

## 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* (AAG SLG), 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
  - Require reporting as a material GAGAS noncompliance finding.
  - May represent significant / material violations of “finance-related legal and contractual provisions”

<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 financial statement amounts and support notes to the statements.

- GASB Cod. 2300.106(h) require “notes to the financial statements should disclose significant violations of finance-related legal and contractual provisions” and “actions taken to address significant violations”.
  - See the OCS Implementation Guide page 7 for the Finance Related Legal or 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.

**NOTE: Red text throughout this Ohio Compliance Supplement is related to COVID-19**

The legal matrix matches the applicability of OCS steps to various entity types. The information in the matrix does not necessarily encompass every item requiring testing for these entities. Additionally, when footnotes in the matrix reference specific sections of the Ohio Rev. Code, you should read those sections when planning and/or conducting the audit.

The legal matrix is depicted in a separate Excel file: [https://ohioauditor.gov/ocs/2023/Legal\\_Matrix.xlsx](https://ohioauditor.gov/ocs/2023/Legal_Matrix.xlsx). Entities are included alphabetically in the tab titled “OCS – Exhibit 5”.

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**DIRECT LAWS**

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

**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, or in the case of the City of Cincinnati, no later than October 1. This paragraph does not apply to school district appropriations.

**NOTE: The Governor's public health orders went into effect in March 2020, prior to the April 1, 2020 deadline. As a result, many local governments were unable to meet in person and were uncertain about whether the Ohio Rev. Code permitted virtual meetings to conduct business. The Ohio Attorney General later clarified that virtual meetings could be held during the period covered by the Governor's public health emergency in accordance with then-recently passed HB 197, but this guidance was not made publicly available until April 6<sup>th</sup>, 2020. The Governor's emergency public health orders were rescinded on June 18<sup>th</sup>, 2021 via Executive Order 2021-08D and are no longer in effect. From July 2, 2021 through February 16, 2022, in order for resolutions, rules, and other formal actions to be effective, a public body had to conduct meetings and hearings in person. During this time period, if members of public bodies were attending a meeting virtually these members were not considered present as in person, were not counted for quorum purposes, and could not vote. Effective February 17, 2022 through June 30, 2022, H.B. 51 allows members of public bodies to attend meetings virtually, considers them as if present in person, allows them to vote, and counts them for quorum purposes. H.B. 51 also gives resolutions, rules, and other formal actions the same effect as actions that occurred during an open meeting or hearing. Barring further additional legislation authorizing virtual meetings for public bodies, on July 1, 2022, public bodies will once again be required to hold meetings and hearings in person.**

~~For two year audits including the portions of calendar years 2020 and 2021 covered by the Governor's public health orders, auditors are encouraged to evaluate the due diligence on the part of the local government to convene a meeting as soon as possible, particularly once the Ohio Attorney General FAQs became available, and pass the permanent appropriations. In other words, if they were late but following due diligence AND did not overspend their temporary appropriations, auditors do not need to issue compliance citations. Instead, work papers should note the lateness and the evidence of due diligence observed. On the other hand, if there is no evidence of due diligence and/or temporary appropriations were overspent, a citation should be issued.~~

~~See also the Open Meetings Act COVID-19 guidance from the Ohio Attorney General:  
[https://www.ohioattorneygeneral.gov/Media/Newsletters/Open\\_Book/April\\_2020/Ohio\\_Open\\_Meetings\\_Act\\_Under\\_the\\_COVID-19\\_Emerge](https://www.ohioattorneygeneral.gov/Media/Newsletters/Open_Book/April_2020/Ohio_Open_Meetings_Act_Under_the_COVID-19_Emerge).~~

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. (Note: Except for those items covered by carryover encumbrances and federal and state grants/loans that are "deemed appropriated", money must be appropriated to be expended pursuant to Ohio Rev. Code § 5705.41. As a practical matter, a school district will have to pass some type of appropriation between July 1 and October 1 if it intends to expend money;

however, failing to file a temporary appropriation measure by July 1 does not violate Ohio Rev. Code § 5705.38(B).)

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>.

There are two circumstances when school district certificates/certifications would be issued after October 1<sup>st</sup>:

- 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.

### 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.)

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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.

<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.*

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.
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. [Ohio Rev. Code § 5705.36(A)]
- Budget stabilization reserves [Ohio Rev. Code §§ 5705.13, 5705.29(F)]
- The balance in a township reserve balance account established under Ohio Rev. Code § 5705.132.
- For some time, AOS policy has been that agency/custodial funds do not require budgeting. Agency/custodial funds<sup>6</sup> account for money a government holds in a custodial 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.

<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, 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.

<sup>5</sup> Ohio Rev. Code § 5705.131 refers to “nonexpendable trust funds.” There are many additional accounting and reporting considerations for these funds. See AOS Bulletins 2011-004, 2020-003 & 2020.008.

<sup>6</sup> GASB Statement No. 84 eliminates “agency funds” from existence and adds “custodial funds.” Most agency funds are consistent with the new definition for custodial funds and are not subject to budgetary requirements. However, with the implementation of GASB 84, some funds previously classified as “agency funds” may fall under another fund type where budgetary requirements do apply (e.g., special revenue).



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>• <del>Tiekler Files</del></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 the minutes and determine if the governing board adopted an annual appropriation measure by the required date.
2. If a school district has delayed adoption of an annual appropriation measure, inquire about the reasons for the delay.
3. Scan appropriation measures to determine whether they meet at least the minimum legal level of control Ohio Rev. Code § 5705.38(C) prescribes.
4. 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 §§ 5705.41 (D) and 5705.42 - Restriction upon appropriation and expenditure of money – certificate of fiscal officer.

**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>7</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].

**NOTE: An appropriation for federal COVID 19 funding, such as CARES Act, Consolidated Appropriations Act and the American Rescue Plan Act of 2021 moneys and Infrastructure Investment and Jobs Act is effectively created by operation of Ohio Rev. Code § 5705.42. Ohio Rev. Code § 5705.42 indicates Federal and State grants or loans are “deemed appropriated” for such purpose by the taxing authority as provided by law. In addition, those moneys are also treated as if they are in the process of collection by the fiscal officer of the subdivision. This means that under Ohio Rev. Code § 5705.42, the moneys are treated by the fiscal officer as if they have been appropriated for a specific purpose, without requiring the taxing authority to adopt an amended appropriation measure. However, the fiscal officer should include the appropriated amounts on the (amended) certificate. The fiscal officer should also record the appropriation in the accounting system. The “deemed appropriated” criteria applies to the COVID 19 funding but not to the funds for which the revenue is reallocated as described in AOS Bulletin 2021-004. The funds receiving the reallocation will need to estimate receipts and appropriate in the traditional manner.**

See [AOS COVID-19 FAQ's](#) and [AOS Bulletin 2021-004](#).

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

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<sup>7</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 “as such” which AOS interprets to be the accounting system\* and/or the budgetary statements or footnotes as applicable for their financial reporting framework. 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. (GASB Cod. 2400.702-14)

\*NOTE: If the auditee does not record the appropriation amount in the accounting system, but does report in the financial statements and/or footnotes, auditors should consider issuing a management letter comment for the auditee to record in their accounting system.



treasury **or in the process of collection**<sup>8</sup> to the credit of an appropriate fund free from any previous encumbrances. [Ohio Rev. Code § 5705.41(D)(1)]<sup>9</sup> <sup>10</sup>

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>11</sup>

Per Ohio Rev. Code § 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 Ohio Rev. Code § 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>12</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)]

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<sup>8</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>9</sup> Under Ohio Rev. Code §§ 9.10 and 9.11, 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>10</sup> Ohio Rev. Code § 3315.20 permits schools to incur a fund cash deficit in certain circumstances.

<sup>11</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>12</sup> 1987 Op. Att’y. 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 20XX, the government should charge the cost to 20XX appropriations, even if the fiscal officer signs a *Then and Now* Certificate in January 20XX+1.

Fiscal officers may prepare "blanket" certificates for a sum not exceeding an amount established by resolution or ordinance<sup>13</sup> adopted by the members of the legislative authority against any specific line item account over a period not extending<sup>14</sup> beyond the end of the current fiscal year. The blanket 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>15</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. Att'y. 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. Att'y. Gen. No. 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 as a fixed charge.

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

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<sup>13</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>14</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. The "extend beyond the fiscal year" language in the first two paragraphs of Ohio Rev. Code § 5705.41(D)(3) (first paragraph applicable to blanket certificates and second paragraph applicable to super blanket certificates) means that a blanket certificate and a super blanket certificate cannot be created to exist for more than one fiscal year. For example, you could not create one blanket certificate that is in effect for more than one fiscal year (e.g., FY22 through FY24). A blanket or super blanket certificate once issued can only exist in one single fiscal year. Nevertheless, once an expense or a non-continuing contract has been certified, there is no need to certify it again; the preservation of that money as available to meet that previously certified expense/contract remains in a subsequent fiscal year (i.e. represents a carryover encumbrance if a valid obligation does indeed exist). (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.)~~

<sup>15</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."~~

The Attorney General, in 1987 Op. Att’y. 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 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>• Ticker 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:**

1. Search for material unrecorded liabilities and/or encumbrances at year end. Refer to minutes and records immediately following the fiscal year cutoff date.
2. 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.
  - 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).<sup>7</sup>
3. 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.

4. 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 appropriation, ordinance – transfer – unencumbered balance – appropriation for 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 (1979), as well as in *Burkholder v. Lauber*, 6 Ohio Misc. 152 (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.

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:**

1. Inquire (or determine from reading the minutes) if amended or supplemental appropriation measures have been passed.
2. 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.
3. 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):**

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

**Summary of Requirements:** Each subdivision must establish (when applicable) the following funds:

- General fund [Ohio Rev. Code § 5705.09];
- Sinking fund whenever the subdivision has outstanding bonds other than serial bonds [Ohio Rev. Code § 5705.09];
- Bond retirement fund, for the retirement of serial bonds, notes, or certificates of indebtedness [Ohio Rev. Code § 5705.09];
- A special fund for each special levy [Ohio Rev. Code §§ 5705.09, 5705.2112(D)];
- A special bond fund for each bond issue [Ohio Rev. Code § 5705.09];
- 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 [Ohio Rev. Code § 5705.09];
- A special fund for each public utility operated by a subdivision [Ohio Rev. Code § 5705.09];
- A trust fund for any amount received by a subdivision in trust [Ohio Rev. Code § 5705.09];
- A sanitary police pension fund, an urban redevelopment tax increment equivalent fund, or a cemetery fund [Ohio Rev. Code § 5705.121];
- Fund balance reserves [Ohio Rev. Code § 5705.13 (see also Section 1-8)];
- A nonexpendable trust fund [Ohio Rev. Code § 5705.131];
- An urban redevelopment tax increment equivalent fund [Ohio Rev. Code § 5709.43];
- Downtown redevelopment district fund [Ohio Rev. Code § 5709.47];
- A township public improvement tax increment equivalent fund [Ohio Rev. Code § 5709.75];
- A redevelopment tax equivalent fund [Ohio Rev. Code § 5709.80].
- A Union Cemetery District permanent endowment fund [Ohio Rev. Code § 759.36] See also section 1-21 ~~1-25~~ – Permanent endowment funds.

Establishing these funds (or other funds statutes mandate) does not require Auditor of State authorization.

**NOTE: While Local governments do not need to seek AOS approval for establishing new funds for COVID-19 or Infrastructure Investment and Jobs Act federal programs, legislation to create the fund should be approved by the entity's governing board. Additionally, the governing board of direct recipients and Non-Entitlement Units should pass a resolution or formal action to apply for and accept COVID-19 funds.**

**For two year audits including any months falling within the covered period of ~~March 2020 to through~~ December 2021, local government subrecipients (i.e., certain counties, cities, villages and townships) of the Coronavirus Relief Funds distributed by the State under H.B. 481, as amended by H.B. 614, needed to only adopt the resolution or ordinance required by these bills. The resolution served as governing board authorization for the establishment of the Coronavirus Relief Fund.**

**Local governments have authority under Ohio Rev. Code § 5705.09 to establish new COVID-19, Infrastructure Investment and Jobs Act, and other federal funds, without seeking AOS approval.**

**Auditors should refer to the AOS COVID-19 FAQ, “How do I reimburse expenditures made out of other state and local funds with my COVID-19 federal funding?” and Bulletin 2021-004, when auditing the establishment of new funds for federal financial assistance related to COVID-19 funding.**

**Refer to AOS COVID-19 FAQs at: [https://ohioauditor.gov/resources/covid19\\_faqs.html](https://ohioauditor.gov/resources/covid19_faqs.html).**

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. [Ohio Rev. Code § 5705.12]

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.

Ohio Rev. Code §§ 5705.09(F) and 5705.10(I) imply that a resolution must be present in order for the restrictions on the use of the funds to be documented and evident. **As mentioned above, for two year audits including any months in the covered period of ~~March 2020~~ through December 2021, in the case of Coronavirus Relief Fund (CRF) moneys that a local government receives under H.B. 481 and/or H.B. 614, the resolution that the local government provided in order to receive the CRF moneys is sufficient to satisfy Ohio Rev. Code §§ 5705.09(F) and 5705.10(I).**

Also, as further described in GASB NCGAS 1, legal provisions governing the establishment of funds may sometimes conflict with GAAP. These differences often occur because constitutional, charter, or other legal provisions governing fiscal operations are antiquated and difficult to change. A variety of possible conflicts of this kind may be encountered. One type can arise from statutory specification of fund purpose and accounting requirements. For example, law may require that both operating and capital expenditures for a designated general governmental function be paid from and accounted for through the General Fund, even though the capital expenditures are financed by long-term borrowing. Such a provision violates the generally accepted accounting principle that such capital outlays financed from general obligation bond proceeds be accounted for through a Capital Projects Fund. Another example would be the statutory requirement of the cash basis of accounting for an Enterprise Fund, whereas the accrual basis is essential to determining an enterprise's financial position and operating results in conformity with GAAP.

While the budgetary basis of a local government’s accounting system must comply with legal requirements, the basic financial statements should be prepared in conformity with GAAP. Furthermore, local governments that want their independent auditors to express unqualified opinions that their financial statements are prepared in conformity with GAAP obviously must prepare statements in accordance with

these principles. GAAP-based reporting requires disclosure of material violations of legal and contractual provisions.

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>• <del>Tickler Files</del>/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:**

1. Compare funds on the subdivision’s chart of accounts with funds that existed in the prior audit period.
2. 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.)*
  - 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.
3. 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 §§ 131.01, 1545.23, 3315.20, 5155.33, 5705.01, 5705.05-.06, 5705.10, 5705.14(E) and 5735.28 - Distributing revenue derived from tax levies, proceeds from sale of bond issue, proceeds from sale of permanent improvement.

**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; Current expenses, as defined in Ohio Rev. Code § 5705.01(F), are “lawful expenditures of a subdivision, except those for permanent improvements, and except payments for interest, sinking fund, and retirement of bonds, notes, and certificates of indebtedness of the subdivision.”
- 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].

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>16</sup>

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)].

- "Public obligations" means both of the following: (1) Securities; (2) Obligations of a public issuer to make payments under installment sale, lease, lease purchase, or similar agreements, which obligations may bear interest or interest equivalent [Ohio Rev. Code § 131.01(GG)].
- "Fractionalized interests in public obligations" means participations, certificates of participation, shares, or other instruments or agreements, separate from the public obligations

<sup>16</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)



- themselves, evidencing ownership of interests in public obligations or of rights to receive payments of, or on account of, principal or interest or their equivalents payable by or on behalf of an obligor pursuant to public obligations.” [Ohio Rev. Code § 133.01(N)]
- "Bond retirement fund" means the bond retirement fund provided for in section 5705.09 of the Revised Code, and also means a sinking fund or any other special fund, regardless of the name applied to it, established by or pursuant to law or the proceedings for the payment of debt charges. Provision may be made in the applicable proceedings for the establishment in a bond retirement fund of separate accounts relating to debt charges on particular securities, or on securities payable from the same or common sources, and for the application of moneys in those accounts only to specified debt charges on specified securities or categories of securities. Subject to law and any provisions in the applicable proceedings, moneys in a bond retirement fund or separate account in a bond retirement fund may be transferred to other funds and accounts [Ohio Rev. Code § 131.01(D)].

**Note:** We wish to emphasize to governments and to their auditors the importance of complying with this. We have seen 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.

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, 3313.411, or 3313.413 the proceeds received from the sale shall be used to either: [Ohio Rev. Code § 5705.10(H)]

- 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.

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<sup>17</sup> 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>18</sup> However, after a county home has been closed

<sup>17</sup> **Permanent improvement** includes any capital asset with a useful life five years or greater. [Ohio Rev. Code § 5705.01(E)]

<sup>18</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.

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)].

Even if the permanent improvement was purchased or maintained with special levy revenue, the proceeds from the sale of the permanent improvement shall be credited in accordance with Ohio Rev. Code § 5705.10(F) or other specific statute that addresses the crediting or use of sale proceeds.

Monies collected under Ohio Rev. Code §§ 4501.04, 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>19</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<sup>20</sup>, but only if all of the following conditions are satisfied<sup>21</sup>:

- 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)]

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<sup>19</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.

<sup>20</sup> Deficits should not be permitted when the funding source is an automatic or cash advance payout from the State of Ohio (e.g. 467 Student Wellness Funds). That is, the deficit conditions prescribed by Ohio Rev. Code §3315.20 are only permissible when schools have to submit cash requests for payments to receive funding.

<sup>21</sup> **A school district, community school or STEM school may have a deficit in the special revenue fund established to receive funds from the Elementary and Secondary School Emergency Relief Fund under the CARES Act, Consolidated Appropriations Act and American Rescue Plan Act in fiscal year 2021 and 2022 when that deficit resulted from a temporary delay in the Department of Education’s ability to process claims reimbursements. [Sec. 209.60 of Am. Sub. H.B. No. 169 134<sup>th</sup> G.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>• Ticker 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 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.
3. Inspect accounting ledgers as of fiscal year end. 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.*

*Also, if management can demonstrate that the general fund had sufficient allowable resources to cover the deficit of a special fund, and management has documented an evaluation to that effect at the time the deficit was incurred then a citation may not be necessary. The key here is that management made this evaluation prior to incurring the deficit and documented it. Auditors should review evidence that such an evaluation occurred if that is the case. An evaluation not performed until after auditors have brought the matter to management's attention would not provide evidence of sufficient budgetary control and compliance and a citation would still be warranted. Even in situations where management has performed such an evaluation, we encourage the use of transfers and advances to avoid a special fund incurring a deficit (and an internal control recommendation would still be appropriate even if we determine a citation is not). (This note would not apply to schools as they must meet all exceptions as outlined in Ohio Rev. Code § 3315.20 – see testing in step 4)*

4. 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>.
  - 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.
5. 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.

6. 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.

<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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**1-6 Compliance Requirements:** Ohio Rev. Code §§ 5705.05-.06, and 5705.14-16- 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>22</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)]<sup>23</sup>
- Money may be transferred from the general fund to any other fund of the subdivision [Ohio Rev. Code § 5705.14(E)]. **Note:** Ohio Rev. Code § 5705.14 indicates “except in the case of transfer pursuant to division (E) of this section, transfers authorized by this section shall only be made by resolution of the taxing authority passed with the affirmative vote of two-thirds of the members.”

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<sup>22</sup> GASB 2300.127 requires certain disclosures regarding the amounts and purposes of transfers in the notes to the financial statements.

<sup>23</sup> An example would be a proprietary fund where the government sells its enterprise assets to a private vendor or another government.

According to 1989 Op. Att’y. Gen. No. 89-075, a resolution passed by a simple majority of the legislative authority is required to transfer moneys from the general fund to any other fund of the subdivision. When moneys are transferred from a fund other than the general fund in accordance with Ohio Rev. Code § 5705.14, a resolution passed by a two-thirds majority is required.

- 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.<sup>24</sup> 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, which includes approval of the Tax Commissioner. [Ohio Rev. Code § 743.05]
- 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

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<sup>24</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.



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 Ohio Rev. Code § 5101.161 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)].
- The transfers listed above 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 Tax Commissioner (effective 6/30/17)<sup>25</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>25</sup> Forms for the approval of the Tax Commissioner are available at <https://tax.ohio.gov/wps/portal/gov/tax/government/forms-for-local-officials>.

**NOTE:** Where a local government decided within the program period of performance but after the fiscal year end to reimburse eligible expenditures made prior to fiscal year end with allowable federal programs: This reimbursement activity, while allowable, has considerations that should be evaluated to determine if they are accounted for correctly and addressed any cut-off considerations appropriately in the preparation of their financial statements. See further guidance in Appendix A-1 of the [OCS Implementation Guide](#), [AOS Bulletin 2021-004](#), and AOS Advisory Memo, *Prior Fiscal Year Expenditures Reimbursed with Federal Funds in the Subsequent Fiscal Year* at [20210702-PriorFiscalYearExpenditures.pdf \(ohioauditor.gov\)](#).

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>• Ticker 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*.

1. 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.
  
2. 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.
  
3. Determine if selected transfers were authorized by vote of the governing board as described above.
  
4. If applicable, determine if selected transfers were authorized by the County Budget Commission, or Tax Commissioner as described above.

<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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**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 by estimated revenue); 5705.41 (restriction upon 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 Section ~~1-13~~ ~~4-16~~ if the subdivision accounts for a purchase of its own debt as an *investment* and *debt*. See Ohio Rev. Code §§ 133.03 and 133.29, and Appendix A-1 of the [OCS Implementation Guide](#), the Village Officer's Handbook ([Ohio Village Officer's Handbook](#)), and the Ohio Township Handbook ([Ohio Township Handbook 03-19.pdf](#)) for additional guidance on legal requirements applicable to intra-entity borrowing. Ohio Compliance Supplement Chapter 1, Section ~~1-13~~ ~~4-16~~ describes the legal compliance requirements for the issuance and retirement of manuscript debt.

**NOTE:** As explained in the Transfers section (OCS 1-6), upon availability of federal award funding, entities should use advances to cover temporary fund deficits if a COVID-19 program is operating on a cash request/reimbursement basis. Auditors must evaluate whether schools meet the criteria in Ohio Rev. Code § 3315.20, which 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:

- 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)]

~~ODE federal funding in CCIP is generally expenditure driven. However, federal funding outside CCIP can be advance funded or expenditure driven. -funding many of the school COVID-19 federal programs to schools, which~~ Advanced funding would preclude a school district from satisfying the request for payment criterion above. Where federal programs are advance-funded, Ohio Rev. Code § 3315.20 cannot be relied upon to avoid advancement of funds to prevent fund cash deficits.

**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 Ohio Rev. Code § 731.56, 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”. For more information, see the Manuscript Debt section in section 1-13 (*Previously 1-16*) *Compliance Requirement: Ohio Rev. Code §§ 133.29, 135.14, 135.35, 731.56-.58, 1995 Op. Att’y. Gen. No. 55-5263, and 1985 Op. Att’y. Gen. No. 85-072 - Governments investing in their own securities.*

<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>• Presence of Effective Accounting System</li> <li>• Independent Inspection/Comparisons of Advances and Source Documentation</li> <li>• Ticker 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. 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.

2. 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.
3. 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.
4. 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.
5. 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, 5705.132, 5705.222 and 5705.29 - 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;
- Ohio Rev. Code § 5705.222(C) – Reserve balance account for county board of developmental disabilities;
- Ohio Rev. Code § 5705.29 – Contingencies may be established not designated for any particular purpose.

**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>26</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>27</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>28</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.

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<sup>26</sup> Ohio Rev. Code § 5705.13 refers to these accounts as “reserve” accounts. However, for the GASB Statement No. 54 financial reporting that 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. Note: Bulletin 2020-008 simplified the reporting of fund balance classifications in the AOS regulatory cash basis financial statements and footnotes beginning with the December 31, 2020 FYE reporting.

<sup>27</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, under Ohio Rev. Code § 5705.13(A)(3). This is our AOS opinion; however, statutory language is less than precise, and may be subject to an alternative interpretation if accompanied with a well-reasoned legal opinion.

<sup>28</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.

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 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>29</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.
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>30</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

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<sup>29</sup> Similar to the preceding note, GAAP/OCBOA governments should report these amounts as *committed, assigned, or restricted* fund balance as appropriate under the circumstances described in GASB Statement No. 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. Note: Bulletin 2020-008 simplified the reporting of fund balance classifications in the AOS regulatory cash basis financial statements and footnotes beginning with the December 31, 2020 FYE reporting.

<sup>30</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.

established under this section cannot exceed, *at any time in any fiscal 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>31</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>32</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.

**Note:** Steps 5 and 6 do not apply to a subdivision or taxing unit for which the county budget commission has waived the requirement to adopt a tax budget pursuant to section 5705.281 of the Revised Code. The tax budget shall present the following information in such detail as is prescribed by the Auditor of State.

5. Ohio Rev. Code § 5705.29(A)(1) Allows entities (except schools) to establish contingencies, not designated for any particular purpose (contingency reserve balance – spending reserve) and not to exceed 3% of appropriations for current expenses.
6. Ohio Rev. Code § 5705.29(A)(1) Allows school districts to establish contingencies, not designated for any particular purpose (contingency reserve balance – spending reserve) and not to exceed 13% of appropriations for current expenses.
  - a. In the fiscal year in which a levy is first extended, an estimate of expenditures to be known as a **voluntary contingency reserve balance**, which shall not be greater than 25% of the total amount of the levy estimated to be available for such year. (Ohio Rev. Code § 5705.29(E)(1)).
  - b. In the fiscal year following the year in which a levy is first extended an estimate of expenditures to be known as a **voluntary contingency reserve balance**, which shall not be greater than 20% of

<sup>31</sup> Appendix IV-5 of the March 2019 [Ohio Township Handbook](#) lists all *Other Financing Sources*.

<sup>32</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.

the total amount of the levy estimated to be available for such year. (Ohio Rev. Code § 5705.29(E)(2))

The full amount of any reserve balance shall be retained by the county auditor and county treasurer out of the first semiannual settlement of taxes until the beginning of the next succeeding fiscal year where it shall be turned over to the board of education to be used for the purposes of such fiscal year. Except in cases where by two thirds vote, the board of education appropriates (for any lawful purpose) any amount withheld for this contingency during the fiscal year; wherein, the county auditor shall draw a warrant payable (from the districts account) to the district in the amount requested. (Ohio Rev. Code § 5705.29(E)(3-4))

7. *County Board of Developmental Disabilities*

Ohio Rev. Code § 5705.222(C) requires the county auditor, upon receipt of a resolution from the county board of developmental disabilities, to establish a capital improvements account or a reserve balance account, or both, as specified in the resolution. The capital improvements account shall be a contingency account for the necessary acquisition, replacement, renovation, or construction of facilities and movable and fixed equipment. Upon the request of the county board of developmental disabilities, moneys not needed to pay for current expenses may be appropriated to this account, in amounts such that this account does not exceed twenty-five per cent of the replacement value of all capital facilities and equipment currently used by the county board of developmental disabilities for developmental disabilities programs and services. Other moneys available for current capital expenses from federal, state, or local sources may also be appropriated to this account.

The reserve balance account shall contain those moneys that are not needed to pay for current operating expenses and not deposited in the capital improvements account but that will be needed to pay for operating expenses in the future. Upon the request of a county board of developmental disabilities, the board of county commissioners may appropriate county funds, including funds from federal and state sources, to the reserve balance account. The total balance in a reserve balance account shall not exceed forty per cent of the county board of developmental disabilities' expenditures for all services in the preceding calendar year. Amounts in a capital improvements account or reserve balance account that are not in excess of the limitations prescribed in this division shall be considered reasonable and shall not be taken into consideration by the county budget commission when determining whether to reduce the taxing authority of a county under Ohio Rev. Code § 5705.32.

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>• <del>Tickler Files</del>/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. 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 27.
  - For self-insurance and worker's compensation reserve accounts, compare amounts reserved to estimates received from the entity's actuary.
2. 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).
3. 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.
4. 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.
5. If an entity (other than a school district) has established a voluntary contingency reserve balance:
- 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 reserve is limited to 3% of appropriations
  - For self-insurance and worker's compensation reserve accounts, compare amounts reserved to estimates received from the entity's actuary.
6. If school district has established a voluntary contingency reserve balance:
- 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 is limited to the lesser of:
    - 13% of appropriations for current expenses; or
    - 25% of the total amount of the levy estimated to be available for the initial year, or 20% in succeeding years.
  - For self-insurance and worker's compensation reserve accounts, compare amounts reserved to estimates received from the entity's actuary.
7. If a county board of developmental disabilities has established a reserve balance account:
- Recalculate reserve percentages and inspect accounting ledgers to determine whether the amount reserved is limited to 40% of the county board of developmental disabilities expenditures for all services in the preceding calendar year.

**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):**



**1-9 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>• <del>Tickler Files</del>/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. During revenue tests, trace a representative number of children services agency receipts to the 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):**

**1-10 (Previously 1-13) Compliance Requirement:** Ohio Const. Art. XII, Section 11; Ohio Const. Art. XVIII, Section 12, Ohio Rev. Code §§ 133.10, 133.22, 133.23, 133.24, 133.26, 167.041, 308.08, 308.09, 321.34, 505.262, 505.401, 3318.36, 5531.10, 5705.03, 5705.05, 5705.09, 5705.10 and 5705.2113; 1981 Op. Att’y. Gen. No. 81-035 and 1996 Op. Att’y. Gen. No. 96-048 – Issuing or Retiring Bonds and Notes.

### Summary of Requirements:

#### *Common Types of Debt*

**BACKGROUND INFORMATION:** Per Ohio Rev. Code § 133.01(Q), *general obligation (G.O.)* 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>33</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 may levy sufficient taxes annually as are necessary to pay the interest and sinking fund on and retire at maturity the 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

<sup>33</sup> Pledged revenue is revenue the debt legislation or covenant provisions pledged as collateral to the debt owners.

any year may be reduced by the amount to be available from special assessments,<sup>34</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>35</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 and rescue 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]

#### ***Debt Issuance for Qualifying Partnerships (Career-Technical Education Compact)***

Pursuant to Ohio Rev. Code Chapter 133, 5705.2113 a ***Qualifying Partnership***<sup>36</sup> may declare that it is necessary to issue general obligation bonds to acquire "classroom facilities and necessary appurtenances", subject to the approval of a majority of the electors in the combined territory. Under the authority of Ohio Rev. Code § 5705.2112 and 5705.2113, a qualifying partnership may levy and issue taxes to pay for all or part of the bonds pledged for the Classroom Facilities project. Further, pursuant to Ohio Rev. Code §§ 3318.71, 5705.2112, and 5705.2113, the member districts in the compact agreement (i.e., contract) must designate a fiscal agent to act on behalf of the members in the qualifying partnership. Auditors should carefully review the contract agreement of the Qualifying Partnership to determine the exact terms and conditions along with potential bond covenants related to the bond issuance that must be maintained by the members of the qualifying partnership. Additionally, auditors must assess which school district the related debt issuance belongs to and whether the qualifying partnership has its own-source revenue for purposes of determining "legally separate" and other GASB Codification 2600 criteria. Generally, all member districts of the qualifying partnership share equal responsibility for the related bond obligation. These can be

<sup>34</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>35</sup> Unless the grant regulations prohibit debt payments. For example, 2 C.F.R. 200.449(a) would generally permit using Federal grants to pay debt related to assets used in Federal programs.

<sup>36</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]

complex determinations; therefore, auditors are encouraged to consult with the Center for Audit Excellence as needed.

### ***Debt Issuance for Regional Airport Authorities***

Ohio Rev. Code § 308.08 provides additional borrowing authority for regional airport authorities. This section allows the airport to issue revenue bonds to construct, replace, extend, enlarge, maintain, or operate any airport or airport facility (or repay or refund any outstanding debt issues related to the aforementioned purposes). The bonds may be collateralized by pledged revenues and do not impose any liability on the airport, except the creditor's right to the pledged revenue. This debt is not a general obligation. Additionally, Ohio Rev. Code § 308.09 permits the board of trustees of the regional airport authority to secure the revenue bonds via trust agreement with a corporate trustee. This trust agreement may not convey or mortgage any of the regional airport authority property nor pledge the general credit of the regional airport authority.

### ***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.

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. Att'y. Gen. No. 96-048]<sup>37</sup>

### ***Special Features***

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<sup>37</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. Att'y. Gen. No. 96-048 provide specific authority for townships to issue Chapter 133 securities for the purposes this paragraph describes.

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 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>38</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>39</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. Att’y. 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.

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<sup>38</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. [Ohio Rev. Code § 133.16] Do not confuse this with *capitalized interest discussed in GASB Statement No. 34, 37, 62* (¶10), §2 etc.

<sup>39</sup> Ohio Rev. Code § 5531.10(C) does not require establishing 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 consistent. 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).

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. [Ohio Rev. Code § 5705.14]

- 1981 Op. Att’y. Gen. No. 81-035 further clarifies ‘commingled’ funds with the following and says that counties wishing to spend moneys in a general fund directly for a specified purpose must be able to establish that no ‘restricted’ funds are being used:

*“the use of some of the revenue deposited in the general fund of a subdivision is not restricted by law (except, of course, by the public purpose requirement), it may, in fact, be restricted by practical considerations. Where moneys from various sources are deposited in the general fund and thereafter become commingled, it may be difficult or impossible from a practical standpoint to insure that general levy revenues or any other similarly restricted revenues would not be included within a proposed expenditure.”* Additionally, *The Supreme Court of Ohio, in State ex rel. Locher v. Menning, 95 Ohio St. 97, 99, 115 N.E. 571, 572 (1916), held as follows: “The authority to act in financial transactions must be clear and distinctly granted, and, if such authority is of doubtful import, the doubt is resolved against its exercise in all cases where a financial obligation is sought to be imposed upon the county.”*

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. Att’y. 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)]



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>• Ticker 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**

Note: Procedures 1 through 3 apply to all entity types. In addition, procedures 4 through 9 would apply to the entity types listed in the corresponding headings.

**All Entity Types**

1. 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:
  - a. The legality of the source of repayment and collateral<sup>40</sup>. (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.)
    - i. 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.
    - ii. Whether the government used the proceeds for the purposes authorized.
    - iii. Whether the government made any debt covenants in the debt legislation. Auditors should select material debt covenants for testing annually to ensure ongoing compliance. In addition, if the debt is subject to the filing requirements of the Municipal Securities

<sup>40</sup> Auditors may consult with CFAE if they encounter complex arrangements associated with the offerings. Such complexities may include interest rate swaps. For Ohio governments, interest-rate swaps normally refer to debt issued at a variable interest rate, which the government (issuer) converts to a fixed interest rate.

- Swaptions describe an option to swap variable for fixed-rate debt if the strike rate meets the forward rate.
- Swaps and swaptions can result in deferred inflows or outflows, but if properly used they are hedging instruments, designed to hedge (i.e. reduce) interest-rate risk. If properly used, they are not classified as investments.

Swaps and swaptions are derivatives per GASB Statement No. 53 (GASB Cod. D40.103--109), but they do meet the Ohio Rev. Code 135 derivative definition; therefore Ohio Rev. Code 135 does not prohibit them.



Rulemaking Board (MSRB), auditors should include Optional Procedures Manual Section O-8 and perform testing accordingly.

- iv. 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.
  - v. 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.)
2. 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)]
  3. 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:
    - a. 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)];
    - b. Restrictions, if any, in the debt-authorizing legislation were followed;
    - c. Revenue derived from a general levy for current expenses is not used to pay debt charges [Ohio Rev. Code § 5705.05]; or
    - d. 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. Att'y. 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***

4. 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,

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

5. Review the agreement and determine if they are following the requirements;

- 6. Determine expenditures for the loans are for proper public purposes;
- 7. Determine if the repayment for the loans is paid from the proper fund.

***Career-Technical Education Compact Qualifying Partnerships***

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

If so,

- a. trace the bond issuance to the respective budget(s);
- b. inspect the resolution(s) authorizing the bond issuance;
- c. determine whether the issuance is in accordance with Ohio Rev. Code Chapter 133 requirements; and
- d. determine whether the proceeds were used to acquire classroom facilities.

***Regional Airport Authority***

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

If so,

- a. inspect the resolution authorizing the bond issuance;
- b. determine whether the proceeds were used to construct, replace, extend, enlarge, maintain, or operate any airport or airport facility;
- c. If secured with a trustee, obtain and evaluate the agreement to determine that it does not convey or mortgage any of the regional airport authority property nor pledge the general credit of the regional airport authority.

**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):**

**1-11 (Previously 1-14) 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>41</sup> Long-term TAN are *generally* subject to (2) below.<sup>41</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)]

Ohio Rev. Code § 133.10(A) applies to subdivisions generally, Ohio Rev. Code § 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)]

#### **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)]

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<sup>41</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 Cod. B50 and GFOA's Annual Comprehensive Financial Report (ACFR) checklist for guidance on GAAP debt classifications.

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 Ohio Rev. Code § 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 Ohio Rev. Code § 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 Ohio Rev. Code § 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>42</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)]

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<sup>42</sup> A *Lakeshore improvement project* includes constructing ("Construction" includes acquisition, alteration, construction, creation, development enlargement, equipment, improvement, installation, reconstruction, remodeling, renovation, or any combination thereof) 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>• <del>Tickler Files</del>/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:**

1. 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.
2. Determine whether:
 

**Note:** For Lake Erie Shoreline Improvements only steps d and e apply.

  - a. 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.)
  - b. 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.)
  - c. The government repaid the debt with the pledged or other legal revenue (RAN and TAN), or refinanced BAN according to the BAN legislation.
  - d. The government properly segregated any revenue pledged for debt service and used that revenue for debt service.
  - e. The government used the note proceeds for the purposes authorized.

- f. Identify material debt covenants by reviewing the debt documents, official statement and opinions of bond counsel. Annually test material covenants to ensure ongoing compliance throughout the life of the outstanding 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):**



**1-12 (Previously 1-15) 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 either receives an allocation of the library fund, or, levies a property tax under Ohio Rev. Code § 5705.23 to anticipate its portion of the proceeds of the library fund distribution or the property tax 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 or the property tax receipts.

The maximum annual debt service for these notes cannot exceed:

1. 40% of the average LLGSF funding (public library funds) the library received for the two years preceding the year the notes were issued
2. The portion of the lawfully available proceeds from the property tax levied under Ohio Rev. Code § 5705.23 that the board has, in the authorizing proceedings, covenanted to appropriate annually for the purpose of paying note service charges.

The notes are payable from the LLGSF monies (public library funds) or the property tax receipts 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 40 years from the date of the original issue of notes.

<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>• <del>Ticker Files</del>/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:**

1. By reading the minutes, inspecting bond ledgers or other documents, or by inquiry, determine if the library used this type of borrowing.
2. Calculate, or inspect the library's calculations, that the maximum annual note debt service charges does not exceed 40% 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.)
3. Inspect the notes for the statement that the notes are payable solely from the resources 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.
4. Inspect the notes for the maximum maturities of 10/40 years.
5. Identify material debt covenants by reviewing the debt documents, official statement and opinions of bond counsel. Annually test material covenants to ensure ongoing compliance throughout the life of the outstanding 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):**

**1-13 (Previously 1-16) Compliance Requirement:** Ohio Rev. Code §§ 133.29, 135.14, 135.35, 731.56-.58, 1995 Op. Att’y. Gen. No. 55-5263, and 1985 Op. Att’y. Gen. No. 85-072 - 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. Att’y. 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 shall 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.

### **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. Att’y. 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. 1300.122 and 1800.102(a)).

GAAP Governments must use the Advance/Interfund method for financial statement reporting (GASB Cod. I50.701-4). 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>• Ticker 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:**

1. Determine whether the entity issued manuscript debt during the audit period or has any manuscript debt outstanding as of fiscal year end.
2. 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.
3. Determine the issuance date<sup>43</sup> of the debt/investment and review the entity’s debt/investment schedules to determine whether the principal matured within five years.
4. 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.
5. **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.
6. **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.
7. 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).

<sup>43</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.

**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):**



**1-14 (Previously 1-17) Compliance Requirements:** Ohio Admin. Code 117-2-03(B) and 126:3-1-01(A)(2)(a) and Ohio Rev. Code §§ 117.38, 167.04, 991.06, 1724.05 and 1726.11, and AOS Bulletin 2015-007 - Annual financial reporting.

### Summary of Requirements:

The Auditor of State prescribes and requires by rules, that certain public offices prepare and file annual financial reports in accordance with generally accepted accounting principles. Certain public offices may also be required by statute, rule, or agreement to prepare and file performance or other special purpose reports.<sup>44</sup>

**Note:** The Auditor of State (AOS) requires the use of the Hinkle Annual Financial Data Reporting System (Hinkle System), 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), for all entities that are statutorily mandated to file financial reports. Each entity shall file its financial report annually via the Hinkle System, and it is the expectation of AOS that each entity will only submit the filing once by the statutory due date (or approved extension date.) Prior to submitting the filing, the entity should complete all reviews, verify the correct basis of accounting has been selected, and view the uploaded file to ensure it is the correct and complete file. Refer to the AOS website at <https://ohioauditor.gov/financialreporting/default.html> and AOS Bulletin 2015-007 for additional information. Additionally, auditors should perform a GASB Codification 2600 analysis for entities not mentioned in AOS Bulletin 2015-007 to determine whether they may be legally separate for financial reporting purposes. This analysis should be documented in the entity's permanent file.

Ohio Rev. Code § 991.06 requires The Ohio Exposition Commission to file annual financial reports with the Auditor of State no later than September 30<sup>th</sup> of each year.

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

Ohio Admin. Code 117-2-03(B) requires counties, cities, school districts, educational service centers, community schools, and government insurance pools 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 Rev. Code § 3345.72 and Ohio Admin. Code 126:3-1-01(A)(2)(a) to report annually [but not necessarily account] on a GAAP basis.

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>45</sup>

<sup>44</sup> Ohio Admin. Code 117-10-01(B) requires county and independent agricultural societies to record and report all financial transactions in accordance with Appendix A of the Auditor of State manual, "Uniform System of Accounting for Agricultural Societies." This Manual is available at [www.ohioauditor.gov](http://www.ohioauditor.gov), under *Resources/Publications*.

<sup>45</sup> We will cite noncompliance if a "GAAP mandated public office" files special purpose framework (OCBOA) - cash, modified cash or regulatory cash financial statements. When citing, follow the appropriate example from the standardized comments found on the AOS Intranet.

Per AOS Bulletin 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>46</sup>

### **Cash Basis Entities**

Per Ohio Rev. Code § 117.38, entities filing on a cash-basis<sup>47</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>48</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>46</sup> The AOS may waive these penalties, upon the filing of the past due financial report.

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>49</sup>.

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<sup>46</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>47</sup> Cash basis includes special purpose framework (OCBOA)-cash, OCBOA modified cash and regulatory cash basis.

<sup>48</sup> Ohio Rev. Code § 117.01(D) states in part that, as used in Ohio Rev. Code Chapter 117, “*Public office* means any state agency, public institution, political subdivision, 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. Att’y. 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 community schools qualify as public offices as defined under this section.

<sup>49</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:** 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.) Failing to include the Management’s Discussion & Analysis when filing would not be considered a lack of controls over financial reporting or materially impact the financial statements; therefore would be reported in the management letter.

Material noncompliance would exist if:

- An entity subject to GAAP did not follow GAAP in its annual report.
- An entity’s filing was significantly incomplete (see discussion of complete in the *GAAP Basis Entities* and *Cash Basis Entities* sections above).For additional information, refer to AOS Bulletin 2015-007.
- The filing was significantly misstated.

**Councils of Governments**

Ohio Rev. Code § 167.04(D) requires the officers of a council of governments to notify the Auditor of State of the regional council’s formation, provide a copy of the council’s by-laws, and provide on a form prescribed by the auditor of state any other information regarding the regional council that the Auditor of State considers necessary. The council shall take no official action, other than formation, before notifying the Auditor of State of its formation in accordance with this section. Any official action the council takes before making such notification, including entering into any contract, is void.

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:**

1. Confirm whether the report was filed timely.

**Note:** The Hinkle System tracker and/or GPInfoSearch include 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>50</sup>

2. Auditors should inspect the filed report (AOS auditors can obtain this report through the Hinkle System tracker and/or GPinfoSearch. GPinfoSearch information is available to contracted IPA firms for their clients via logging into the IPA Portal.)
3. 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, 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>51</sup>
4. Determine whether the filed report includes the financial statements, notes to the financial statements, and required supplementary information (if applicable) (i.e. determine if the filing was substantially **complete** as described above.
5. 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. A re-filing should only occur in situations where the original filing was incomplete, the basis of accounting identified in the filing is inconsistent with the financial statements and/or notes to the financial statements filed, or the financial statements were either unauditably or for a different reporting year. Modifications to the financial statements, such as an inclusion/modification of a note disclosure or correction of an error that was noted during the audit, are **not** reasons for re-filing. Errors identified should be considered during the audit, and any adjustments should be reflected in the financial statements in the audit report. Re-filing the financial statements does not eliminate the auditor's responsibility for consideration of errors noted. Auditors should not request an entity to re-file without first contacting the Hinkle System administrator ([HinkleSystem@ohioauditor.gov](mailto:HinkleSystem@ohioauditor.gov)) to determine if the re-filing is appropriate. If a public office is required to refile financial statements due to an incomplete filing, 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>52</sup>. Failure to file via the Hinkle System may result in the AOS declaring the public office "unauditable."

Ohio Rev. Code § 117.41 enables the AOS to declare a public office to be "unauditable" when its accounts, records, files or reports have been improperly maintained and, as such, are insufficient to allow the audit to be performed.

6. If the government is not mandated to follow GAAP and presents AOS Regulatory cash basis ("AOS basis") financial statements (rather than OCBOA cash or OCBOA modified cash financial statements ("GAAP look-alike")):

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<sup>50</sup> Auditor judgment may be required to determine if a non-compliance citation should be issued, considering whether the client made a good-faith effort to file by the statutory or extended due date.

<sup>51</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>52</sup> Auditors should use professional judgement when determining whether to report noncompliance with timely filing if the public office or other entity required to file originally submitted timely but had to refile in order for the AOS/IPA firm to audit the financial statements submitted via the Hinkle System. ~~However, GAAP mandated public offices should be cited if the final financial statements filed via the Hinkle System are not GAAP basis.~~

- Follow AU-C 800.22 which applies when regulatory cash basis statements are available for general use (local government statements we or IPAs audit are available for general use). AU-C 800.22 requires issuing a dual opinion:
  - An adverse opinion on conformance with GAAP.
  - A second opinion on the regulatory cash basis.
- 7. If a GAAP-mandated government does not follow GAAP or present OCBOA cash or OCBOA modified cash (“GAAP look alike”) basis financial statements but presents regulatory cash basis (“AOS Basis”) financial statements:
  - Issue adverse opinion on conformance with GAAP.
    - These governments do not qualify for the “dual opinion.”
  - Issue GAGAS noncompliance finding.
- 8. If a GAAP-mandated government presents their financial statements using OCBOA cash or OCBOA modified cash basis (“GAAP look-alike”):
  - Follow AU-C 800.A31 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 the basis of accounting is other than GAAP.
  - Issue GAGAS noncompliance finding.

**Councils of Governments (COG)**

- 9. For any new COG established, review the Auditor of State’s listing of registered COGs (<https://ohioauditor.gov/local/cog/CogListing.aspx>) and determine if the COG has completed the registration process with the Auditor of State as required.

**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):**

**1-15 (Previously 1-18) Compliance Requirements:** Ohio Rev. Code §§ 1702.57, 1724.05, 1724.06, 1726.11, and 1726.12 - GAAP and annual financial reporting for community improvement corporations (CICs)<sup>53</sup> and development corporations (DCs).<sup>54</sup>

**Summary of Requirements:** Annual Reporting

The Auditor of State prescribes and requires by rules, that certain public offices prepare and file annual financial reports in accordance with generally accepted accounting principles. Certain public offices may also be required by statute, rule, or agreement to prepare and file performance or other special purpose reports.

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>55</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 three circumstances:

- When a CIC/DC files its annual report more than 90 days delinquent (i.e., does not file its annual GAAP financial statement report within 210 days of its fiscal year end).
- When a CIC/DC does not present auditable records within 90 days of a determination by the Auditor of State that a corporation is unauditabile.
- When a DC has failed to begin business for a period of three years from the effective date of the filing of its articles of incorporation.

~~Late filings are handled by the Hinkle System Coordinator, and the regional chief auditor will handle those that are declared unauditabile and fail to file within 90 days, who forward to the Chief Deputy Auditor for certification. Late filing notifications to the Secretary of State will be prepared by the Hinkle System Coordinator for approval by the Chief Deputy Auditor after determining the region has communicated with~~

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<sup>53</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 chapter 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 chapter 1724 or 1726.

<sup>54</sup> Development corporations organized under Ohio Rev. Code Chapter 1726 are stock-issuing entities.

<sup>55</sup> CICs or DCs that do not file GAAP statements and notes (and required supplementary information, if any) within 210 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. Att’y. 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.)

the CIC/DC, and the regional chief auditor will prepare the unauditable declaration for approval by the Chief Deputy Auditor, if applicable.

Upon certification, the Secretary of State is to cancel the Corporation’s articles of incorporation until the deficiency is remedied.

**Secretary of State Requirements (SoS)**

The Secretary of State of Ohio maintains a database ([SoS Database](#)) which details the status of all corporations with respect to Ohio Rev. Code § 1702.57, which states in part “No person shall exercise or attempt to exercise any rights, privileges, immunities, powers, franchises, or authority under the articles of a domestic corporation after such articles have been canceled or after such corporation has been dissolved or after the period of existence of the corporation specified in its articles has expired.”

Those statuses are:

- Active – The Corporation is allowed to legally function.
- Dead – The corporation cannot legally function because the corporation has taken action to dissolve
- Cancelled – The corporation cannot legally function because the SoS has taken action to dissolve the corporation (as the result of inactivity by the corporation)
- Held – The Corporation cannot legally function under this status but the SoS has placed a hold on the corporation’s name for one year (in case they want to reinstate) before moving the status to *cancelled*.

<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>• Presence of an Effective Accounting System</li> <li>• Legislative and Management Monitoring</li> </ul>		

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

1. If testing in OCS ~~1-14~~ 1-17 indicates the corporation’s report has NOT been filed, notify the corporation immediately of the requirement to file (per AOS Bulletin 2015-007, the financial statements file via the Hinkle System must be audited.) After notification, if the corporation does not file:
  - a. The regional 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 and/or declare the corporation unauditable. (*Note:* IPA firms should contact the regional chief auditor regarding these issues.)
  - b. If a corporation does not file its annual GAAP financial statement report via the Hinkle System within 210 days of its reporting year end, or does not present auditable records within 90 days of



the Auditor of State’s determination of unauditability, the AOS must notify the Secretary of State’s Office.<sup>56</sup>

2. If a corporation is operating and has created financial statements and filed them with the AOS via the Hinkle system, but are not in “Active” status auditors should:
  - a. Continue to audit the entity (inactive status does not mean the entity is not subject to audit);
  - b. Consider whether the situation constitutes an illegal operation which will likely be considered to be non-compliance with Ohio Rev. Code § 1702.57;
  - c. If this should be referred to the Secretary of State, contact the Regional Chief Auditor.<sup>56</sup>

**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>56</sup> Refer to the process for “Referrals to Ohio Secretary of State” as described in the OCS Implementation Guide.

**1-16 (Previously 1-19) Compliance Requirement:** Ohio Rev. Code §§ 9.833 and 305.172 - Health Care Self Insurance<sup>57 58</sup>

**Summary of Requirement:** Ohio Rev. Code § 9.833 requires individual, self-insured governments (or county board of developmental disabilities) or joint self-insured health-care programs to calculate (i.e., reserve<sup>59</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. Programs must prepare (i.e. obtain) and maintain a 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.<sup>60</sup> 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 a special fund<sup>61</sup> 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 and/or see table at [https://ohioauditor.gov/ocs/2023/Self\\_Insurance\\_Table\\_2022-11.xlsx](https://ohioauditor.gov/ocs/2023/Self_Insurance_Table_2022-11.xlsx).

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<sup>57</sup> Ohio Rev. Code § 9.833(D) also permits subdivisions or county boards of developmental disabilities 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>58</sup> Ohio Rev. Code §§ 305.172 and 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>59</sup> “Reserve” in this context means liabilities measured in accordance with accepted actuarial principles.

<sup>60</sup> This is presumed to be satisfied through submission on the Hinkle system.

<sup>61</sup> Ohio Rev. Code § 9.833(C)(2) indicates political subdivisions shall establish a “special” fund to account for this activity. GASB Cod. C50.126 through C50.131 (GASB Statement No. 66) permits the use of governmental funds or internal service funds for this purpose. See GASB Cod. C50.715-2 for further guidance. Note: The law requires the use of a “special” fund. We interpret this to mean either a special revenue fund or internal service fund. Additionally, under GASB requirements, regardless of the legal accounting requirements, it would be permissible to combine this fund with the general fund for financial statement reporting purposes.

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>• Ticker 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:**

Questions are organized according to the Self Insurance table

([https://ohioauditor.gov/ocs/2023/Self\\_Insurance\\_Table\\_2022-11.xlsx](https://ohioauditor.gov/ocs/2023/Self_Insurance_Table_2022-11.xlsx)), and only test for ‘required’ or ‘prohibited’ compliance elements as follows:

- Single Subdivision<sup>62</sup> Programs test: 1, 2a, 4
- Single Municipality Programs test: none (no required or prohibited elements)<sup>63</sup>
- Pool Members test: 1, 2a, 3
- Pools test: 2b, 4

1. [Ohio Rev. Code § 9.833(C)(2)] Was a separate internal service special fund<sup>61</sup> established by ordinance or resolution to account for all claims, administrative and other related program costs?
2. [Ohio Rev. Code §§ 9.833(C)(2&6) & 5705.10] Are self-insurance fund costs recovered by appropriate charges:
  - a. Single Subdivision Programs or Pool Members: to other funds based on those funds’ relative exposures or loss experiences? (These interfund charges should be recorded as revenues and expenditures rather than transfers, and are not subject to the restrictions on interfund transfers or Ohio Rev. Code § 5705.14 - .16)
  - b. Pools: to participating subdivisions based on the subdivisions’ relative experience, loss exposure or as otherwise agreed by contract?

<sup>62</sup> Ohio Rev. Code §§ 9.833 and 2744.01 define a political subdivision in part 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. According to 2017 Op. Att’y. Gen. No. 2017-001, a person authorized by a board of county commissioners or a board of township trustees to perform work related to the demolition of vacant or abandoned buildings and the remediation of other nuisance properties is considered an “employee” when acting within the scope of their employment even if not compensated for the work. As used in Ohio Rev. Code § 9.833, a “political subdivision” also includes the entity types described in Ohio Rev. Code § 3905.36. Ohio Rev. Code § 9.833 also says “County Board means a county board of developmental disabilities.”

<sup>63</sup> These programs are not required to establish a separate internal service “special” fund. However, if they do establish such a fund, then the procedures related to recovering the costs are applicable and required.

Note: If the answer is no to either of the above, does another appropriate and allowable financing source exist to cover the costs?

3. [Ohio Rev. Code § 5705.13(A)(2)] Are there any reserves established on fund equity to provide for self-insurance costs?
4. [Ohio Rev. Code § 9.833(C)(1&4)] Was a report prepared by a member of the American Academy of Actuaries<sup>64</sup> within 90 days of year end listing where:
  - a. The actuary's opinion language (including the scope of the work):
    - i. Generally complied with the example described in the "Actuarial Opinions" section of AOS Bulletin 2001-005, and  
*Note: Consider whether any qualification in the actuary's report affects the financial statement opinion or indicates noncompliance with Ohio Rev. Code § 9.833.*
    - ii. Indicated amounts reserved conform to accepted loss reserving standards.
  - b. The actuarial liability as of the last day of the fiscal year, and
  - c. Program disbursements, including claims paid, legal representation and consultant costs?

**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>64</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.

**1-17 (Previously 1-20) 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 shall be submitted by the pool administrator to the Auditor of State, and it should be retained by the government to 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 & 2011-008 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>• <del>Ticker Files</del> 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>		

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

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

Questions are organized according to the *Self Insurance table*

([https://ohioauditor.gov/ocs/2023/Self\\_Insurance\\_Table\\_2022-11.xlsx](https://ohioauditor.gov/ocs/2023/Self_Insurance_Table_2022-11.xlsx)) from AOS Bulletin 2011-008 (see ~~link above~~), and only test for 'required' or 'prohibited' compliance elements as follows:

- *Single Subdivision*<sup>66</sup> Programs test: none (no required or prohibited elements)<sup>63</sup>
  - *Pool Members* test: #2
  - *Pools* test: 1, 3
1. [Ohio Rev. Code § 2744.081(A)(4)] Are self-insurance fund costs recovered by appropriate charges to participating subdivisions based on the subdivisions' relative experience, loss exposure or as otherwise agreed by contract?
  2. [Ohio Rev. Code § 5705.13(A)(2)] Are there any reserves established on fund equity to provide for self-insurance costs?
  3. [Ohio Rev. Code § 2744.081(A)(1&3)] Was a report prepared by a member of the American Academy of Actuaries<sup>64</sup> within 90 days of year end listing where:
    - a. The actuary's opinion language (including the scope of the work):
      - i. Generally complied with the example described in the "Actuarial Opinions" section of AOS Bulletin 2001-005, and  
*Note: Consider whether any qualification in the actuary's report affects the financial statement opinion or indicates noncompliance with Ohio Rev. Code § 2744.081.*
      - ii. Indicated amounts reserved conform to accepted loss reserving standards.
    - b. The actuarial liability as of the last day of the fiscal year, and
    - c. Program disbursements, including claims paid, legal representation and consultant costs?

**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>66</sup> Ohio Rev. Code §§ 9.833 and 2744.01 define a political subdivision in part 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. According to 2017 Op. Att'y. Gen. No. 2017-001, a person authorized by a board of county commissioners or a board of township trustees to perform work related to the demolition of vacant or abandoned buildings and the remediation of other nuisance properties is considered an "employee" when acting within the scope of their employment even if not compensated for the work. As used in Ohio Rev. Code § 9.833, a "political subdivision" also includes the entity types described in Ohio Rev. Code § 3905.36. Ohio Rev. Code § 9.833 also says "County Board means a county board of developmental disabilities."

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

**1-18 (Previously 1-22) 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 Years of service</b>	<b>Vacation leave earned</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 Years of service</b>	<b>Minimum vacation leave earned</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.

#### **Families First Coronavirus Response Act (FFCRA) Leave:**

**Allowable period: Mandatory not later than 15 days after the date of the bill linked below (or) April 1, 2020 through December 31, 2020. Optionally, it may be extended through March 31, 2021. The American Rescue Plan Act (ARPA) further extended the tax credit from April 1, 2021 through September 30, 2021, though the ARPA credit will now apply against an employer's Medicare taxes rather than Social Security taxes. In addition, ARPA increased the maximum tax credits available and expanded the leave reasons eligible for the credit.**

#### **Link to guidelines:**

- **December mandate included in FFCRA:** <https://www.congress.gov/bill/116th-congress/house-bill/6201/text/enr>
- **March extension included in Consolidated Appropriations Act (CAA):** <https://www.congress.gov/bill/116th-congress/house-bill/133>
  - **See also Department of Labor FAQs for more information at** <https://www.dol.gov/agencies/whd/pandemic/ffcra-questions>
- **April 1, 2021 through September 30, 2021 extension included in American Rescue Plan Act (ARPA):** <https://www.congress.gov/bill/117th-congress/house-bill/1319/text>

**Summary: An employer shall provide to each employee paid sick time to the extent the employee is unable to work (or telework) from March 1 through December 31, 2020 or March 31, 2021 (if their policy indicates they chose to optionally extend based on the CAA which is linked above), and/or April 1, 2021 through September 30, 2021 because:**

- 1. The employee is subject to a Federal, State, or local quarantine or isolation order related to COVID-19;**
- 2. The employee has been advised by a health care provider to self-quarantine due to concerns related to COVID-19;**
- 3. The employee is experiencing COVID-19 symptoms and is seeking a medical diagnosis;**
- 4. The employee is caring for an individual subject to an order described in (1) or self-quarantine as described in (2);**
- 5. The employee is caring for a child whose school or place of care is closed (or child care provider is unavailable) for reasons related to COVID-19;**

6. The employee is experiencing any other substantially-similar condition specified by the Secretary of Health and Human Services, in consultation with the Secretaries of Labor and Treasury.
7. Employee is obtaining a COVID-19 vaccine;
8. Employee is recovering from an injury, disability, illness, or condition related to the COVID-19 vaccine; or
9. Employee is seeking or waiting on a diagnostic test or medical diagnosis for COVID-19.

Additionally, an employee qualifies for expanded family leave if the employee is caring for a child whose school or place of care is closed (or child care provider is unavailable) for reasons related to COVID-19.

**Duration of Leave/Calculation of Pay:**

For leave reasons (1), (2), (3), (7), (8), or (9): employees taking leave are entitled to pay at either their regular rate or the applicable minimum wage, whichever is higher, up to \$511 per day and \$5,110 in the aggregate (over a 2-week period).

For leave reasons (4) or (6): employees taking leave are entitled to pay at 2/3 their regular rate or 2/3 the applicable minimum wage, whichever is higher, up to \$200 per day and \$2,000 in the aggregate (over a 2-week period).

For leave reason (5): employees taking leave are entitled to pay at 2/3 their regular rate or 2/3 the applicable minimum wage, whichever is higher, up to \$200 per day and \$12,000 in the aggregate (over a 12-week period, including expanded family leave).

**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> <li>• Management’s communication of changes in laws and regulations to employees</li> </ul>		

**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.

**Families First Coronavirus Relief Act Leave Procedures:**

- 5. Inquire with management and document the procedures followed for granting and recording FFCRA leave.**
- 6. Review the calculations of employees' FFCRA leave credited / used, including appropriate leave requests. Determine whether the computations use the hours the FFCRA law allows. (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).**

**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.

**1-19 (Previously 1-23) Compliance Requirements:** Internal Revenue Code (I.R.C.) 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;  
**Note: Section 2 Division G of the Families First Coronavirus Response Act, Coronavirus Aid, Relief, Economic Security Act [<https://www.congress.gov/116/bills/hr6201/BILLS-116hr6201enr.pdf>], Coronavirus Aid, Relief, and Economic Security Act [<https://www.congress.gov/bill/116th-congress/house-bill/748/text>], Consolidated Appropriations Act [<https://www.congress.gov/116/bills/hr133/BILLS-116hr133enr.pdf>], Treasury IRS Guidance n-20-65 [<https://www.irs.gov/pub/irs-drop/n-20-65.pdf>], and Treasury IRS Guidance n-21-11 [<https://www.irs.gov/pub/irs-drop/n-21-11.pdf>] include authority for crediting certain paid leave costs against the tax obligations related to this statutes and/or deferring the tax obligations to future periods. The American Rescue Plan Act of 2021 (ARP) [[Text - H.R.1319 - 117th Congress \(2021-2022\): American Rescue Plan Act of 2021 | Congress.gov | Library of Congress](https://www.congress.gov/117/bills/hr1319/BILLS-117hr1319enr.pdf)], enacted March 11, 2021, amended and extended the tax credits (and the availability of advance payments of the tax credits) for paid sick and family leave for wages paid with respect to the period beginning April 1, 2021, and ending on September 30, 2021.**
  
- 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/NEC]<sup>67</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;  
**Note: The IRS has deemed that grants local governments provide to small businesses under the CARES Act Coronavirus Relief Fund are taxable. Refer to IRS COVID-19 FAQs at: <https://www.irs.gov/newsroom/cares-act-coronavirus-relief-fund-frequently-asked-questions>.**
  - § 1.6050E-1: Income tax refund reporting.
  
- Ohio Rev. Code § 5747.06 - Collection of Ohio income tax at source.
  
- Janus v. American Federation of State, County, and Municipal Employees, Council 31, No. 16-1466, 585 U.S. \_\_\_ (2018), 138 S.Ct. 2448; public employees cannot be forced to pay “fair share” fees to labor unions. [Effective June 27, 2018] See also -

<sup>67</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.

[https://www.supremecourt.gov/opinions/17pdf/16-1466\\_2b3j.pdf](https://www.supremecourt.gov/opinions/17pdf/16-1466_2b3j.pdf)

- 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 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.

**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.
  - **If the government applied the provisions in the Families First Coronavirus Response Act, Coronavirus, Aid, Relief, Economic Security Act, Treasury IRS Guidance n-20-65 as modified by Treasury IRS Guidance n-21-11, or the American Rescue Plan Act of 2021 determine if they properly credited the paid leave costs against the tax obligations and / or deferred the tax obligations to future periods.**
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>68</sup>. If so, determine the benefit amounts were reflected in the affected employees W-2. Review a representative number of W-2s that include these amounts, and verify a 1099 was not issued.
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 verify a W-2 was not issued,
  - 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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<sup>68</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.

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

**1-20 (Previously 1-24) Compliance Requirement:** Various ORC Sections – Definitions, rates of contributions etc.

- Ohio Rev. Code §§ 145.01, 145.03, 145.402, 145.47, 145.48, and Ohio Admin. Code 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, 3307.26, 3307.35, 3307.51, 3307.53, 3307.56, 3307.561 (This addition is a result of SB 42), 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 3309.51 and 3314.10<sup>69</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.)

**NOTE: Auditors should be alert for changes in the account classification for related costs as compared to prior years because payments to cover payroll or benefits expenses of public employees for those employees whose work duties that are substantially dedicated to mitigating or responding to the COVID-19 public health emergency may be charged to the ~~Coronavirus Relief Fund~~ and premium pay for those essential workers (as defined by the American Rescue Plan's Local Fiscal Recovery program) that regularly perform in-person work, interact with others at work, or physically handle items handled by others charged to the Local Fiscal Recovery Fund. Among other limitations under the American Rescue Plan Coronavirus State and Local Fiscal Recovery Funds, employees are not eligible for premium pay during periods they were teleworking. Additionally, elected officials should avoid voting on premium payments for themselves as this may constitute a violation of Ohio Ethics Laws. If AOS auditors find premium payments paid out to elected officials, they should consult with the Center for Audit Excellence and AOS Legal department for a determination of lawfulness and allowability under the Ethics Laws and federal program, respectively.**

[US Treasury Coronavirus Relief Fund FAQs](#) & [SLFRPFAQ.pdf \(treasury.gov\)](#).

**Summary of Requirement:** These sections require governments to enroll most of their employees<sup>70</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 computed on earnable (i.e. usually gross) salary, that is computed on gross

<sup>69</sup> The SERS board certifies to ODE amounts ODE is to withhold from community school foundation payments for pension costs.

<sup>70</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.



pay before deducting medical, dental, vision, and flexible spending (Ohio Rev. Code § 145.47, and Ohio Admin. Code 145-1-26).

Certain community school teaching employees are included in STRS and others are excluded. Ohio Rev. Code §§ 3307.01(B)(1) and 3314.10 include in STRS membership any person who is employed in the school as a teacher or faculty member.<sup>71</sup> The following are excluded under § 3307.01(B)(2)(b):

- The person is employed by a community school operator;
- The operator on or before February 1, 2016 was withholding and paying 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 February 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. Each teacher shall contribute a certain percent not greater than 14%, of the teacher's earned compensation. (Ohio Rev. Code § 3307.26(A)).

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 for employees of an operator withholding and paying social security taxes on or before February 1, 2016:

- 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;

OR

- 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 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.

#### **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.**

<sup>71</sup> "Faculty" means the teaching staff of a university, college, or school, including any academic administrators as defined in Ohio Rev. Code § 3307.01(P).

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 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.

<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 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.

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):**

**1-21 (Previously 1-25) Compliance Requirement:** Ohio Rev. Code §§ 1715.51-59, 517.15 and 759.36 – Permanent endowment funds.

**Summary of Requirements:** Accounting for gifts, endowments, and/or bequests with donor-restrictions.

**Uniform Prudent Management of Institutional Funds (UPMIFA)<sup>74</sup>  
Ohio Rev. Code §§ 1715.51--.59**

.53(C) Terms in a gift instrument designating a gift as an endowment, or a direction or authorization in the gift instrument to use only "income," "interest," "dividends," or "rents, issues, or profits" or "to preserve the principal intact," or words of similar import, ***create an endowment fund of permanent duration, unless other language in the gift instrument limits the duration or purpose of the fund***, and do not otherwise limit the authority under division (A) of this section to appropriate for expenditure or accumulate.

.55 indicates the restrictions on the permanent/non-spendable portion of the endowment may be released or modified if:

- A. The donor consents in a record<sup>75</sup>,
- B. Application of an institution, to an appropriate court, indicating the restriction has:
  - become impracticable or wasteful,
  - impairs the management or investment of the fund, or
  - a restriction, that if modified, will further the purposes of the fund.

**AND**

1. The institutional fund subject to the restriction has a total value of less than two hundred fifty thousand dollars;
2. More than ten years have elapsed since the fund was established;
3. The institution uses the property in a manner consistent with the charitable purposes expressed in the gift instrument.

***Exceptions to requiring donor or court approval:***

Ohio Rev. Code § 1715.53(D) The government may appropriate and spend not greater than 5% of the fair market value of an endowment fund (considered an “irrebuttable presumption of prudence”). Assuming:

- Fair market value is determined at least quarterly and averaged over a period of not less than 3 years (or period the fund has been in existence if less than 3 years) immediately preceding the year in which the appropriation for expenditure was made,
- An appropriation of greater than 5% is only unallowable for the portions that exceed 5%.

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<sup>74</sup> Under this act, a governmental organization that qualifies as an “institution” may manage and invest an institutional fund. [Ohio Rev. Code § 1715.52(E)(3)] The term “institution” includes, a governmental organization to the extent that it holds funds exclusively for a charitable purpose.” Ohio Rev. Code § 1715.51(B)(2).

If a particular governmental entity has statutory authority itself to hold and invest donations that it receives, it may do so. If a particular governmental entity does not have statutory authority itself to invest and hold moneys that it receives as donations, the moneys must be paid to the appropriate treasurer for deposit and investment.

<sup>75</sup> According to Ohio Rev. Code § 1715.51(H) “record” means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.

**Townships with a cemetery endowment fund – Ohio Rev. Code § 517.15** <sup>76</sup>

Dollars received into a Cemetery Fund under this section can be for a variety of purposes, as follows:

- (A) “Gifts, devises, or bequests received for the purpose of maintaining, improving, or beautifying township cemeteries;” (These dollars would be presented in a special revenue fund.)
- (B) “Charges added to the price regularly charged for burial lots for the purpose of maintaining, improving, or beautifying township cemeteries;” (These dollars may be presented in a permanent fund.)
- (C) “Contributions of money from the township general fund;” These dollars would most likely not be the foundation revenue of the fund. (These dollars would be presented in a special revenue 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;” (These dollars would be presented in a private purpose trust fund.)
- (E) “Individual gift, 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.” (These dollars would be presented in a private purpose trust fund.)

State statute allows this activity to be in one fund; however, maintaining separate funds may simplify financial reporting issues.

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.<sup>77</sup>

**Union Cemetery Districts – Ohio Rev. Code § 759.36**

The board of cemetery trustees may create a permanent endowment fund for the express purpose of keeping the cemetery clean and in good order and may:

- A. Add to the price regularly charged for lots a sum for that purpose;
- B. Receive gifts for that purpose;
- C. Enter into separate agreements with the purchasers of lots by which an agreed part of the purchase price shall constitute a permanent fund;
- D. Receive individual gifts for the fund, the income thereof to be used for the upkeep and care of lots.<sup>78</sup>

When any such funds are received or created, they shall be a permanent fund for such use and the income therefrom shall be used only for such purpose, and the principal sum shall be kept and invested ... **except that upon unanimous consent of the board of cemetery trustees, the board may use the principal of the fund if the board is unable to keep the cemetery clean and in good order using only the income from the fund.** See also section 1-4 Establishing funds and Permission to establish special funds.

<sup>76</sup> See also AOS Audit Bulletin 2011-004 & 2020-008. Bulletin 2020-008 simplified the reporting of fund balance classifications in the AOS regulatory cash basis financial statements and footnotes beginning with the December 31, 2020 FYE reporting.

<sup>77</sup> 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.

<sup>78</sup> AOS staff should consult with the AOS Legal Division for determination on whether the Board of Trustees has the authority to override individual requests.

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. Obtain supporting documentation for any material endowments (may include bequests, legal agreements, resolutions/ordinances, minutes, etc.). Dependent upon the supporting documentation available, the activity may be recorded in:
  - a. A Private Purpose Trust Fund: If documentation indicates all or some of the amount given is required to be used for the benefit of individuals, private organizations, or other governments (i.e. for the beautification of a particular burial lot);
  - b. A Permanent Fund: If documentation indicates there are legal restrictions to spend only the interest and not the principal **AND** the restrictions are for the benefit of the government or its citizenry.
  - c. A Special Revenue Fund: If documentation supports program level restrictions (i.e. ‘embellishment or care of the cemeteries grounds); or
  - d. The General Fund: If no evidence is available to support the above classifications **and** the board/council pass a resolution authorizing the transfer.<sup>79 80</sup>

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<sup>79</sup> The board minutes (from the time of bequest) can be, in some cases, considered as sufficient evidence of intent if nothing else is available; however, all efforts to obtain evidence should be exhausted before money is moved to the general funds.

<sup>80</sup> If a situation arises in which an entity does not pass a resolution, we will issue a comment to recommend that the entity take such action to ensure a legally sufficient transfer in accordance with the Ohio Rev. Code and GASB. An audit adjustment will not be made if no such resolution is made first.

**If an endowment fund is appropriately recorded, and the government wants to release or modify a portion of it:**

2. If more than 5% (as described in Ohio Rev. Code § 1715.53(D) above) of any of the “non-spendable” portions were released, spent, or otherwise modified during the period.
  - a. [Townships or Union Cemetery Districts] Determine if the Board of Trustees gave unanimous consent to use the fund principal as described above, and evaluate the supporting documentation retained as evidence of their inability to maintain, improve and beautify cemeteries using only the income from the fund.
  - b. [for all other entities]:
    - i. Review any applications/approvals from appropriate courts,
    - ii. Determine if limitations on time and/or totals were adhered to, and
    - iii. Determine if the uses are consistent with expressed purposes.

*Note:* Non-compliance with these UPMIFA may require audit reactions beyond non-compliance citations (i.e. opinion modifications, findings for recovery/adjustment, etc.) and 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):**



**1-22 (Previously 1-28) 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 Ohio Rev. Code § 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>81</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>81</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>• Ticker 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 allocates 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):**

**1-23 (Previously 1-29) Compliance Requirement:** Ohio Rev. Code §§ 507.09 and 505.24(C) - Allocating township trustee and fiscal officer compensation.

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

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>82</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. Att'y. 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. Att'y. Gen. No. 2004-036 requires trustees compensated on a per diem basis to establish administrative procedures to document the 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.

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<sup>82</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. Att'y. Gen. No. 2004-036. If a Township has a duly enacted policy defining what constitutes a "day" in compliance with 2004 Op. Att'y. 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.

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. Att'y. 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(C)). 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 can be found at: [Example Payroll Certification.pdf](#). 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 can be found at: [Example Payroll Certification.pdf](#). 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. 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.

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.

**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):**

**1-24 (Previously 1-30) 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>83</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>84</sup>

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>		

<sup>83</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>84</sup> 2008 Op. Att’y. 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.

For additional information see:

- Department of Agriculture's Redbook: [Fairs RedBook.pdf](#)
- Uniform System of Accounting for Agricultural Societies: [https://ohioauditor.gov/publications/docs/uniform\\_system\\_of\\_accounting\\_for\\_agricultural\\_societies\\_2020\\_revision.pdf](https://ohioauditor.gov/publications/docs/uniform_system_of_accounting_for_agricultural_societies_2020_revision.pdf)

### *Agricultural Society Compliance Supplement*

#### **Applicability: County and independent societies**

**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* 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 Cod. 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's budget resolution. Determining whether noncompliance exists requires judgment based on whether the Society intends its 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*).
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**

- 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, upon the presentation of a petition signed by not less than five hundred resident electors of the county, shall submit to the electors of the county whether or not county bonds shall be issued and sold to liquidate such indebtedness with a copy of such resolution to be certified to the county board of elections and such board of elections, within ten days after such certification. 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>85</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*.)

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<sup>85</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."

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:**

1. Inspect cash receipt records and minutes and determine if indebtedness exists.
2. 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.
3. 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.
4. For years in which the society owes debt service to the county, agree payments to the amortization schedule.
5. 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**

**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:**

1. 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.
2. 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.
3. Determine if the footnotes adequately describe any leases or other society obligations, amortization schedules, etc.
4. 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**

**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) Subject to section 1711.33 of the Revised Code, 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 annual payments for debt obligation incurred by a county agricultural society pursuant to this division (B) shall not exceed an amount equal to twenty-five percent of its prior three-year average of 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:**

1. By reading the permanent file, minutes, cash receipt records, other documents, and by inquiry, determine if any such indebtedness exists.
2. 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.



3. Loans and Credit<sup>86</sup>
  - a. 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.
  - b. Examine the society’s computation supporting that the annual payments for debt obligation from loans and credit does not exceed twenty-five percent of its prior three-year average of annual revenues.
4. 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.
5. 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.
6. For years in which the society owes debt service, agree payments to the amortization schedule.
7. 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):**

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<sup>86</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**

**Accounting Compliance Requirement:** Ohio Admin. Code 117-10-01 – Financial reporting and accounting for county agricultural societies and independent agricultural societies.

**Summary of Requirement:** Ohio Admin. Code 117-10-01 – 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 Appendix A of the *Uniform System of Accounting for Agricultural Societies*<sup>87</sup>. **Note:** You can view the latest version of this at [www.ohioauditor.gov](http://www.ohioauditor.gov), under *Resources/Publications*.

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:**

1. Compare the *Uniform System of Accounting for Agricultural Societies* requirements with the systems and records the society is using.
2. Determine if:
  - The required chart of accounts is used.
  - A cash journal, a receipts ledger, an expense ledger, and an investment ledger are used.
  - The prescribed formats for accounting and reporting information are used (including receipts, purchase orders, vouchers, checks, and bank reconciliations).

<sup>87</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.

**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 also test OCS requirements for:

- Deposits and investments in Chapter 2,
- Health care self-insurance and liability insurance in Chapter 1

Refer to OCS Implementation Guide Exhibit 5 for guidance on specific applicability.

**Applicability: County and independent societies**

**Compliance Requirement:** Ohio Rev. Code §§ 117.38, 1711.06, 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 this chapter 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 § 1711.06]

Every county agricultural society annually shall do all of the following:

- (A) Make a report of its proceedings during the year;
- (B) File a financial report, in accordance with section 117.38 of the Revised Code and forward it to the Director of Agriculture as provided for in section 1711.06.

[Ohio Rev. Code § 1711.05]

Cash-basis entities must file annual reports with the Auditor of State. The Auditor of State has prescribed a form for the report here - <http://www.ohioauditor.gov/references/shells/regulatory.html>. 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] See section ~~1-14~~ 4-17 for detail on filing requirements with the Auditor of State.

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 The Hinkle System, 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 annual report was filed with the Director of Agriculture.
4. Review documentation to determine the following reports were completed and distributed appropriately:
  - a. an abstract of the treasurer’s account was published in a newspaper of general circulation in the county.
  - b. a synopsis of its awards for improvement in agriculture and in household manufactures shall be forwarded to the Director of Agriculture and that it was sent before the annual meeting of directors of the society.

**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**

**Other Potentially Direct and Material Laws and Regulations:** Ohio Rev. Code §§ 3769.082 and 3769.086 – 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, twelve percent of the total 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 money 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 money 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 money are to be distributed, make application for participation in such to the director of agriculture on forms provided by the director.
- Distribution of money 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 money 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.

Ohio Rev. Code § 3769.086 says:

- (A) If a county agricultural society or independent agricultural society is unable to conduct races in accordance with section 3769.082 of the Revised Code because of unfavorable weather or another cause or if the number of horse races and stake races that are conducted by an agricultural society is fewer than the number that was scheduled to be conducted, the pro rata remainder of the money distributed from the Ohio fairs fund under division (A)(3) of section 3769.082 of the Revised Code for each horse race and stake race not conducted shall be returned to the director to be credited to the fund.
- (B) If a county agricultural society or independent agricultural society is unable to conduct an annual fair, the society shall return the money distributed by the director in accordance with division (A)(1) of section 3769.082 of the Revised Code. However, the society may keep such money if the society cancels the annual fair because of unfavorable weather or another cause, provided that the society still conducts live horse racing.
- (C) If the Ohio expositions commission is unable to conduct an annual fair, the commission shall return the money distributed by the director in accordance with division (A)(2) of section 3769.082 of the Revised Code. However, the commission may keep such money if the society cancels the annual fair because of unfavorable weather or another cause, provided that the commission still conducts live horse racing

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. 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.
2. 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.
3. As needed, and in accordance with Ohio Rev. Code § 3769.086, determine whether the society:
  - Returned money to the director, or
  - Met one of the exceptions allowing the society to keep the money.



**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 also test OCS requirements for:

- **Income tax in Chapter 1,**
- **Public Deposits in Chapter 2,**
- **Sunshine Laws in Chapter 2,**

Refer to OCS Implementation Guide Exhibit 5 for guidance on specific applicability.