and online with standing data, very limited recomputations of additions to leave balances should suffice for testing credits (i.e. additions) to leave accrual.)
3. Review the calculations of employees’ leave balances credited and used, including appropriate leave forms. Determine whether the computations use the hours the Ohio Revised Code, local legislation or collective bargaining agreements authorize.
4. Determine if any employees left service this year. For a representative number of employees who left service determine whether the computations use the hours the Ohio Revised Code, local legislation or collective bargaining agreements authorize.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**If the compliance attributes listed in 1-23 below were tested during payroll substantive testing, no additional tests are needed.**

**1-2322 Compliance Requirements:** Internal Revenue Code (IRC) Chapter 26 [26 U.S.C.] - Collection of Income Tax at Source on Wages; 26 U.S.C. §3401 through 3406:

- §3401: Definitions;
- §3402: Withholding of income tax from wages;
- §3403: Employers liable for payment of the tax deducted and withheld;
- §3404: Return of amount deducted and withheld shall be made by appropriate officer of the governmental employer;
- §3405: Withholding on pensions and annuities;
- §3406: Backup withholding
  
- 26 U.S.C. §3102(a): Deduction of [Medicare] tax from wages;
- 26 U.S.C. §132: Exclusion of certain fringe benefits from gross income;
- Internal Revenue Regulations (26 C.F.R.):
  - §1.61-21: Taxation of fringe benefits;
  - §1.6041-1: Reporting of income aggregating \$600 or more [i.e., 1099s-MISC]<sup>68</sup>;
  - §1.6041-2: Reporting of wage income aggregating \$600 or more [i.e., W-2s];
  - §1.6041-3: Various exclusions;
  - §1.6041-6: Time and place for filing forms 1099 and 1096;
  - §1.6050E-1: Income tax refund reporting.
- Ohio Rev. Code §5747.06 - Collection of Ohio income tax at source.
- Various local ordinances require withholding on wages earned in the particular municipality. These should be consulted for the requirements.

**Summary of Requirement:**

These sections of the various tax codes require the employing government to withhold federal, state, and local income and employment-related taxes (such as Medicare). They also require the government to report those tax matters to the appropriate tax authorities and to the recipients. Certain of these sections require consideration of whether employer-provided “fringe” benefits, such as use of government automobiles for private purposes, constitute taxable income to be reported and withheld upon.

Effective for tax years beginning after December 31, 2009, Section 2043 of the Small Business Jobs and Credit Act of 2010 (Public Law No. 111-240) removed employer-provided cell phones from the definition of “listed property” in the tax code. While cell phones are still subject to being a taxable benefit, the new legislation removes the special record-keeping requirements of listed property. However, employers still should have a policy prohibiting any more than a de minimis personal use of government-owned cell phones.

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<sup>68</sup> All payments to attorneys of \$600 or more that are not otherwise reported (e.g., on form W-2 for attorneys who are employees) must be reported on form 1099-MISC.

**POSSIBLE NONCOMPLIANCE RISK FACTORS:**

**Note:** Auditors should consider whether governments have historically demonstrated effective internal controls over payroll. Additionally, adequate training of payroll personnel and supervisory monitoring controls can help mitigate the risk of noncompliance with payroll compliance requirements.

**Risk of material noncompliance is elevated when governments are in financial distress and may not pay withholdings when due.**

*Note:* See the *Ohio Compliance Supplement Implementation Guide* regarding IRS Referrals.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Time summaries / timecards</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

**Note:** It is normally efficient to integrate step 1 below with payroll testing.

1. When testing payroll, determine if the government withholds state, federal and local income taxes.
2. Determine if the government provided any employees with potentially taxable fringe benefits, such as the use of a government-owned vehicle, or an auto or uniform allowance<sup>69</sup>. If so,

<sup>69</sup> The IRS rules regarding whether fringe benefits are taxable can be complex, and subject to frequent revision, such as by interpretive private letter rulings. For example: Uniforms are usually nontaxable if they meet these two tests: (1) the employee must be required to wear the article of clothing while at work (2) the item cannot be adaptable to everyday wear. Many commonly-required work clothes are adaptable (heavy-duty jeans, etc.) and would therefore normally be taxable benefits. ~~In private letter\* ruling 201005014, the IRS determined employer provided clothing is a nontaxable benefit for employees of a political subdivision of a state. However, the IRS cautioned us that the private letter ruling applied only to the narrow circumstances described therein and ought to not be construed to mean government provided clothing is generally nontaxable. Therefore, governments should obtain IRS~~

- determine the benefit amounts were reflected in the affected employees' W-2s. Review a representative number of how they compute the benefit amounts reflected in the affected employees' Forms W-2s? Review 1 or 2 employees' W-2s that include these amounts.
3. Determine if the government paid any independent contractor (other than a corporation) \$600 or more during this year. If so,
    - a. Review a representative number of issued Forms 1099s, and
    - b. Review vendor list and disbursement ledger and determine if Forms 1099 were issued.
  4. If the government assesses an income tax, scan a few Forms 1099G for municipal income tax refunds exceeding \$10 each.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

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publications or advice from a qualified tax practitioner in determining whether benefits are taxable. It is impractical to include this guidance in the Ohio Compliance Supplement.

\* Letter Rulings may not be cited as a precedent by any government other than the one which requested the ruling; however, your legal advisor might find it useful to review.

**Revised: SB 42, 130<sup>th</sup> GA**  
**Effective: 3/23/15**

**Revised: HB 2, 131<sup>st</sup> GA**  
**Effective: 2/1/16\***

**\*While effective 2/1/16, the Auditor of State will not require implementation or audit testing of HB 2 requirements until the 2016/2017 school year. However, community schools must implement HB 2 requirements as specified by their sponsors and the Ohio Department of Education. If a community school implements certain HB2 requirements in the 2015/2016 school year, auditors should audit according to the new requirements.**

**If the compliance attributes listed in 1-24 below were tested during payroll and nonpayroll substantive testing, no additional tests are needed.**

**1-24~~23~~ Compliance Requirement:** Various ORC Sections – Definitions, rates of contributions etc.

- Ohio Rev. Code § 145.01, 145.03, 145.402(This addition is a result of SB 42), 145.47, 145.48, and Ohio Administrative Code Rule 145-1-26 - **Public Employees Retirement System (PERS)**, definitions, exclusions, exemptions and rates of contributions.
- Ohio Rev. Code § 742.01, 742.02, 742.31 to 742.34 - **Police and Fire Disability and Pension Fund**, definitions, rates of contributions and reporting requirements.
- Ohio Rev. Code § 3307.01, 3307.35, 3307.51, 3307.53, 3307.56, 3307.561(This addition is a result of SB 42), ~~and 3307.691 and 3314.10~~ - **State Teachers Retirement System (STRS)**, definitions, employment of retired members, contribution rates. (These sections also apply to community school employees.)
- Ohio Rev. Code § 3309.23, 3309.341, 3309.43(This addition is a result of SB 42), 3309.47, 3309.49 and 3309.51<sup>70</sup> - Membership in **Public School Employees Retirement System (SERS)**, employment of retired members, contribution rate, payment of expense fund. (These sections also apply to community school employees.)

**Summary of Requirement:** These sections require governments to enroll most of their employees<sup>71</sup> in the appropriate retirement system, and to withhold from the employees' wages, or pay on behalf of the employees, a certain percentage of earned wages as defined and to pay over to the appropriate system the amounts withheld, matched with an appropriate percentage of employer matching contributions.

PERS withholdings should be taken out prior to deducting medical, dental, vision, and flexible spending (Ohio Rev. Code § 3309.23 and Ohio Administrative Code Rule 145-1-26).

Certain community school teaching employees are included in STRS and others are excluded. Ohio

<sup>70</sup> The ~~Secretary of SERS board~~ certifies to ODE amounts ODE is to withhold from community school foundation payments for pension costs. (This change is a result of SB 42)

<sup>71</sup> Independent contractors performing the same duties as school employees as defined in Ohio Rev. Code §3307.01, such as contract teachers teaching in a classroom, may also be subject to membership in the STRS retirement system.

Rev. Code §3307.01(B)(2)(b) and 3314.10 include in STRS membership any person who is a teacher to whom all of the following apply:

- The person is employed by a community school operator;
- The operator withholds and pays Social Security taxes on the person's behalf;
- The person had contributing service in a community school in Ohio within one year preceding the later of July 1, 2016, or the date on which the operator for the first time withholds and pays Social Security taxes for that person.

STRS excludes from membership any person not described above for whom a community school operator withholds and pays Social Security taxes, if the person is employed as a teacher or terminates employment with an operator and has no contributing service in a community school in Ohio for at least one year from the date of terminating employment.

Ohio Rev. Code §3309.011, 3309.013 and 3314.10 specify which nonteaching community school employees are included in SERS membership and which are excluded. It excludes both of the following:

- Any person initially employed on or after July 1, 2016, by a community school operator that withholds Social Security taxes beginning with the first paycheck after commencing employment;

AND

- Except as described below, any person who is a former employee of a community school operator and is reemployed on or after July 1, 2016, by the same operator if the operator withholds Social Security taxes beginning with the first paycheck after commencing reemployment.

SERS includes in membership any person reemployed on or after July 1, 2016, by the same operator if the operator withholds Social Security taxes beginning with the first paycheck after commencing reemployment and either of the following apply:

- The person is employed by the same operator at any time within the period July 1, 2015, to June 30, 2016, and the date of reemployment is before July 1, 2017;

OR

- Both of the following conditions are true: (1) the person is employed by the same operator at any time in the 12-month period preceding the date the operator initially withholds and pays Social Security taxes and the person had previously only contributed to SERS and (2) the person's date of reemployment is not more than 12 months after the date the operator initially withholds and pays the taxes.

#### **POSSIBLE NONCOMPLIANCE RISK FACTORS:**

***Note:* Auditors should consider whether governments have historically remitted employee and employer contributions to the appropriate retirement systems timely and demonstrated effective internal controls over payroll. Additionally, adequate training of payroll personnel and supervisory monitoring controls can help mitigate the risk of noncompliance with retirement system compliance requirements.**

**Risk of material noncompliance is elevated when governments are in financial distress and may not pay the contributions when due.**

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Time summaries / timecards</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

1. When testing payroll transactions, determine if the government withheld pension amounts at the proper rate.<sup>72 73</sup> *(Note: PERS withholdings must be taken out prior to medical, dental, vision and flexible spending account deductions. Also, unless they meet the exceptions described above, employees of community school operators (i.e., management companies) must make contributions to STRS or SERS, even if the operator is already contributing to Social Security for these employees.)*
2. Scan payroll ledgers. List a few employees for which no pension is withheld. Ask the CFO

<sup>72</sup> Pursuant to 26 U.S.C. § 3121(b)(7) and Ohio Rev. Code §3307.01(B)(2)(b), 3309.011, 3309.013, and 3314.10, AOS considers employees of community school management companies who perform teaching and administrative services to be members of STRS or SERS unless they meet certain limited exceptions. Therefore, the mandatory employee and employer contributions must be paid into the appropriate State retirement systems unless the employee meets the exceptions described above. We have therefore previously cited management companies that *also* deducted and paid contributions to social security. AOS formally requested the IRS to confirm that it would defer to the Ohio Retirement Systems’ determination and consider the community school employees exempt from social security due to their participation in a qualified retirement plan. However, the IRS declined to confirm this exemption. Therefore, management companies may determine to risk potential IRS penalties and deem an employee to be an employee of the management company rather than the school. Contributions should continue to be remitted to the appropriate Ohio Retirement Systems if management company Boards determine the employees are members of an Ohio Retirement System. Failure to do so will still result in non-compliance citations. **However, auditors should no longer issue noncompliance citations for additional contributions to the social security system.**

<sup>73</sup> Per Ohio Admin. Code §145-1-26 (G)(9) payments made as fees or commissions that are fixed charges or calculated as a percentage of an amount ~~not directly related to work or services performed~~ are not "earnable salary". Ohio PERS (OPERS) has determined that payments for meetings such as those made to Village Council should not be used for a basis of OPERS contributions. Therefore, any person receiving per meeting payments (i.e., board of public affairs, joint fire districts, cemetery districts) should be subject to the same determination.

to provide documentation or explanation as to why there is no withholdings for these employees.

*Note:* Third party contractors who provide pupil services (i.e. therapists and therapy assistants, pathologists, audiologists, social workers, nurses) are required members of STRS per STRS.

3. Examine selected payments of the withholdings from the government to the pension system. (This is an important step. Governments in financial distress occasionally resort to not paying withholdings when due. While unusual, this circumstance, even if not quantitatively material **would usually be qualitative material noncompliance.**)

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

## SCHOOL DISTRICTS

**1-2524 Compliance Requirement:** Ohio Rev. Code §3317.01, 3317.02, 3317.03(E), 3313.981(F), 3313.48, and 3321.04; Ohio Admin. Code §3301-35-06 - School District Average Daily Membership.

Note: The background added to this section has been gleaned through meetings and conversations with the ODE EMIS office. ODE's EMIS Manual has not yet been updated to reflect this information.

### Summary of Requirements:

Schools are funded based on annualized enrollment as opposed to daily attendance. However, there is an important nexus between student attendance and enrollment for Foundation funding purposes. Students are considered as enrolled in a school until the last day of attendance or until permissible student withdrawal can occur. Schools must provide documentation that clearly demonstrates students have participated in learning opportunities. Students with excused absences remain enrolled and will be funded. Students with unexcused absences, however, must be withdrawn upon being legally deemed truant under the school's policies and related Ohio truancy statutes.

Beginning in the 2014-2015 school year, traditional school districts, and joint vocational school districts must comply with minimum hours of instruction instead of a minimum number of school days each year.<sup>74</sup> Average Daily Membership (ADM) is a material variable used to compute school districts' funding, pursuant to Ohio Rev. Code § 3317.022(A). Ohio Rev. Code § 3317.03 defines ADM. Pursuant to Ohio Rev. Code § 3317.03, the school superintendent shall report to the state board of education as of the last day of October, March, and June of each year the enrollment of students receiving services from schools under the superintendent's supervision, and the numbers of other students entitled to attend school in the district under Ohio Rev. Code §3313.64 or § 3313.65.

Schools must comply with minimum hours of instruction instead of a minimum number of school days each year (Ohio Rev. Code § 3313.48).

The minimum "open for instruction" hours are:

- 455 hours for students in half-day kindergarten;
- 910 hours for students in full-day kindergarten through Grade 6; and
- 1,001 hours for students in Grades 7-12

Open for instruction includes time when the district or building is open and all students are participating in:

- Regularly scheduled classes;
- Supervised activities, such as assemblies;
- Approved education options; and
- Co-curricular activities during the scheduled school day.
- As part of the minimum hours, districts and schools may use;
- Up to two equivalent days for the purpose of individualized parent-teacher conferences and reporting periods;

<sup>74</sup> Some school districts were unable to change their Student Information Systems from days to hours during the 2015-2016 school year due to the requirements of the negotiated agreements in effect with their bargaining unit employees. These schools report their student information to ODE in EMIS on the basis of days and ODE converts it to hours for funding purposes. As these negotiated agreements expire, however, the school districts will eventually be required to convert to hours.

- Up to two equivalent days for the purpose of professional meetings of teachers; and
- Morning and afternoon recess periods of no more than fifteen minutes each for students in Grades Kindergarten through 6.

Time spent during lunch periods, breakfast periods and extracurricular activities does not count as open for instruction. A schedule must include five days in each week.

Calamity days are no longer applicable. Instead, schools may schedule “excess” hours above the minimum number. Hours missed above the minimum do not have to be made up. However, if a school closes enough that it will fall below the minimum number of hours, the school must extend its scheduled year.<sup>75</sup>

The ADM~~new~~ counts will be based on the annualized full-time equivalent (FTE) enrollment of each student. A full-time student is one who attends the entire school day and entire school year; that will result with the student having a FTE of 1.00. Students should never have an FTE greater than 1.0. Students who attend a school for less than the entire year will have an FTE equal to the total days/hours attended divided by the number of days/hours in the school year. Schools are funded on a per-pupil FTE basis.<sup>76</sup> School districts will be able to continuously update this information, but must report actual FTE information by the last day of October, March, and June. A student’s FTE will be determined based on the individualized calendar/class schedule each student is assigned to for the school year and their enrollment and withdrawal dates.

In order for ODE to calculate the State Foundation payments to schools on an hourly/per student FTE basis, schools are required to assign each student to a calendar in EMIS. ODE requires schools to create a Master Calendar that details each day a school is in session (or not in session). ODE uses the Master Calendar to validate that a particular day is a full or partial school day that students assigned to this calendar are supposed to be in attendance. Schools may also need to create subcalendars for different schools buildings, grades, or other groups of students that have a deviation from the Master Calendar. For example, Kindergarten students might only have half day attendance where students in Grades 1 through 5 have full day attendance. In this example, schools would need to create a subcalendar for its Kindergarten students in order to document the deviation from the Master Calendar that students in Grades 1 through 5 are assigned.

Furthermore, if a district has five buildings, each building may need its own unique Master Calendar as well as other calendars to cover unique situations. For example, the district may require the high school students to attend the day before Thanksgiving but the elementary and middle school students have the day off because of Parent Teacher Conferences. Having a separate Master Calendar in each building allows for this and other scenarios.

Attending groups may consist of (but are not limited to) the following groups of students:

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<sup>75</sup> One way to make up the hours missed below the minimum required is to use web lessons and blizzard bags (Ohio Rev. Code § 3313.482). Schools will submit plans explaining how they will make up the missed hours, instead of days, up to the equivalent of three scheduled days. Web lessons/blizzard bags may only be used when it is necessary to close the school because of: ...disease epidemic; hazardous weather conditions; law enforcement emergencies; inoperability of school buses or other equipment necessary to the school's operation; damage to a school building; or other temporary circumstances due to utility failure rendering the school building unfit for school use.

<sup>76</sup> See footnote 17 in the Optional Procedures Manual for further information on the ‘formula amount’.

- KG grade level students with staggered start days (KG students starting on a later day than all other regular students)
- Seniors who get out of school earlier than all other students in the building
- Post Secondary students who have attending patterns such as M/W/F and T/TH of the next week, M/W/1/2 day Friday, etc.
- Students who attend another district but your district is responsible for reporting their attendance
- Any other attending pattern where events/exceptions are neither district wide or building wide for a particular subset of students

When counting the number of students enrolled for Foundation Funding purposes, Ohio Rev. Code §3313.981 sets the requirements for the inclusion and exclusion of students who live in one district but who are paying “tuition” (i.e. *formula funding* defined in Ohio Rev. Code §3317.08) and enrolled in another district. A student should be included in the FTE count of the district in which he/she resides and not the district in which he/she pays tuition to attend.

Valid legal reasons for not attending Ohio public schools are set forth in Ohio Rev. Code §3321.04. Any reason not delineated in this code provision shall be deemed unexcused and the pupil should not be reported as enrolled for that day.

Enrollment begins “on the date on which the school has both received the documentation of the student’s enrollment from a parent and the student has commenced learning opportunities offered by the district.” Learning opportunities are defined as both classroom-based and nonclassroom-based learning opportunities overseen by licensed educational employees.

A district must withdraw the student for funding purposes when:

1. the district receives documentation terminating enrollment of the student [Ohio Rev. Code §3317.034(C)].
2. the district is provided documentation of a student’s enrollment in another school [Ohio Rev. Code §3317.034(C)], and
3. the student ceases to participate in learning opportunities provided by the school [Ohio Rev. Code §3317.034(C)]~~, the student fails to participate in learning opportunities and has not received an excused absence for one hundred and five continuous hours. If a student is withdrawn from the district for failure to participate in learning opportunities under division (C)(1)(a)(v) of this section and the district board determines that the student is truant, the district shall take the appropriate action required under sections 3321.19 and 3321.191 of the Revised Code.~~
  - Important Note: HB 367 amended #3 above and removed the 105 hour rule from statute, effective March 23, 2015,

The ADMODE will continue to adjust the FTE used for in the funding formula will continue to adjust as the school updates its information is updated throughout the year. At the close of the school’s fiscal year end, ODE will reconcile the Final FTE Foundation payments and determine whether the school has a corresponding receivable from or payable due to ODE based upon the accumulation of student FTE’s throughout the year. This reconciliation is particularly complex for mobile students and students residing in one district but attending another school. It is critical that schools accurately and timely report their student data to ODE in order for this reconciliation to be performed. At the close of the 2014-2015 school year, for example, ODE had concerns about the reliability of student data many schools reported. As a result, ODE performed numerous reconciliations and adjustments to the Final FTE Foundation payments from August 2015 into calendar year 2016. While we believe this extended adjustment period was due in part to the changes ODE made in the EMIS redesign, we

~~expect that the Final FTE Foundation payment adjustment period will continue to span several months after the schools' fiscal year end. For this reason, schools should continue to evaluate whether these adjustments could result in a receivable, payable, or potential contingency footnote disclosure in their GAAP-basis annual financial statements.~~

~~Schools must comply with minimum hours of instruction instead of a minimum number of school days each year (Ohio Rev. Code §3313.48).~~

~~The minimum "open for instruction" hours are:~~

- ~~• 455 hours for students in half-day kindergarten;~~
- ~~• 910 hours for students in full-day kindergarten through Grade 6; and~~
- ~~• 1,001 hours for students in Grades 7-12~~

~~Open for instruction includes time when the district or building is open and all students are participating in:~~

- ~~• Regularly scheduled classes;~~
- ~~• Supervised activities, such as assemblies;~~
- ~~• Approved education options; and~~
- ~~• Co-curricular activities during the scheduled school day.~~
- ~~• As part of the minimum hours, districts and schools may use:~~
  - ~~• Up to two equivalent days for the purpose of individualized parent teacher conferences and reporting periods;~~
  - ~~• Up to two equivalent days for the purpose of professional meetings of teachers; and~~
  - ~~• Morning and afternoon recess periods of no more than fifteen minutes each for students in Grades Kindergarten through 6.~~

~~Time spent during lunch periods, breakfast periods and extracurricular activities does not count as open for instruction. A schedule must include five days in each week.~~

~~Calamity days are no longer applicable. Instead, schools may schedule "excess" hours above the minimum number. Hours missed above the minimum do not have to be made up. However, if a school closes enough that it will fall below the minimum number of hours, the school must extend its scheduled year.<sup>77</sup>~~

~~New in the 2014-2015 school year, ODE makes the Student Cross Reference (SCR) Report available to all schools to track enrollment of students on a statewide basis. Using SCR, schools have the opportunity to review student data, including student attributes and potential overlaps, submitted by it and other schools in the State. The SCR gives schools the opportunity to reconcile student enrollment questions and issues and reduce or eliminate errors that could suspend or impact a school's Foundation funding payment. Schools must submit changes in a student's status to ODE (via the Data Collector) within 30 days of the change. ODE refreshes school submissions nightly so that all schools have the ability to view student changes on nearly a real-time basis. Schools have the ability to access the SCR system via their SAFE account and the Ohio District Data Exchange (ODDEX) role. The SCR screen shot can be used as supporting documentation for entry of a student~~

<sup>77</sup> ~~One way to make up the hours missed below the minimum required is to use web lessons and blizzard bags (Ohio Rev. Code § 3313.482). Schools will submit plans explaining how they will make up the missed hours, instead of days, up to the equivalent of three scheduled days. Web lessons/blizzard bags may only be used when it is necessary to close the school because of: Disease epidemic; Hazardous weather conditions; Law enforcement emergencies; Inoperability of school buses or other equipment necessary to the school's operation; Damage to a school building; or Other temporary circumstances due to utility failure rendering the school building unfit for school use.~~

withdrawal. ODE will not fund overlapping student enrollment dates across different schools until the conflict is resolved by the schools. Students should not be funded for greater than 1.0 FTE.

As part of their EMIS reporting requirements, School districts must collect the following data on each pupil which will be used, in part, for Foundation Funding and report card calculations and is viewable by other attending schools within the SCR:

- Student name (listed alphabetically)
- Grade level
- Date of enrollment (date pupil enrolled in the counting school)
- Status – this is the status code used in EMIS (i.e., most will be 0 = resident student).
- Resident district IRN number (i.e., Most students will be residents of the home school district). The counting school should use the child’s resident school district IRN number for students outside of the district, such as open enrollment students.
- Attending home IRN number and indicator
- Pupil attendance (the attendance documents should indicate each day a student is not in attendance and the reason for the absence).

This data should be part of an attendance record for each student. To complete the attendance status, the person taking attendance must keep an accurate record of those students who are present and those who are absent. In addition, each day of absence must be determined to be excused or unexcused. Under Ohio Admin. Rule 3301-69-02(B)(2) 3301-51-13, there are ~~eight~~<sup>seven</sup> reasons for absence to be excused:

1. Personal illness
2. Illness in the family
3. Quarantine of the home
4. Death of a relative
5. Medical or dental appointment
- ~~6. Working at home due to absence of parents or guardians (any absence arising because of this shall not extend beyond the period for which the parents or guardians were absent)~~
6. Observance of religious holidays
7. College visitation
8. Emergency or other set of circumstances in which the judgment of the superintendent of schools, constitutes a good and sufficient cause for absence from school.

The school district must determine by contact with the parent or guardian if the reason for absence is one of the ~~seven~~ listed. If the reason for absence is not one of the ~~seven~~, the student must be marked unexcused for that day. Written documentation is required for excused absences and should be dated and collected in a timely fashion.

Ohio Rev. Code § 2151.011(B)(22) provides an additional list of legitimate excuses authorized as *excused* absences.

- Excuses for “excused” absences should be available in the school office and with the class list for each attendance teacher. This includes notes from home, phone logs, suspension notices, and other relevant documents.
  - All excuses from parents, and other documents, regardless of format or condition, become official attendance records. Ohio Rev. Code § 3317.031 requires, “this membership record shall be kept intact for at least five years and shall be made available to the State Board of Education or its representative in making an audit of the average daily membership or the transportation of the district.”

All notes and other verification information relative to excused absences and tardiness should be organized by attendance period in a folder. Suspension or expulsion are examples of other types of verification that should be included in the folder. If a telephone call is the means of confirming excused absences, a copy of the log should be included in the folder. The log should contain the date of the absence, the date of the call, the name of the person making the call, the name and relationship of the person contacted, and the reason for the absence.

~~Each school district is responsible for accurately reporting statistics to the Ohio Department of Education's Educational Management Information System (EMIS), which uses the statistics to compute the school district's ADM. Of the many statistics required to be reported, one of the most important is the determination of school attendance.~~

~~When counting the number of students enrolled for ADM purposes, Ohio Rev. Code §3313.981 sets the requirements for the inclusion and exclusion of students who live in one district but who are paying "tuition" (i.e. formula funding defined in Ohio Rev. Code §3317.08) and enrolled in another district. A student should be included in the ADM count of the district in which he/she resides and not the district in which he/she pays tuition to attend.~~

~~Valid legal reasons for not attending Ohio public schools are set forth in Ohio Rev. Code §3321.04. Any reason not delineated in this code provision shall be deemed unexcused and the pupil should not be reported as enrolled for that day for ADM purposes.~~

~~Average daily membership (ADM) measures the number of students in each district. All students are counted in the ADM of the district in which they reside.~~

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring and reconciliation</li> <li>• Management's identification of changes in laws and regulations</li> <li>• Management's communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

Note: In past years, we have instructed auditors to recalculate FTE for students as part of these testing procedures. However, after an in-depth review of EMIS with ODE during 2015, AOS has determined that it is most efficient and accurate to test student FTE calculations on a statewide basis. For purposes of local school audits, the most effective audit procedures include a review and

*evaluation of school policies as well as verification that schools are maintaining the appropriate student enrollment, attendance, and withdraw documentation. A school's timeliness of student enrollment and withdrawal dates is also a critical component in ensuring accurate FTE reporting to ODE. Finally, school EMIS personnel should be actively reviewing and reconciling student enrollment differences in the Student Cross Reference system to avoid potential overlaps in Foundation funding at multiple schools for the same student.*

Document and evaluate the school's procedures for assigning students to instructional calendars. ~~Select a representative number of students and determine whether they were assigned to a school calendar that is reflective of their daily course schedule as evidenced by the documentation in their student file.~~

~~Determine whether the Master Calendars for each grade and/or school building include at least the requisite minimum number of instructional hours.~~

- ~~If the school district was open for instruction for less than the required minimum number of hours, determine whether the school district received a written waiver from the superintendent of public instruction. *Authorized waivers are rare and should always be evidenced in writing.*~~

Document and evaluate procedures for enrolling and withdrawing pupils, and for processing excused student absences. As part of this evaluation, determine whether the district's policies include sufficient procedures for identifying and tracking all student for whom the district is financially responsible; (a) students residing in and attending district schools, (b) students attending schools in other districts through open enrollment and contractual arrangements, (c) students placed by the courts in facilities outside the district, (d) students attending community schools, and (e) students attending non-public schools through one of the scholarship programs. Also, determine whether the school's student withdrawal policy includes sufficient guidance to EMIS and other administrative personnel for monitoring student absences, identifying truant students, and determining the appropriate timeframe within which personnel should begin truancy proceedings and withdraw a student.

For students with excused absences, select five and, request the representative building attendance officers or EMIS Coordinator to provide access to the students' attendance records, including the students' files, and determine whether the school maintained documentation to support excuses. This may require reviewing attendance data in the school district's electronic student information system (e.g., DASL, PowerSchool, Progress-Books, etc.). *Note: A call log might be sufficient documentation if it contains enough detail to justify an excused absence. For example, if excused for a medical reason, does the log document a conversation with a parent explaining the illness?*

Select a representative number of students that were ~~withdrawn~~ ~~withdrew~~ during the school year. The withdrawal list may be obtained by the school through EMIS or the school's student attendance database.

- Identify when students were withdrawn and determine whether it was timely (e.g., waiting several weeks or more to withdrawal a student is not timely) based on evidence in the student's file.
- Determine whether the appropriate EMIS withdrawal code was used (refer to Chapter 2 of the EMIS Manual) to withdraw the student based on evidence in the student's file. Chapter 2 of the EMIS Manual provides examples of the types of documentation required to be obtained and maintained by the school for each type of withdrawal code.

- ~~Recalculate the FTE based upon the supporting documentation contained in EMIS and the student file for the selected students to ensure it is reasonable based upon the first day of school and the last date the student attended.~~
- Compare the dates determined in the steps above to EMIS or other student attendance database reports. Inquire with management about any significant differences or adjustments. Consider reporting noncompliance or other client communication for any significant unexplained variances.
  - A school should not wait until March to remove a student from its enrollment if the student withdrew in October. Significant delays in reporting student withdrawals constitutes noncompliance. Likewise, a student with excessive truancy should have received multiple communications from the school. Schools should maintain a daily call log or obtain timely excuses from the parent, guardian, or adult-aged student for excessive absenteeism that does not result in removal of a student from enrollment.

Select a representative number of students that enrolled during the school year. The new enrollment list may be obtained by the school through EMIS or the school's student attendance database.

- Identify when students were enrolled and began participating in learning opportunities and determine whether it was timely (e.g., again, waiting several weeks or more is not timely) based on evidence in the student's file. ~~Enrollment should not begin prior to the date a parent or guardian signs and approves a student's enrollment form unless the student is age 18 or older.~~
- ~~Determine whether the student was assigned to the appropriate student schedule calendar based upon the student's coursework as documented in the student file.~~
- ~~Recalculate the FTE based upon the documentation contained in EMIS and the student file for the selected students to ensure it reasonable based upon the student's first day of participation in learning opportunities and the last day of the school year.~~
- Compare the dates determined in the steps above to EMIS or other student attendance database reports. Inquire with management about any significant differences or adjustments. Considering reporting noncompliance or other client communication for any significant unexplained variances.

~~Document and evaluate the school's procedures for reviewing the Student Cross Reference report. Determine whether appropriate school personnel are reviewing and reconciling this information in a timely manner. In most schools, appropriate school personnel include the EMIS staff; however, it may be necessary for school administrators and teachers to review and provide input on students included in the SCR report as well. Consider whether the school is obtaining input from all the key individuals at least on an as needed basis. This might be demonstrated by notes, email discussion, meeting minutes, etc. where these individuals have communicated in an effort to resolve a potential error or flag for a student reported in the SCR.~~

*~~Note: In making these evaluations, auditors should consider that ODE may not always make the Student Cross Reference reports available to schools for certain periods. If ODE did not make the report available, auditors should not penalize the school for a lack of review. But where these reports are available to schools, school EMIS personnel should be monitoring them appropriately and working with other schools to reconcile discrepancies.~~*

*~~Also, since schools are funded on an annual basis, ODE must reconcile and make Final Foundation Funding payments after the fiscal year end close out is performed. These Final Payments occur no sooner than August and may span several months before ODE finalizes the Foundation Funding payments. Therefore, Auditors should consider whether their auditees should include a receivable.~~*

payable, or contingency footnote in accordance with GAAP related to Final Foundation Funding adjustments made by ODE after year end.

Where the number of students paying tuition under Ohio Rev. Code §3317.08 is expected to be significant, inspect documentation that indicates students who are paying tuition to attend are excluded from the school district's ADM (consider using analytical procedures).

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**Revised: HB 2, 131<sup>st</sup> GA**  
**Effective: 2/1/16\***

**\*While effective 2/1/16, the Auditor of State will not require implementation or audit testing of HB 2 requirements until the 2016/2017 school year. However, community schools must implement HB 2 requirements as specified by their sponsors and the Ohio Department of Education. If a community school implements certain HB2 requirements in the 2015/2016 school year, auditors should audit according to the new requirements.<sup>78</sup>**

**August 2016:** This section has been substantially rewritten to provide clarification of the requirements / procedures. Therefore, to prevent confusion, the only changes identified are those double underlined in the Summary of Requirements as a result of HB 2.

## COMMUNITY SCHOOLS

**1-2625 Compliance Requirement:** Ohio Rev. Code § 3313.64, 3314.03, and 3314.08 – Community School Funding.

### Summary of Requirements:

Ohio Rev. Code § 3314.08 provides the formula by which Community Schools are funded. Community Schools receive funding from the state through the per-pupil foundation allocation. Unlike city, local, exempted village and joint vocational school districts, Community Schools have no tax base from which to draw funds for buildings and investment in infrastructure. Ohio Rev. Code §3314.191 states that no payments will be made under Ohio Rev. Code §3314.08 during the first year of operations unless certain conditions are met.

Community schools are funded based on annualized enrollment. However, there is an important nexus between student attendance and enrollment for Foundation funding purposes. Students are considered as enrolled in a community school until the last day of attendance or until permissible student withdrawal can occur. Community schools must provide documentation that clearly demonstrates students have participated in learning opportunities. Participation in learning opportunities is assessed differently for brick and mortar community schools as compared to e-schools. Community schools with blended learning environments (i.e. a mixture of both classroom and non-classroom/internet-based learning) have unique challenges in documenting and assessing student participation.

The community school's Foundation funding will be based on the annualized full-time equivalent (FTE) enrollment of each student. A full-time student is one who attends the entire school day and entire school year; that will result with the student having a FTE of 1.0. Students should never have an FTE greater than 1.0. Students who attend a school for less than the entire year will have an FTE equal to the total days/hours attended divided by the number of days/hours in the school year. Community schools will be able to continuously update estimated student FTE information in EMIS,

<sup>78</sup> While the HB 2 changes to the compliance requirement will not be tested until the 2016/2017 fiscal year, these are areas that auditors should evaluate if a control weakness existed in the 2015/2016 fiscal year where the current contract language is weak even if HB 2 was not yet implemented. AOS auditors should consult with the Center for Audit Excellence if a control deficiency comment is deemed necessary. Schools will be required to comply either in 2016/2017 or upon the expiration of their existing contract at the time of renewal or replacement.

but must report actual FTE information no later than the end of the school year. A student's FTE will be determined based on the individualized calendar/class schedule each student is assigned to for the school year and his or her enrollment and withdrawal dates.

Brick and mortar community schools have a building used to provide free public education, including instructional, resource, food service, and general or administrative support areas, so long as they are part of the facility (34 CFR 222.176). Brick and mortar students with excused absences remain enrolled and will be funded since the school provided the learning opportunity. That is, a teacher provided instruction to the class even though the student was absent on a given day. However, brick and mortar students with unexcused absences will be funded only up until the student reaches 105 consecutive hours of non-attendance, at which point the student must be immediately withdrawn. If a brick and mortar student is attending only on a part-time basis (e.g., a student is splitting his/her instructional time between the community school and a JVS), the community school should adjust the student's "Percent of Time Attended" factor in EMIS to reflect less than 1.0 FTE for the student.

E-Schools are "Internet- or computer-based community schools" in which the enrolled students work primarily from their residences on assignments in non-classroom-based learning opportunities provided via an internet- or other computer-based instructional method that does not rely on regular classroom instruction or via comprehensive instructional methods that include internet-based, other computer-based, and non-computer-based learning opportunities unless a student receives career-technical education under section 3314.086 of the Revised Code (Ohio Revised Code Section 3314.02(A)(7)).

Each internet- or computer-based community school is required to keep accurate records of each student's participation in daily learning opportunities. The records should be easily submitted to the department of education upon request by the department or the Auditor of State. Additionally, no e-school student may participate in more than ten hours of learning opportunities in any 24-hour period. If a student participates beyond this limit, the additional time does not count toward the annual minimum numbers of hours required to be provided to a student (Ohio Rev. Code §3314.27).

For e-schools, non-classroom activities other than correspondence courses or non-classroom online instruction for a student that constitutes less than one-half of the student's instructional day must be documented and approved in writing by a teacher, supervisor or school administrator and must include an hourly/daily/weekly accounting that the hours documented were hours in which the student accessed a learning opportunity. [ODE FTE Review and Community School Enrollment Handbook, Revised January 5, 2015, E-school Review]

In e-schools, students who are absent (i.e., do not log in on a designated school day or have documentation of participating in approved non-classroom based learning) are not funded. That is to say, if an e-school student is not participating 100% of the time (based on the school's calendar in EMIS) but remains enrolled the entire school year (i.e., the student did not reach 105 consecutive hours of unexcused absence), the school should adjust the student's "Percent of Time Attended" factor in EMIS to reflect less than 1.0 FTE for the entire school year. A school has not provided a learning opportunity to an e-school student until the student either accesses the online educational system or completed documented of non-computer-based learning opportunities.

Blended learning is the permissible delivery of educational instruction for site-based community schools. "Blended learning" means the delivery of instruction in a combination of time in a supervised, physical location away from home and online delivery where the student has some element of control over time, place, path, or pace of learning. Community schools that offer blended learning are permissible under the law, subject to approval by their sponsor (Ohio Rev. Code

§3301.079 (K)(1)). Additionally, community schools offering blended learning opportunities are required to make a declaration of such to ODE (Ohio Rev. Code §3302.41 (A))

Pursuant to Ohio Rev. Code §3301.0714, schools must enter data concerning the enrollment and attendance of their students into ODE's Education Management Information System (EMIS). EMIS is used by all schools to enter and review student enrollment and demographic data.

### Reporting Attendance

ODE's FTE Review and Community School Enrollment Handbook, Revised January 5, 2015, was applicable to community schools for the period July 1, 2015 through June 30, 2016. Although ODE has published a January 2016 edition of this manual, it is still in draft form. Auditors should refer to ODE's 2015 Handbook for additional guidance about the compliance requirements described in this OCS Step. Reviewing and understanding the guidance in this Handbook is a critical part of accurately testing student enrollment and attendance. The 2015 Handbook is available at: <https://education.ohio.gov/getattachment/Topics/Finance-and-Funding/School-Payment-Reports/State-Funding-For-Schools/Community-School-Funding/Community-School-Funding-Information/FTE-Review-Handbook-January-2015.pdf.aspx>.

Ohio Rev. Code §3313.64(J) states that the treasurer of each school district shall, by the fifteenth day of January and July, furnish the superintendent of public instruction a report listing the names of each child in the permanent or legal custody of a government agency or person other than the child's parent and each child who resides in a home, who attended the district's schools during the preceding six calendar months. For each child, the report shall state the duration of attendance of that child, the school district responsible for tuition on behalf of the child, and any other information that the superintendent requires. Upon receipt of this report, the superintendent shall deduct each district's tuition obligations and pay to the district of attendance that amount plus any amount required to be paid by the state.

Ohio Rev. Code §3314.08 requires the board of education of each school district to annually report the number of students entitled to attend school in the district that are actually enrolled in community schools. This section also requires the governing authority of each community school to annually report the number of students enrolled in the community school. For each student, the governing board of the community school must report the city, exempted village, or local school district in which the student is entitled to attend.

Based on these reported numbers, the state Department of Education shall calculate and subtract the appropriate amount of state aid from each school district. The amount subtracted shall be paid to the corresponding community school or to the internet or computer-based community school entitled to receive those funds. When calculating and subtracting the appropriate amount of state aid, the department should take into consideration any enrollment of students in community schools for less than the equivalent of a full school year.

Ohio Rev. Code §3314.03, in part, requires the contract entered into between a sponsor and the governing authority of a community school state the following:

- that the governing authority will adopt an attendance policy that includes a procedure for automatically withdrawing a student from the school if the student, without a legitimate

- excuse, fails to participate in one hundred five (105) consecutive hours of the learning opportunities offered to the student;<sup>79</sup>
- that the school will provide learning opportunities to a minimum of twenty-five students for a *minimum* of nine hundred twenty (920) hours per school year.
    - The Ohio Department of Education shall determine each community school student's percentage of full-time equivalency based on the *percentage of learning opportunities* offered by the community school to that student, reported either as number of hours or number of days. However, no internet- or computer-based community school shall be credited for any time a student spends participating in learning opportunities beyond ten hours within any period of twenty-four consecutive hours. Whether it reports hours or days of learning opportunities, each community school shall offer not less than nine hundred twenty hours of learning opportunities during the school year. [Ohio Rev. Code §3314.08(H)(3)]
  - that the governing authority will adopt a policy regarding the admission of students who reside outside the district in which the school is located; and
  - a financial plan detailing an estimated school budget for each year of the period of the contract and specifying the total estimated per pupil expenditure amount of each such year.
  - Site-based schools are also permitted to have blended learning opportunities under the authority of Ohio Rev. Code §3302.41 and §3301.079 (K)(1), subject to approval by their sponsor. As defined in Ohio Rev. Code §3301.079 (K)(1), "blended learning" is the delivery of instruction in a combination of time in a supervised, physical location away from home and online delivery where the student has some element of control over time, place, path, or pace of learning. Community schools offering blended learning opportunities must indicate:
    - what blended learning model(s) will be used,
    - description of how student instructional needs will be determined and documented,
    - the method used to determine competency, granting credit, and promoting students,
    - attendance requirements,
    - description of how student progress will be monitored,
    - description of how private student data will be protected,
    - description of the professional development activities offered to teachers.

The community school delivering blended learning must also make a declaration of blended learning opportunities to ODE by July 1st of each school year pursuant to Ohio Rev. Code §3302.41(A). Additional details can be found in section 2-13 of Chapter 2.
  - Beginning in July 2015, ODE will determine the timing of a newly opening community school's first payment upon the rating of its sponsor under the new Sponsor Evaluation System pursuant to the changes authorized in Ohio Rev. Code 3314.016.
  - an addendum to the contract outlining the facilities to be used and their locations containing at least the following information:
    - A detailed description of each facility used for instructional purposes;
    - The annual costs associated with leasing each facility that are paid by or on behalf of the school;
    - The annual mortgage principal and interest payments that are paid by the school;
  - The name of the lender or landlord, identified as such, and the lender's or landlord's relationship to the operator, if any. that the school's attendance and participation records shall be made available to the department of education, auditor of state, and school's sponsor to the extent permitted under and in accordance with the "Family Educational Rights and Privacy Act of 1974," 88 Stat. 571, 20 U.S.C. 1232g, as amended, and any regulations promulgated under that act, and section 3319.321 of the Revised Code.

<sup>79</sup> Valid legal reasons for non-attendance are set forth in Ohio Admin. Code §3301-69-02.

- a provision requiring that all moneys the school's operator loans to the school, including facilities loans or cash flow assistance, must be accounted for, documented, and bear interest at a fair market rate.
- Requirements Effective 2-1-2016 are listed in 3314.016.

New in the 2014-2015 school year, ODE makes the Student Cross Reference (SCR) Report available to all schools to track enrollment of students on a statewide basis. Using SCR, schools have the opportunity to review student data, including student attributes and potential overlaps, submitted by it and other schools in the State. The SCR gives schools the opportunity to reconcile student enrollment questions and issues and reduce or eliminate errors that could suspend or impact a school's Foundation funding payment. Schools must submit changes in a student's status to ODE (via the Data Collector) within 30 days of the change. ODE refreshes school submissions nightly so that all schools have the ability to view student changes on nearly a real-time basis. Schools have the ability to access the SCR system via their SAFE account and the Ohio District Data Exchange (ODDEX) role. The SCR screen shot can be used as supporting documentation for entry of a student withdrawal. ODE will not fund overlapping student enrollment dates across different schools until the conflict is resolved by the schools. Students should not be funded for greater than 1.0 FTE.

ODE will continue to adjust the FTE used for the funding formula as the school updates its information throughout the year. At the close of the school's fiscal year end, ODE will reconcile the Final FTE Foundation payments and determine whether the school has a corresponding receivable from or payable due to ODE based upon the accumulation of student FTE's throughout the year. This reconciliation is particularly complex for mobile students and students residing in one district but attending another school. It is critical that schools accurately and timely report their student data to ODE in order for this reconciliation to be performed. For this reason, schools should continue to evaluate whether ODE's Final FTE adjustments could result in a material receivable, payable, or potential contingency footnote disclosure in their GAAP-basis annual financial statements.

**POSSIBLE NONCOMPLIANCE RISK FACTORS:**

***Note:* In assessing the risk of noncompliance, auditors should consider the risk of a community school reporting "ghost" students. If this risk factor is believed to be present, auditors should consider performing an unannounced student head count. AOS auditors should consult with the Chief Deputy Auditor prior to conducting such counts, however, to ensure the necessary staff and resources are available for such a count. Auditors should be conscientious to avoid significant disruption to student classroom activities.**

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests**

**Auditors should refer to ODE’s 2015 Handbook for additional guidance about the compliance requirements described in this OCS Step. Reviewing and understanding the guidance in this Handbook is a critical part of accurately testing student enrollment and attendance. The 2015 Handbook is available at:**  
<https://education.ohio.gov/getattachment/Topics/Finance-and-Funding/School-Payment-Reports/State-Funding-For-Schools/Community-School-Funding/Community-School-Funding-Information/FTE-Review-Handbook-January-2015.pdf.aspx>.

*Note: In past years, we have instructed auditors to recalculate FTE for students as part of these testing procedures. However, after an in-depth review of EMIS with ODE during 2015, AOS has determined that it is most efficient and accurate to test student FTE calculations on a statewide basis. For purposes of local school audits, the most effective audit procedures include a review and evaluation of school policies as well as verification that schools are maintaining the appropriate student enrollment, attendance, and withdrawal documentation. A school’s timeliness of student enrollment and withdrawal dates is also a critical component in ensuring accurate FTE reporting to ODE. Finally, school EMIS personnel should be actively reviewing and reconciling student enrollment differences in the Student Cross Reference report and other EMIS tools to avoid potential overlaps in Foundation funding at multiple schools for the same student.*

If significant exceptions are found for the following procedures, AOS audit staff should consult with the Center for Audit Excellence. The consult should be added to Spiceworks with the “Community Schools” specialty. Sufficient details of the exception(s) should be provided, or at least available, to determine whether an opinion modification or a referral to ODE is necessary. AOS will not issue Findings for Recovery for community school funding errors due to the complexity of the funding formula and our inability to determine the amounts due back to the resident school districts. Instead, AOS will make a referral to ODE whenever there are significant exceptions identified in student enrollment and attendance testing.

**Procedures For all Community Schools (both Brick and Mortar and E-Schools):**

Note: For e-schools and brick and mortar schools with blended learning opportunities that have an online component, inquire with management and document how the online educational system tracks student participation. The capabilities of online educational systems vary from e-school to e-school. Some e-schools can track log-ins and log-outs; however, the duration of time online may not equate to the hours a student actually spends learning. For example, some systems are unable to track keystrokes or activity outside of the educational learning system (e.g., working in Microsoft Word or Excel, research on the internet, etc.). When evaluating student attendance and participation in an online or blended learning school, it is important to understand how much reliance the school/auditor can place upon a student's time spent logged into the system as evidence of participation. Where there can be little reliance on log reports, the school may need to supplement online learning documentation with manually kept student activity logs certified by teachers or others with direct knowledge of the student's participation. Online and blended learning schools might also maintain student activity grade books, which document assignments completed, and teacher grades throughout the year to help support participation. Such books should be maintained on a per student, per assignment basis.

Obtain a copy of the school's enrollment and attendance policies and procedures. Document and evaluate the school's procedures for:

- Enrolling and withdrawing pupils timely;
- Documenting attendance and/or participation, for both classroom and non-classroom time, if applicable.
- Documenting student absences; and
- Notifying the resident public school of withdrawn students or students truant for more than 105 or more consecutive hours.

As part of this evaluation, determine whether the Community School's policies include sufficient procedures for identifying and tracking all students for whom the *community school* is responsible. These students include those: (a) residing in and entitled to attend public schools (b) over the age of 18 that are not residing with a guardian (c) placed by the courts in facilities outside the district, (d) attending other community schools, and (e) that have been absent due to truancy for 105 consecutive hours or greater.

Inquire with community school management about the learning opportunities it offered as part of its operating standards during the audit period. Determine whether the community school offered the minimum 920 hours of learning opportunities by reviewing the school calendar in EMIS. Inquire with management to determine if school was closed during the audit period due to weather or electrical outages and ensure the EMIS calendar included sufficient hours to meet the minimum 920 hours of learning opportunities despite these closures (i.e., the closures should be reflected in the final EMIS calendar for the school year). If the community school offered more or less than the required minimum, determine whether the community school reported the accurate number of learning opportunities to the Ohio Department of Education.

Document and evaluate the school's procedures for reviewing the Student Cross Reference report. Determine whether appropriate school personnel are reviewing and reconciling this information in a timely manner.

*Note: In making these evaluations, auditors should consider that ODE may not always make the Student Cross Reference reports available to schools for certain periods. If ODE did not make the report available, auditors should not penalize the school for a lack of review. But where these reports are available to schools, school EMIS personnel should be monitoring them appropriately and working with other schools to reconcile discrepancies.*

*Also, since community schools are funded on an annual basis, ODE must reconcile and make Final Foundation Funding payments after the fiscal year end close out is performed. These Final Payments occur no sooner than August and may span several months before ODE finalizes the Foundation Funding payments. Therefore, Auditors should consider whether their auditees should include a receivable, payable, or contingency footnote in accordance with GAAP related to Final Foundation Funding adjustments made by ODE after year-end.*

### **Procedures For Brick & Mortar, Site-Based Schools (non-electronic schools)**

Determine whether the brick and mortar, site-based school offers blended learning or credit flexibility opportunities. If so, review the school's educational plan approved by the sponsor to determine the nature and format of blended learning and/or credit flexibility opportunities. **Note:** If the school is offering these alternative classroom opportunities without sponsor approval in the Educational Plan of the charter, this constitutes noncompliance. Also, for blended learning, ensure the school provided the required declaration to ODE that it was offering blended learning during the academic year.

For community schools offering blended learning or credit flexibility opportunities, determine the school's policy for capturing, recording, and maintaining attendance and participation records for both classroom and non-classroom learning opportunities. These policies should be documented in the school's educational plan and approved by the sponsor and must be sufficient to support participation in the entire academic school year or portion of the year enrolled (i.e. 920 hours if enrolled the entire year).

If ODE has conducted a recent FTE review that covers a substantial portion (at least 6 months) of the audit period and has issued its report summarizing the results of its review, we can perform the following alternative step in place of selecting students:

- Where an ODE FTE review is available, obtain a copy of the written report and review the procedures performed for sufficiency. *Generally speaking, the procedures outlined in ODE's FTE Review and Community School Enrollment Handbook are sufficient for audit coverage.*
- AOS can rely upon ODE's FTE review, reporting any results necessary as part of our audit in the Schedule of Findings or Management Letter based upon the auditor's assessment of materiality.

If ODE has not performed an FTE review that covers at least six months of our audit period or if ODE has not yet issued a report summarizing the results of its review by the end of the audit fieldwork, perform the following:<sup>80</sup>

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<sup>80</sup> If auditing a school where you believe the risk over student enrollment information is elevated (i.e. a school referring to the sponsor and ODE for investigation in one of the recent AOS Community School Student Attendance reports, etc.) auditors should consider sampling or other expanded testing to gain an acceptable level of assurance over the compliance requirement.

- Select a representative number of newly enrolled community school students during the school year. The new enrollment list may be obtained by the community school through EMIS or the school's student attendance information system.
  - Identify when students were enrolled and began participating in learning opportunities and determine whether it was timely. Waiting several weeks or more from the date a parent or guardian signs the student enrollment form is not timely.
  - Determine whether the school maintained copies of the student's birth certificate, proof of residency, and parent/guardian signed enrollment forms in the student file to support enrollment and resident district determinations.
  
- Select a representative number of community school students that were enrolled for the entire school year from the school's EMIS Enrollment report.
  - Determine if the brick and mortar school uses a mainly computer-assisted classroom instructional program to provide learning opportunities to its students in the school facility. If so, determine whether the log records match the daily hours of instructions listed in the school's daily EMIS calendar for selected students. *Auditors should consider reporting noncompliance or other client communication where these hours do not match. Also, auditors should consult with the Center for Audit Excellence if they find that the brick and mortar school is educating students in an online curriculum outside of the school facility (i.e. similar to an e-school) as this could be potential noncompliance.*
  - Determine whether student engage in correspondence courses. If so, determine whether such courses are described in the school's educational plan and approved by the sponsor. Schools with correspondence courses should develop an educational plan signed by the parent/guardian prior to completion of work. Determine whether students participating in correspondence courses maintained student participation logs documenting the dates and times and the course work completed. These logs should be maintained in the student file and be signed by a teacher to certify completion of the work performed.
  - Determine and document the school's policies and procedures for monitoring truant, students referring them for court action, and withdrawal from enrollment.
  - Review the student files for the selected students and determine whether the school is following its policies for documenting and measuring student enrollment, attendance and participation.
    - Determine whether the school has birth certification and proof of residency documentation for the student contained in the student file.
    - Determine whether the school has completed/signed student enrollment forms contained in the student file.
    - Determine whether the school has maintained a records of student tardies and absences in the student file or elsewhere sufficient to enable the school to monitor its compliance with the 105 consecutive hour rule for truancy.
    - For students with credit flexibility (e.g., includes completing coursework, testing out to show mastery of course content, pursuing an educational option and/or an individually approved option, and any combination thereof), determine whether the school has completed individualized educational plans according to ODE's requirements. *Additional details can be found in section 2-13 of Chapter 2.* Determine whether such documentation is included in the student file and reasonably supports the student's FTE as reported by the school in EMIS.
    - For students participating in blended learning, determine whether the student file contains sufficient supporting documentation for participation in both



facilities and “informally” counting students on site. (This count must be informal. In other words, do not line up the students and ask them to count off – your count should not intrude on school activities. We realize this will not provide an exact count. Instead, you are looking for evidence of obviously material overstatements of FTE. Auditors wishing to perform a student count should obtain prior approval from the Chief Deputy Auditor and contact the Center for Audit Excellence for additional guidance and procedures prior to the count.)

### ***Procedures For E-schools***

**Note:** *For e-schools and brick and mortar schools with blended learning opportunities that have an online component, inquire with management and document how the online educational system tracks student participation. The capabilities of online educational systems vary from e-school to e-school. Some e-schools can track log-ins and log-outs; however, the duration of time online may not equate to the hours a student actually spends learning. For example, some systems are unable to track keystrokes or activity outside of the educational learning system (e.g., working in Microsoft Word or Excel, research on the internet, etc.). When evaluating student attendance and participation in an online or blended learning school, it is important to understand how much reliance the school/auditor can place upon a student’s time spent logged into the system as evidence of participation. Where there can be little reliance on log reports, the school may need to supplement online learning documentation with manually kept student activity logs certified by teachers or others with direct knowledge of the student’s participation. Online and blended learning schools might also maintain student activity grade books, which document assignments completed, and teacher grades throughout the year to help support participation. Such books should be maintained on a per student, per assignment basis.*

If ODE has conducted a recent FTE review that covers a substantial portion (at least 6 months) of the audit period and has issued its report summarizing the results of its review, we can perform the following alternative step in place of selecting students:

- Where an ODE FTE review is available, obtain a copy of the written report and review the procedures performed for sufficiency. *Generally speaking, the procedures outlined in ODE’s FTE Review and Community School Enrollment Handbook are sufficient for audit coverage.*
- AOS can rely upon ODE’s FTE review, reporting any results necessary as part of our audit in the Schedule of Findings or Management Letter based upon the auditor’s assessment of materiality.

If ODE has not performed an FTE review that covers at least six months of our audit period or if ODE has not yet issued a report summarizing the results of its review by the end of audit fieldwork, perform the following:<sup>81</sup>

- Select a representative number of newly enrolled students from the E-school’s EMIS or other student information system and compare the reported enrollment date to the latter of the: (1) first login date, or (2) date the computer was received.

**Note:** *Students are not enrolled in an E-school until the latter of first login date or the date the computer was received. Students may waive the right to a computer; however, this documentation must be kept on file by the community school. The community school should be able to produce a report that documents login dates. Community schools should also maintain*

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<sup>81</sup> If auditing a school where you believe the risk over student enrollment information is elevated (i.e. a school referring to the sponsor and ODE for investigation in one of the recent AOS Community School Student Attendance reports, etc.) auditors should consider sampling or other expanded testing to gain an acceptable level of assurance over the compliance requirement.

*shipping logs (with tracking numbers) from the computer vendor. If the student's parent physically picked up the computer, the community school should have the parent's signature on file to support receipt of the computer or contained in the student's file.*

- Determine whether the school maintained copies of the student's birth certificate, proof of residency, and parent/guardian signed enrollment forms in the student file to support enrollment and resident district determinations.
- Determine and document how the e-school's online educational learning system operates and how much reliance can be placed upon log in and log out times (i.e., duration of time) in the system as evidence of student attendance and participation. *Auditors should assess the risk of noncompliance and tailor their sample sizes and the audit procedures below according to the assessed level of risk.*
- Select a representative number of community school students that were enrolled for the entire school year from the school's EMIS Enrollment report.
  - Determine whether the school maintains log records or student-prepared participation logs that match the daily hours of instructions listed in the school's daily EMIS calendar for selected students. The total log time hours and non-classroom/non-computer learning documentation for each student should match the hours reported in EMIS. If the student has non-computer learning opportunities, the school should maintain documentation in the student file to document approval in writing by a teacher, supervisor or school administrator of such time. *Auditors should report noncompliance or other client communication where log and non-computer hours documented in the student files do not match EMIS and no other supporting documentation exists.*
    - **Note:** *This is admittedly a difficult step; however, the total computer and non-computer-based learning opportunities must be adequately supported and be reasonably comparable to the total hours of instruction claimed by the school to be provided to the student based upon the FTE reported in EMIS.*
  - Determine and document the school's policies and procedures for monitoring truant, students, referring them for court action, and withdrawal from enrollment.
  - Review the student files for the selected students and determine whether the school is following its policies for documenting and measuring student enrollment, attendance and participation.
    - Determine whether the school has proof of residency documentation for the student contained in the student file.
    - Determine whether the school has completed/signed student enrollment forms contained in the student file.
    - Determine whether the school has maintained a records of student absences in the student file or elsewhere sufficient to enable the school to monitor its compliance with the 105 consecutive hour rule for truancy.
    - For students enrolled less than the full school year, compare the dates of enrollment or withdrawal as determined in the steps above from EMIS to the student enrollment and withdrawal forms and other supporting documentation in the school's student files. Inquire with management about any significant differences or adjustments. Consider reporting noncompliance or other client communication for any significant unexplained variances.

- Select a representative number of students from the community school’s withdrawal list. The withdrawal list may be obtained by the community school through EMIS or the community school’s student information system.
  - Identify when students were withdrawn and determine whether it was timely (e.g., waiting several weeks or more from withdrawal notification is not timely). For example, using grade records and/or attendance records, determine the last day students were reported as attending the community school. If a student was reported absent for 105 consecutive hours, determine the date the student should have been withdrawn and ascertain whether the school reported the withdrawal timely.
  - Inquire with management about any significant differences or adjustments. Consider reporting noncompliance or other client communication for any significant unexplained variances.
    - *A community school should not wait until March to remove a student from its enrollment if the student withdrew in October. Significant delays in reporting student withdrawals constitute noncompliance. Likewise, a student with excessive truancy should have received multiple communications from the school to verify the student’s absence during the 105-hour period. Community schools should maintain a daily call log, copies of written correspondence to parents/guardians, or obtain timely excuses from the parent, guardian, or adult-aged student for excessive absenteeism that does not result in removal of a student from enrollment.*

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

## MUNICIPAL

**1-2726 Compliance Requirement:** Ohio Rev. Code Chapter 5727 – Electronic kilowatt-hour tax.

**Summary of Requirement: Kilowatt-hour tax (kWh tax)**

Municipal (Government) electric systems must assess a monthly kilowatt-hour (kWh) tax on end users. This tax is assessed at a variable rate that decreases as kilowatt-hour usage increases on the meters of end users (the last meter used to measure the kWh distributed). [Ohio Rev. Code §5727.81(A)]

Ohio Rev. Code §5727.82(A)(3) permits municipal electric communities to retain in their general fund the taxes collected from customers served inside their city or village limits (including taxes self-assessing customers pay, per §5727.81(C)(2)).

*Note: This legislation did not change the constitutional rule\* that municipal electric systems can sell no more than one-third of electricity outside city or village limits.*

Municipal electric systems must file a monthly report and remit to the Tax Commissioner,<sup>82</sup> by the 20<sup>th</sup> of the next month, taxes collected from any distribution customers served outside their city or village limits. Even if a municipal electric system has no sales outside of its community limits, a monthly report must be filed. [Ohio Rev. Code §5727.82(A)(1) & (A)(3)]

A self-assessing option exists for large users consuming more than 45 million kWh annually. This self-assessing customer must annually register with the Department of Taxation and pay an annual fee to the State. A self-assessing customer located inside a municipal electric community's limits must remit any kWh tax directly to the community. [Ohio Rev. Code §5727.81(C)(2)]

Every electric system liable for the kWh tax must keep complete and accurate records of all electric distributions and other records as required by the Tax Commissioner. The records must be preserved for four years after the return for the taxes for which the records pertain is due or filed, whichever is later, and be available for inspection. [Ohio Rev. Code §5727.92]

*Note:* AOS Bulletin 2001-011 explains these requirements in more detail. Auditors should familiarize themselves with this Bulletin before testing this requirement.

Receipts can be recorded as either “Other Local Taxes” or “Intergovernmental” depending on the situation. For example, excise taxes collected by an electric distribution plant are normally recorded as “Other Local Taxes.” However, a portion of excise tax collected from the electric distribution plants is paid to the state and distributed to the various subdivisions. These receipts should be recorded as “Intergovernmental.”

\* Per Ohio Const. Art. XVIII, Section 6: “Any municipality, owning or operating a public utility for the purpose of supplying the service or product thereof to the municipality or its inhabitants, may also sell and deliver to others any transportation service of such utility and the surplus product of any other utility in an amount not exceeding in either case fifty per cent of the total service or product supplied by such utility within the municipality, provided that such fifty per cent limitation shall not apply to the sale of water or sewage services.” (*Note:* 50% of the total supplied within the municipality = 1/3 of the total supply.)

<sup>82</sup> Governments must pay the tax to the Tax Commissioner, unless required to remit the taxes via electronic funds transfer to the Treasurer of State per Ohio Rev. Code §5727.83.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Tickler Files/Checklists</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

If the kWh tax is not material to the financial statements:

1. Inquire with management if they are aware of and comply with this law.
2. Inquire with management if they have received any correspondence from an oversight agency regarding compliance or noncompliance with this law. If so, obtain and review correspondence to determine if a material penalty exists.

If the kWh tax is material to the financial statements:

1. Determine how kWh taxes billed /collected for customers residing outside of the municipality’s limits vs. those billed / collected inside the municipality’s limits.
2. Inquire with the municipality if there are any self-assessing customers to whom they supply electricity. If yes, determine how the tax is transmitted to the general fund. (If the self-assessor is located outside of the entity limits, the self-assessor remits the kWh tax directly to the State.)
3. Test how the government computes / segregates the tax billed to its residents and transfers the amount to its general fund.
4. Test that the revenue was posted to the correct line item.

**Audit implications (the indirect and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**Revised: HB 64, 131<sup>st</sup> GA**  
**Effective: 9/29/15**

## TOWNSHIPS

**1-2827 Compliance Requirement:** Ohio Rev. Code §517.15 – Permanent cemetery endowment fund.<sup>83</sup>

**Summary of Requirements:** Previously, this fund accounted for gifts and bequests a township invested, with the interest used to maintain the donor-designated burial lots.

Townships may receipt money from various sources into this fund, which becomes part of the nonexpendable fund principle. These financial sources become part of the endowment fund, along with any gifts, devises, or bequests for the maintenance, improvement, or beautification of the cemetery generally, or of a designated burial lot. The sources of money a township can add to the nonexpendable endowment include gifts, charges added to the price regularly charged for burial lots, contributions and individual gifts and agreements with the purchase of a burial lot.

Townships can expend endowment earnings to maintain, improve and beautify specific burial lots and for general-purpose maintenance, improvement and beautification of the cemeteries.

A board of township trustees may create a permanent cemetery endowment fund for the purpose of maintaining, improving, and beautifying township cemeteries and burial lots in township cemeteries. The fund shall consist of money arising from the following sources:

- A. Gifts, devises, or bequests received for the purpose of maintaining, improving, or beautifying township cemeteries;
- B. Charges added to the price regularly charged for burial lots for the purpose of maintaining, improving, or beautifying township cemeteries;
- C. Contributions of money from the township general fund;
- D. An individual agreement with the purchaser of a burial lot providing that a part of the purchase price is to be applied to the purpose of maintaining, improving, or beautifying any burial lot designated and named by the purchaser;
- E. Individual gifts, devises, or bequests made for the maintenance, improvement, and beautification of any burial lot designated and named by the person making the gift, devise, or bequest.

For A through C above, upon unanimous consent of the board of trustees, the board may use the principal of the fund if the board is unable to maintain, improve, and beautify township cemeteries using only the income from the fund.

However, for D & E above, AOS staff should consult with the AOS Legal Division for determination on whether the Board of Trustees has the authority to override individual requests.

<sup>83</sup> Ohio Rev. Code terminology does not affect fund classification for financial reporting. Financial statement preparers should classify this fund according to GASB Cod. 1300. This fund might be a permanent fund under GASB 54 or private-purpose trust fund under GASB 34. However, due to HB 64, if the board of trustees unanimously consent to use the endowment fund principal in accordance with the guidelines above, then the fund classification should be re-evaluated in accordance with GASB. It is important for the Township to demonstrate compliance. In addition to the unanimous consent, the Board of Trustees should retain document and support the inability to maintain, improve and beautify cemeteries using only the income from the fund as well as use of funds.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Time summaries / timecards</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

1. Determine the sources of the moneys received into the fund. Please show support for these sources. (Scanning the support should normally be sufficient.)
2. Determine for what purposes the moneys in this fund were used. Please show support for these expenditures. (Scanning the support should normally be sufficient.)
3. Compare disbursements to investment earnings. Disbursements in excess of unspent accumulated investment earnings violate Ohio Rev. Code §517.15.
4. If the Board of Trustees gave unanimous consent to use the fund principal as described above, evaluate the supporting documentation retained as evidence of their inability to maintain, improve and beautify cemeteries using only the income from the fund.

Note: if this is for an individual request, AOS staff should consult with AOS Legal Division.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**Revised: HB 64, 131<sup>st</sup> GA**  
**Effective: 9/29/15**

**1-2928 Compliance Requirement:** Ohio Rev. Code §507.09 and 505.24(~~DE~~) Allocating township trustee and fiscal officer compensation.

**Summary of Requirement, per Ohio Rev. Code § 507.09 and § 505.24(~~DE~~):**

AOS Bulletin 2013-002 states attendance at board meetings and other activities supporting the general business of the township must be allocated to the general fund; therefore, allocating 100 percent of an official's compensation to funds other than the general fund is not permitted under Ohio law.

- (1) **Trustees receiving per diem compensation (MUST USE TIME AND EFFORT DOCUMENTATION):** When members of the board of township trustees are compensated per diem, a *majority* of the board must pass a resolution establishing the periodic notification method to be used for reporting the number of days spent in the service *and kinds of services rendered* on those days.<sup>84</sup> The per diem compensation shall be paid from the township general fund or from other township funds in proportion to the kinds of services rendered, as documented. (For example, the township could charge trustee time spent on road repairs to the road & bridge fund.) Ohio Rev. Code §505.24(A) limits the number of days a trustee can be compensated to 200.

However, for *salaries not* paid from the general fund, 2004 Op. Atty. Gen. No. 2004-036 established the following documentation requirements:

As noted above, however, a board of trustees is authorized by Ohio Rev. Code §505.24 to pay trustees' salaries from the general fund or other township funds "in such proportions as the board may specify by resolution." The board may therefore determine, as part of its budgeting process, to appropriate money in the EMS Fund for payment of trustees' salaries. In order to meet the provision in Ohio Rev. Code §505.84, that the EMS Fund be used only for ambulance and emergency medical services, however, the board would be required to establish administrative procedures for assuring that the proportionate amount paid from the EMS Fund for trustees' salaries properly reflected the proportion of time each trustee spent on EMS matters relative to other township matters. This would necessitate trustees documenting all time spent on township business and the type of service performed, in a manner similar to trustees paid a per diem. To the extent that the board is able to determine the portion of time spent on EMS matters, relative to the total time spent on township business, it may pay the proportionate cost of the trustee's salary from the EMS Fund. If a trustee's time is not documented, however, then no part of his salary may be paid from the EMS Fund.

In other words, 2004 Op. Atty. Gen. No. 2004-036 requires trustees compensated on a per diem basis to establish administrative procedures to document the

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<sup>84</sup> The Ohio Rev. Code does not define a "day" for purposes of this requirement. Townships should consult with their legal counsel and adopt a policy in compliance with 2004 Op. Atty. Gen. No. 2004-036. If a Township has a duly enacted policy defining what constitutes a "day" in compliance with 2004 Op. Atty. Gen. No. 2004-036, we will audit in accordance with that policy. If the Township has not adopted a policy, we will audit based on our determination of a "day" as an 8 hour workday indicated above.

proportionate amount chargeable to other township funds based on the kinds of services rendered. The “administrative procedures” can be timesheets or a similar method of record keeping, as long as the trustees document all time spent on township business and the type of service performed. If per diem trustees do not document their time, then no part of salaries may be paid from the restricted funds.

The important factor is the portion of time spent on other township funds, relative to the total time spent on township business (as opposed to the total days in a given month). In other words, do not factor days in which no township work is done into the allocation.

Per the above, per-diem trustees must record the time spent on various tasks and the specific fund to which the township will charge their costs when paying any proportion of a trustee’s salary from a restricted fund. Although the fire and rescue services, ambulance services, and emergency medical services fund under Ohio Rev. Code §505.84 was the focus of 2004 Op. Atty. Gen. No. 2004-036, the ruling also applies to funds for the motor vehicle license tax pursuant to Ohio Rev. Code §4504.18 and 4504.19; motor vehicle tax pursuant to Ohio Rev. Code §4503.02; gasoline tax pursuant to Ohio Rev. Code §5735.27(A)(5)(d); the cemetery fund pursuant to Ohio Rev. Code §517.03, and any other restricted fund. (The sole exception to this is for trustees charging all salaries to the general fund, as described above.) The township must maintain daily records of tasks performed for each individual trustee that, when reviewed cumulatively for the fiscal year, will provide reasonable justification for the apportionment of salary between funds as specified in the resolution. **Monthly summaries in lieu of daily records are not acceptable.**

- (2) **Trustees receiving compensation by annual salary (MUST USE CERTIFICATIONS IF PAID FROM FUNDS OTHER THAN THE GENERAL FUND):** To be paid on a salary basis in equal monthly installments, the board of trustees must *unanimously* pass a resolution to allow it. To be paid from any fund(s) other than the general fund, the resolution must also specify the proportions of the salary that are to be paid from each fund (Ohio Rev. Code §505.24(DC)). If trustees use the salary method and are compensated from funds other than the general fund, they must certify the percentage of the time spent working on matters that are to be paid from funds other than the general fund. Trustees must complete a certification prior to receiving his/her pay for that pay period. The certification must be done individually, but is not required to be notarized. The certification is not required to be a time log. Rather, all that is required is a statement detailing the percentage of time that the trustee/fiscal officer spent during that pay period providing services related to each fund to be charged. A sample certification is attached to AOS bulletin 2011-007. If 100% of the compensation of the township trustee is to be paid to from the general fund, no certification is required.
- (3) **Fiscal officer compensation:** Fiscal officers compensated from funds other than the general fund must certify the percentage of the time spent working on matters that are to be paid from funds other than the general fund. They must complete a certification prior to receiving his/her pay for that pay period. The certification must be done individually, but is not required to be notarized. The certification is not required to be a time log. Rather, all that is required is a statement detailing the percentage of time that the trustee/fiscal officer spent during that pay period providing services related to each fund to be charged. A sample certification is attached to AOS bulletin 2011-007. If

100% of the compensation of the township fiscal officer is to be paid from the general fund, no certification is required.

For salaried trustees only, AOS will forgo issuance of a finding for adjustment in any case where the Township has reasonable supporting documentation (such as detailed time and effort records, timesheets, etc.) in lieu of the certifications. ~~Auditors should ask the Township trustee(s) to sign a retroactive certification for each pay period and attach the supporting time and effort records to the certification.~~ Absent this documentation, auditors should issue a finding for adjustment. Also, auditors should still issue a noncompliance citation for not preparing the certifications as required by statute in all cases.

Undocumented per diem salaries for trustees, where the trustees officers have been paid from funds other than the General Fund, should result in findings for adjustment and the consideration of opinion qualifications including adverse opinions (if the auditee refuses to post the adjustment).

Townships allocating 100 percent of officials’ salaries to restricted funds will be subject to audit findings. Townships must properly allocate the officials’ salaries for the entire period. Failure to make necessary allocation revisions could result in findings for adjustment that may serve to disqualify the township from lower-cost agreed upon procedure audits, result in qualified opinions, or otherwise increase audit costs.

**Note:** If the township allocated salaries incorrectly, it is likely they allocated reimbursable health care benefits incorrectly. Improper allocations of health care benefit reimbursements should be included in the findings for adjustment (if the auditee refuses to post the adjustment).

**POSSIBLE NONCOMPLIANCE RISK FACTORS:**

**Note:** In assessing the risk of noncompliance, auditors should consider recent changes to the statutory requirements described in this OCS step. This statute contains intricate requirements and interpretations.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Time summaries / timecards</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

1. Document how the township records the time spent on each township service.
2. Recompute selected allocations of trustee/fiscal officer salaries or per diem amounts to each fund.

For UAN entities: Use the wage base earning report – detail and summary. For periods before 2015, use the wage detail report.

3. For fiscal officers or trustees paid by annual salary with allocations to funds other than the general fund, trace selected allocations to certifications.
4. For trustees paid per diem, with allocations to funds other than the general fund, trace time or services performed to time or activity sheet.
5. Agree selected postings of the salaries from step 2 to the township’s check register.

<p><b>Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):</b></p>
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**SOLID WASTE MANAGEMENT**

**1-3029 Compliance Requirements:** Ohio Rev. Code §343.01, 3734.52, 3734.55, 3734.56, 3734.57(B), 3734.573, 3734.57(G), and 3734.577 – Expenditures by solid waste management districts.

**Summary of Requirement:** Ohio Rev. Code §343.01 and 3734.52 require all counties in Ohio to be a part of a solid waste management district, either individually or jointly as part of a multi-county (joint) solid waste management district. Ohio Rev. Code §3734.55 and 3734.56 require all solid waste management districts to develop and submit solid waste management plans to Ohio EPA for approval. These plans address a variety of issues associated with solid waste management within the jurisdiction, including demonstrating that adequate landfill capacity exists for waste generated within the district and establishment of recycling goals. Once approved by the Ohio EPA, solid waste management districts are required to implement their plans.

Solid waste management districts are authorized to levy certain fees to fund the programs specified in their plans. Ohio Rev. Code §3734.57(B) specifies that solid waste management districts can levy fees on the disposal of solid waste in landfills within their boundaries, and Ohio Rev. Code §3734.573 specifies that solid waste management districts can levy fees on waste that is generated within their boundaries regardless of where the waste is disposed.<sup>85</sup> Both of these sections require the fee revenue shall be “kept in a separate and distinct fund to the credit of the district.” Ohio Rev. Code §3734.57(G) specifies that “moneys . . . arising from the [disposal of generation fees] shall be expended by the board of county commissioners or directors of the district in accordance with the district’s solid waste management plan or amended plan . . . exclusively for the following purposes: . . .” Ohio Rev. Code §3734.57(G) then provides ten “allowable uses” for the fee revenue.<sup>86</sup>

<b>In determining how the government ensures compliance, consider the following:</b>	<b>What control procedures address the compliance requirement?</b>	<b>W/P Ref.</b>
<ul style="list-style-type: none"> <li>• Policies and Procedures Manuals,</li> <li>• Knowledge and Training of personnel</li> <li>• Time summaries / timecards</li> <li>• Legislative and Management Monitoring</li> <li>• Management’s identification of changes in laws and regulations</li> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

<sup>85</sup> If a district charges a fee to private sector commercially- licensed haulers, the district cannot waive this fee for public sector commercially- licensed haulers. (Ohio Rev. Code §3734.577)

<sup>86</sup> 2008 Op. Atty. Gen. No. 2008-021 clarifies that the fee can be “used by the district for the purposes set forth in Ohio Rev. Code §3734.57(G)(1)-(10)] or to provide other remuneration or services to or on behalf of the district or its residents.” Since the fee can be used to subsidize the normal operations of the district, AOS believes districts should account for this fee within a separate sub-fund or account of the district’s general fund.

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

1. Test that disbursements were:
  - Allowable under one of the ten “allowable use” criteria for the fee revenue listed in Ohio Rev. Code §3734.57(G); and
  - Allowable in accordance with the policies and procedures.
2. If significant unusual items are noted, auditors should make a referral to Ohio EPA, Division of Solid and Infectious Waste Management by sending an email to [Referrals@ohioauditor.gov](mailto:Referrals@ohioauditor.gov).
3. If the solid waste management district administers a fee under Ohio Rev. Code §3734.573, is this maintained in a separate fund.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

## **Appendix A: Agricultural Society Compliance Supplement**

You should use this appendix for all audits of Agricultural Societies in addition to the general laws and regulations noted as applicable to Agricultural Societies in the Legal Matrix within Implementation Guide Exhibit 5.

Agricultural societies incorporate as either county (per Ohio Rev. Code §1711.01) or independent (per Ohio Rev. Code §1711.02). Certain laws herein apply to one or both types. Each step describes to which type of society it applies.

### ***Agricultural Society Compliance Supplement***

**Applicability: County and independent societies**

#### **OCS Chapter 1 Section A**

**Budgetary Compliance Requirement:** An Agricultural Society is not required to follow the budgetary statutes within Ohio Rev. Code Chapter 5705. However, the *Uniform System of Accounting for Agricultural Societies Society Accounting System User Manual* states:

Each agricultural society shall prepare an annual budget of its revenues and expenses. The budget shall cover the period December 1st through November 30th.

The budget shall be considered and approved by the board of directors prior to the first day of the ensuing fiscal year. The budget shall be prepared at the level of the accounts from the chart of accounts which are used by the society.

Budgeted revenues and expenses should be distributed to the month they are likely to be received and expended. The distributed monthly budget should be integrated into the society's accounting system.

Actual revenues and expenses shall be compared to budgeted amounts each month, and reported to and reviewed by the board of directors. The board of directors shall determine the reasons why actual expenses exceed or are less than budgeted expenditures by making inquiries to fair management about the reasons.

We believe Agricultural Society Boards should not present budgetary statements as part of their basic statements, because they lack the legal authority to adopt "legally binding" budget as described in GASB Codification 2400.102. Therefore, if a Society adopts a budget and wishes to present it, the statements should present it as supplemental information (not RSI). However, while not legally binding under the GASB criteria, over expending the budget could be noncompliance with a Society' budget resolution. Determining whether noncompliance exists requires judgment based on whether the Society intends their budget to limit expenditures vs. being only a planning tool, etc.

*[Insert applicable budgetary requirements.]*

**Note:** An appropriation is authorization to expend money.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>➤ Policies and Procedures Manuals</li> <li>➤ Knowledge and Training of personnel</li> <li>➤ Periodic Reviews/Comparisons of Budgeted and Actual Amounts</li> <li>➤ Presence of Effective Accounting System</li> <li>➤ Legislative and Management Monitoring</li> <li>➤ Management’s identification of changes in laws and regulations</li> <li>➤ Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures – Compliance (Substantive) Tests:**

1. Read resolutions and determine whether the society enacted a budget. (If no budget was adopted include a management letter comment that one be adopted per the *Uniform System of Accounting for Agricultural Societies Society Accounting System User Manual*).
2. Inquire (or determine from reading the minutes) if amended or supplemental measures have been passed.
3. Inspect the society’s records throughout the period to determine if updates and adjustments were properly and timely posted.
4. Determine if the accounting system “integrates” budgetary data. This means the accounting system should report appropriations, encumbrances, unencumbered cash balances, and estimated receipts, and should compare budgetary data to actual results. If the client uses a manual system (i.e. spreadsheets) determine if the manual system used by the client adequately tracks and compares budgetary data.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**Applicability: County societies**

**OCS Chapter 1 Section C**

**3a. Debt Compliance Requirement:** Ohio Rev. Code §1711.18 – Issuance of county bonds to pay debts of county society; 1711.19 – Bonds; 1711.20 – Levy for payment of bonds; and 1711.21 – Use of money raised by county taxation.

**Summary of Requirement:** In a county in which there is a county agricultural society indebted fifteen thousand dollars or more and such society has purchased a fairground or title, the board of county commissioners shall submit to the electors of the county whether or not county bonds shall be issued and sold to liquidate such indebtedness. If a majority of the voters vote in favor thereof, the board of county commissioners shall issue and sell bonds of the county in the amount necessary. Such bonds shall bear interest at not more than the rate Ohio Rev. Code §9.95 provides,<sup>87</sup> payable semiannually, and shall be issued for a period of not less than ten nor more than twenty years.

From the proceeds arising from the sale of such bonds, the board shall pay off the indebtedness for which such bonds were sold. The board of county commissioners shall levy a tax upon all the taxable property on the tax duplicate of the county for the purpose of paying such bonds as they mature and the interest thereon.

When money has been raised by taxation by a county for the purpose of leasing lands for county fairs, erecting buildings for county fair purposes, or making improvements on a county fairground, or for any purpose connected with the use of a county fairground or with the management thereof by a county agricultural society, such money shall be used for such purpose only.

**Note:** Bonds a county issues under this section are **county** liabilities, though the society may agree to repay the county for debt service due on the bonds. (If the society contractually agrees to pay the county for the debt service, the society’s notes should disclose a debt obligation to the county. However, do **not** characterize the obligation as *bonds payable*.)

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>➤ Policies and Procedures Manuals</li> <li>➤ Knowledge and Training of personnel</li> <li>➤ Bond Counsel/Lender Involvement</li> <li>➤ Legislative and Management Monitoring</li> <li>➤ Management’s identification of changes in laws and regulations</li> <li>➤ Management’s communication of changes in laws and regulations to employees</li> </ul>		

<sup>87</sup> Ohio Rev. Code §9.95 states, “Interest shall not exceed the maximum or maximum average annual interest rate per annum determined in or pursuant to the proceedings for the securities by the county commissioners.”

**Suggested Audit Procedures – Compliance (Substantive) Tests:**

- Inspect cash receipt records and minutes and determine if indebtedness exists.
- For bonds a county issues during the audit period, compare disbursements of the proceeds to the bond documents to determine if the proceeds were spent for purposes for which the bonds were issued.
- For bonds issued during the audit period, read bond contracts and summarize provisions applicable to the Society, and save in the permanent file. The summary should describe:
  - Purposes for which the debt was issued.
  - Collateral
  - An amortization schedule for any debt service the society owes to the county.
- For years in which the society owes debt service to the county, agree payments to the amortization schedule.
- Determine if a debt footnote describes the purpose, original issue amount, collateral, and an amortization schedule for this debt.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies/material weaknesses, and management letter comments):**

**Applicability: County society**

**OCS Chapter 1 Section C**

**3b. Debt Compliance Requirement:** Ohio Rev. Code §1711.25 to 1711.30 – Sale, lease, purchase, and exchange of sites by county society; payment for new site by county funds or bonds; tax levy; and approval by electors.

**Summary of Requirement:** A county agricultural society may secure a different site for its annual fair. If this occurs, auditors should review the Ohio Revised Code sections listed above and develop appropriate audit procedures.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>➤ Policies and Procedures Manuals</li> <li>➤ Knowledge and Training of personnel</li> <li>➤ Bond Counsel/Lender Involvement</li> <li>➤ Legislative and Management Monitoring</li> <li>➤ Management’s identification of changes in laws and regulations</li> <li>➤ Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures – Compliance (Substantive) Tests:**

- By reading the minutes, determine if the Society procured a different site for its fair, or acquired or disposed of land where the annual fair is held. If so, review the code sections above for specific requirements.
- In the year these transactions occur, read contracts and summarize requirements imposing debt or lease payments, collateral, insurance or other obligations on the society. Save the summary in the permanent file.
- Determine if the footnotes adequately describe any leases or other society obligations, amortization schedules, etc.
- For subsequent years, agree any debt or lease payments owed to the contract summary in the permanent file.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies /material weaknesses, and management letter comments):**

**Applicability: County societies**

**OCS Chapter 1 Section C**

**3c. Debt Compliance Requirement:** Ohio Rev. Code §1711.13 – County agricultural society may obtain mortgage debt or may enter into written agreements to obtain loans and credit for expenses.

**Summary of Requirement:** County agricultural societies may do either or both of the following:

(A) Mortgage their grounds for the purpose of renewing or extending pre-existing debts, and for the purpose of furnishing money to purchase additional land, but if the board of county commissioners has caused money to be paid out of the county treasury to aid in the purchase of the grounds, no mortgage shall be given without the consent of the board. Deeds, conveyances, and agreements in writing, made to and by such societies, for the purchase of real estate as sites for their fairs, shall vest a title in fee simple to the real estate described in those documents, without words of inheritance. This means the Agricultural Society owns the land outright without any third party claims.

(B) Enter into agreements to obtain loans and credit for expenses related to the purposes of the county agricultural society, provided that the agreements are in writing and are first approved by the board of directors of the society. The total net indebtedness incurred by a county agricultural society pursuant to this division (B) shall not exceed an amount equal to twenty-five percent of its annual revenues.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>➤ Policies and Procedures Manuals</li> <li>➤ Knowledge and Training of personnel</li> <li>➤ Bond Counsel/Lender Involvement</li> <li>➤ Legislative and Management Monitoring</li> <li>➤ Management’s identification of changes in laws and regulations</li> <li>➤ Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures – Compliance (Substantive) Tests:**

- By reading the permanent file, minutes, cash receipt records, other documents, and by inquiry, determine if any such indebtedness exists.
- If there is mortgage debt, use the sources described in **a.** above to determine if the board of county commissioners paid county funds to aid in purchasing the grounds. Read a copy of the county commissioners’ resolution to determine if they gave the proper consent for this mortgage debt. Retain a copy of the resolution in the permanent file.

- Loans and Credit<sup>88</sup>
- If the Society has procured loans and credit for expenses related to the purposes of the county agricultural society, verify these agreements are in writing and were first approved by the board of directors of the society.
- Examine the society's computation supporting that the total net indebtedness from loans and credit does not exceed twenty-five percent of its annual revenues.
- For debt issued during the audit period, compare disbursements of the proceeds to the bond documents to determine if the proceeds were spent for purposes for which the bonds were issued.
- For debt issued during the audit period, read related contracts and summarize provisions applicable to the society, and save in the permanent file. The summary should describe:
  - Purposes for which the debt was issued.
  - Collateral / mortgage
  - An amortization schedule for any debt service the society owes to the county.
- For years in which the society owes debt service, agree payments to the amortization schedule.
- Determine if a debt footnote describes the purpose, original issue amount, collateral, and an amortization schedule for this debt.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies /material weaknesses, and management letter comments):**

<sup>88</sup> The law authorizing this type of debt did not exist prior to the addition of (B) to Ohio Rev. Code §1711.13, effective September 26, 2003. Therefore, if any of this type of debt was acquired prior to September 26, 2003, the Agricultural Society shall discharge such debt.

**Applicability: County and independent societies**

**OCS Chapter 1 Section D**

**Accounting Compliance Requirement:** Ohio Admin. Code § 117-10-01 – Financial reporting and accounting for county agricultural societies.

**Summary of Requirement:** Each county agricultural society and independent agricultural society shall, for financial reporting and accounting purposes, record and report all financial transactions on a fiscal year basis beginning on December 1 and ending November 30. Societies shall record and report all financial transactions in accordance with the *Uniform System of Accounting for Agricultural Societies*<sup>89</sup>.

**Note:** You can view the latest version of this at [www.ohioauditor.gov](http://www.ohioauditor.gov), under *Resources/Publications & Manuals*.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>➤ Policies and Procedures Manuals</li> <li>➤ Knowledge and Training of personnel</li> <li>➤ Presence of Effective Accounting System</li> <li>➤ Legislative and Management Monitoring</li> <li>➤ Management’s identification of changes in laws and regulations</li> <li>➤ Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures – Compliance (Substantive) Tests:**

- Compare the *Uniform System of Accounting for Agricultural Societies* requirements with the systems and records the society is using.
- Determine if:
  - The required chart of accounts is used.
  - A cash journal, a receipts ledger, an expense ledger, and an investment ledger are used.

<sup>89</sup> The Auditor of State also requires by rules, that certain public offices follow a prescribed uniform chart of accounts and/or establish a fund accounting system to demonstrate legal compliance, financial accountability and to provide management with information for decision making. These rules are in Chapter 117-2 of the Ohio Admin. Code. As a matter of accountability and internal control, each public office should account for financial activities using an accounting system which demonstrates legal compliance; follows a documented chart of accounts appropriate for its particular activities; and is supported by appropriate subsidiary ledgers/journals. When a public office fails to maintain such an accounting system, auditors should consider whether the failure constitutes a reportable internal control deficiency or weakness.

- The prescribed formats for accounting and reporting information are used (including receipts, purchase orders, vouchers, checks, and bank reconciliations).

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies /material weaknesses, and management letter comments):**

**Note:** Auditors should test the applicable deposit and investment requirements documented in Chapter 2 Section E of the OCS. Refer to Implementation Guide Exhibit 5 for guidance on specific applicability.

**Note:** Auditors should test the applicable health care self insurance and liability insurance requirements documented in Chapter 1 Section F of the OCS. Refer to Implementation Guide Exhibit 5 for guidance on specific applicability.

**Applicability: County and independent societies****OCS Chapter 1 Section F**

**Other Potentially Direct and Material Laws and Regulations:** Ohio Rev. Code §3769.082 – Ohio Fairs Fund; distribution.

**Summary of Requirement:** Ohio Fairs Fund moneys shall be distributed by the director of agriculture annually, on or before the first day of March, as follows:

- To each county agricultural society and to each independent agricultural society conducting an annual fair, a prescribed percentage of Ohio Fairs Fund money, to be allocated for general operations.
- To each county agricultural society and each independent agricultural society conducting horse races (harness races or running races) during their annual fair, the sum of four thousand dollars, to be used as purse money for horse races in accordance with this section, and the additional sum of one thousand dollars to each such county agricultural society and independent agricultural society to be used for race track maintenance and other expenses necessary for the conduct of such horse races or colt stakes.
- A grant of four thousand dollars shall be available to each county or independent agricultural society for the conduct of four stake races for two-year-old and three-year-old colts and for four stake races for two-year-old and three-year-old fillies at each gait of trotting and pacing, provided, that at least five hundred dollars shall be added to each race. Exclusive of entrance fees and the excess moneys provided below, the grant of four thousand dollars for purse money provided, a sum not to exceed three thousand dollars may be used by a society to reach the required purse for each of the eight stake races. Such stake races shall be distributed as evenly as possible throughout the racing season.
- In the event that the moneys available on the first day of March of any year are less than that required above, the amount distributed from the Ohio Fairs Fund may be different than the amounts reflected above.
- County agricultural societies and independent agricultural societies conducting stake races shall, on or before the first day of November in the year immediately preceding the year in which the moneys are to be distributed, make application for participation in such to the director of agriculture on forms provided by the director.
- Distribution of moneys for stake races shall not be paid to county agricultural societies and independent agricultural societies that conduct on their race courses automobile or motorcycle races during any year for which such distribution is requested, unless such automobile or motorcycle races are not conducted during the days and nights that horse racing is being conducted at such fair.
- Any county agricultural society or independent agricultural society which uses the moneys distributed under this section for any purse other than that provided in this section is not eligible to receive distribution from the Ohio Fairs Fund for a period of two years after such misuse of such moneys occurs.

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>➤ Policies and Procedures Manuals</li> <li>➤ Knowledge and Training of personnel</li> <li>➤ Periodic Reviews/Comparisons of Budgeted and Actual Amounts</li> <li>➤ Presence of Effective Accounting System</li> <li>➤ Legislative and Management Monitoring</li> <li>➤ Management’s identification of changes in laws and regulations</li> <li>➤ Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures – Compliance (Substantive) Tests:**

- Determine whether the society receipted Ohio Fairs Fund in the State and Local Fund, and how much was restricted for racing purses and track maintenance according to the above sections.
- Compare amounts distributed for race purses and track maintenance to the amounts restricted to these purposes, and compute whether the amounts disbursed at least equaled the restricted amounts.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies /material weaknesses, and management letter comments):**

**Applicability: County and independent societies**

**OCS Chapter 1 Section F**

**Compliance Requirement:** Ohio Rev. Code §117.38, 901.06, and 1711.05 – Filing financial reports and Publication of treasurer’s account.

**Summary of Requirement:** Prior to the first day of December of each year, the director of agriculture shall set a date in January of the following year, on which the director shall meet with the presidents or other authorized delegates of agricultural societies which conduct fairs in compliance with sections 1711.01 to 1711.35, inclusive, of the Revised Code, and regulations of the department of agriculture. Each society shall deliver its annual report to the director at or before the January meeting. [Ohio Rev. Code § 901.06]

Cash-basis entities must file annual reports with the Auditor of State. Since the Auditor of State has not prescribed a form for the report, the society shall file an annual report using the format as suggested in the handbook titled, “Uniform System of Accounting for Agricultural Societies.” Any public office which does not file the report by the required date shall pay a penalty of twenty-five dollars for each day the report remains unfilled, not to exceed seven hundred fifty dollars. [Ohio Rev. Code §117.38]

In determining how the government ensures compliance, consider the following:	What control procedures address the compliance requirement?	W/P Ref.
<ul style="list-style-type: none"> <li>➤ Policies and Procedures Manuals</li> <li>➤ Knowledge and Training of personnel</li> <li>➤ Periodic Reviews/Comparisons of Budgeted and Actual Amounts</li> <li>➤ Presence of Effective Accounting System</li> <li>➤ Legislative and Management Monitoring</li> <li>➤ Management’s identification of changes in laws and regulations</li> <li>➤ Management’s communication of changes in laws and regulations to employees</li> </ul>		

**Suggested Audit Procedures - Compliance (Substantive) Tests:**

- 1) Trace selected totals from the annual report to the underlying accounting system. If we use the annual report as a trial balance, we will satisfy this requirement by completing the mandatory Trial Balance steps from the financial audit program. If the report is significantly deficient, we should cite Ohio Rev. Code §117.38 for filing an incomplete or misleading report.
- 2) Search ~~LGS’s annual report file~~AFDARS, the Annual Financial Data Reporting System, to determine whether the government filed an annual report with our office.

- 3) Inquire to determine the date the report was filed with the Director of Agriculture.

**Audit implications (adequacy of the system and controls, and the direct and material effects of non-compliance, effects on the audit opinions and/or footnote disclosures, significant deficiencies /material weaknesses, and management letter comments):**

**Note:** Auditors should test depository requirements as applicable in Chapter 2 Section E of the OCS. Refer to Implementation Guide Exhibit 5 for guidance on specific applicability.

**Note:** Auditors should test public meetings requirements as applicable in Chapter 3 of the OCS. Refer to the Implementation Guide Exhibit 5 for guidance on specific applicability.

**Note:** Auditors should test public records requirements as applicable in Chapter 23 of the OCS. Refer to the Implementation Guide Exhibit 5 for guidance on specific applicability.

**Note:** Auditors should test income tax requirements as applicable in Chapter 1 Section F of the OCS. Refer to Implementation Guide Exhibit 5 for guidance on specific applicability.