SOUTHERN OHIO AGRICULTURAL AND COMMUNITY DEVELOPMENT FOUNDATION

REGULAR AUDIT

FOR THE YEAR ENDED JUNE 30, 2006

Auditor of State
Betty Montgomery

SOUTHERN OHIO AGRICULTURAL AND COMMUNITY DEVELOPMENT FOUNDATION

TABLE OF CONTENTS

This page intentionally left blank.

Auditor of State
Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT

Southern Ohio Agricultural and Community Development Foundation
100 South High Street
Hillsboro, Ohio 45133

We have audited the accompanying financial statements of the governmental activities and Special Revenue Fund of the Southern Ohio Agricultural and Community Development Foundation (the Foundation), State of Ohio, as of and for the year ended June 30, 2006, which collectively comprise the Foundation's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*. Those standards require that we plan and perform the audit to reasonably assure whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the Foundation's financial statements present the financial position and changes in financial position of only the Southern Ohio Agricultural and Community Development Foundation. They do not purport to, and do not, present fairly the financial position of the State of Ohio as of June 30, 2006, or the changes in its financial position and cash flows of its proprietary fund types for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and Special Revenue Fund of the Southern Ohio Agricultural and Community Development Foundation as of June 30, 2006, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2L, during the year ended June 30, 2006, the Foundation adopted the Governmental Accounting Standards Board's Statement No. 46, *Net Assets Restricted By Enabling Legislation.*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 3, 2006, on our consideration of the Southern Ohio Agricultural and Community Development Foundation's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grants, and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing in internal control over financial reporting and compliance and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards.* You should read it in conjunction with this report in assessing the results of our audit.

35 N. Fourth St. / Second Floor / Columbus, OH 43215
Telephone: (614) 466-3402 (800) 443-9275 Fax: (614) 728-7199
www.auditor.state.oh.us

Management's Discussion and Analysis is not a required part of the basic financial statements, but is supplementary information the accounting principles generally accepted in the United States of America requires. We have applied certain limited procedures, consisting principally of inquiries of management regarding the methods of measuring and presenting the required supplementary information. However, we did not audit the information and express no opinion in it.

Betty Montgomery

Betty Montgomery
Auditor of State

October 3, 2006

As management of the Southern Ohio Agricultural & Community Development Foundation (the Foundation), we are providing this overview of the Foundation's financial activities for the fiscal year ended June 30, 2006. Please read the overview in conjunction with the Foundation's basic financial statements, which follow.

The Foundation is included within the State of Ohio's Comprehensive Annual Financial Report as part of the primary government. The foundation uses a special revenue fund to report its financial position and results of operations. We believe these financial statements present all activities for which the Foundation is financially responsible.

FINANCIAL HIGHLIGHTS

Key financial highlights for fiscal year 2006 are as follows:

- The assets of the Foundation exceeded its liabilities at the close of the most recent fiscal year by $40.7 million (net assets). Of this amount, $40.4 million may be used in the Foundation's programs to reduce tobacco use and production.
- The Foundation's total net assets increased by $2.4 million during fiscal year 2006.
- The Foundation continued its grant programs and disbursed $11.2 million in grants to Southern Ohio farmers. Grants were awarded for 1) Educational Assistance; 2) Forage Improvement; 3) Forage Handling; 4) Grain Handling; 5) Livestock Systems; 6) Genetic Improvement; 7) Feeding Systems; 8) Economic Development; 9) Agricultural Expansion/ Diversification; and 10) Horticulture Projects.
- Interest earned totaled $1,227,277 during fiscal year 2006.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Foundation's basic financial statements. These basic financial statements are comprised of two components: 1) combined government-wide and fund financial statements, and 2) notes to the financial statements. For most governmental entities, the government-wide and fund financial statements are presented separately; however, since the Foundation is comprised of only one special revenue fund, we are presenting both types of financial statements on one combined set of financial statements, as described below:

- ***Governmental Fund Balance Sheet/Statement of Net Assets***

  The column labeled "Special Revenue Fund" presents information on the Foundations assets, liabilities, and fund balance using the modified-accrual basis of accounting. The fund is an accounting device that the State of Ohio uses to keep track of specific sources of funding and spending for particular purposes. The fund balance may serve as a useful measure of the Foundation's net resources available for spending at the end of the fiscal year.

  The column labeled "Statement of Net Assets" presents information on the Foundation's assets and liabilities, with the difference between the two reported as *net assets*. Such information is presented on the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Foundation is improving or deteriorating.

- ***Statement of Governmental Fund Revenues, Expenditures, and Changes in Fund Balance/Statement of Activities***

  The column labeled "Special Revenue Fund" presents information on near-term inflows, outflows, and balances of expendable resources. Such information is presented on the modified-accrual basis of accounting.

OVERVIEW OF THE FINANCIAL STATEMENTS (Continued)

The column labeled "Statement of Activities" presents information showing how the Foundation's net assets changed during the most recent fiscal year. Such information is presented on the accrual basis of accounting. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows.

Because the focus of fund financial statements is narrower than that of government-wide financial statements, it is useful to compare the information presented on a fund basis with similar information presented on a government-wide basis. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. The combined government-wide and fund financial statements include a reconciliation to facilitate this comparison (see column labeled "Adjustments").

FINANCIAL ANALYSIS OF THE FOUNDATION

The following is a summary of the Foundation's net assets as of June 30, 2006 compared to June 30, 2005.

Net Assets at June 30

	2006	2005	% Change
Assets			
Cash and Investments	$ 27,421,016	$ 23,098,903	18.71%
Interest Receivable	107,363	-	100.00%
Collateral on Lent Securities	18,400	275,774	-93.33%
Tobacco Settlement Receivables	13,150,375	15,205,619	-13.52%
Prepaid Assets	3,171	-	100.00%
Capital Assets	53,450	64,351	-16.94%
Other Assets	5,231	5,817	-10.07%
Total Assets	40,759,006	38,650,464	
Liabilities			
Accounts Payable	8,917	19,976	-55.36%
Wages Payable	22,375	21,122	5.93%
Obligations under Lent Securities	18,400	275,774	-93.33%
Compensated Absences Payable	58,183	56,849	2.35%
Total Liabilities	107,875	373,721	
Net Assets			
Invested in capital assets	53,450	64,351	-16.94%
Restricted for Indemnification Program	163,312	163,312	0.00%
Unrestricted Net Assets	40,434,369	38,049,080	6.27%
	$ 40,651,131	$ 38,276,743	

Collateral on Lent Securities and Obligations under Lend Securities directly relate to security lending activity on behalf of the Treasurer of the State of Ohio. The amount of securities out on loan at June 30, 2006 was significantly less than the amount out on loan at the end of the previous period resulting in the significant decreases in these two accounts.

The following is a summary of the Foundation's Statement of Activities for the year ending June 30, 2006 compared to the year ending June 30, 2005

Statement of Activity for the year ending June 30

	2006	2005	% Change
Revenues			
Tobacco Settlement Income received from the State of Ohio	$ 13,150,375	$ 15,205,619	-13.52%
Interest Income	1,227,277	845,499	45.15%
Other Income	-	45,000	100.00%
Total Revenues	14,377,652	16,096,118	
Expenses			
Salaries and Benefits	411,506	404,453	1.74%
Purchased Services	296,222	290,472	1.98%
Materials, Supplies and Other	70,976	65,955	7.61%
Depreciation	31,934	30,753	3.84%
Grants	11,192,626	10,277,798	8.90%
Total Expenses	12,003,264	11,069,431	
Change in Net Assets	2,374,388	5,026,687	-52.76%
Net Assets, Beginning of Year	38,276,743	33,250,056	
Net Assets, End of Year	$ 40,651,131	$ 38,276,743	

The Foundation's increase in Net Assets is the result of Tobacco Settlement Income received from the State of Ohio and Interest Income exceeding grant awards and administrative costs.

BUDGET VARIANCES

The majority of the Foundation's assets are maintained in unappropriated accounts requiring no budgetary monitoring or reporting. The remaining assets of the Foundation are maintained in two special revenue funds within the Central Accounting System (CAS), CAS Funds 5M9 and K87. Although appropriated, CAS Funds 5M9 and K87 are not major special revenue funds, and therefore, budgetary reporting is not required.

CAPITAL ASSETS

The following is a summary of the Foundation's net capital assets at the end of fiscal year 2006, compared to the end of fiscal year 2005:

	2006	2005
Vehicles	$ 29,347	$ 21,508
Equipment	16,398	27,434
Computer Software	7,705	15,409
Total Capital Assets, net	$ 53,450	$ 64,351

Total net capital assets for the Foundation decreased by $10,901 during fiscal year 2006. This is the amount by which current depreciation expense exceeded current year additions.

ECONOMIC FACTORS

The Southern Ohio Agricultural and Community Development Foundation continues to believe in its mission: "To help create and enhance economic opportunities for Ohio's burley tobacco farm families and their rural communities. Monies not used for administrative expenses and programs will be available for new programs as they are developed and are approved by the Board, or for investment."

For fiscal year 2006, the Foundation's Board has approved the following grant programs to burley tobacco farmers and rural communities in the 22 southern counties of Ohio:

- **Educational Assistance:** The SOACDF Educational Assistance Program assists tobacco farmers who have suffered the economic impact of reductions in quota in recent years. The funds are intended to help these individuals acquire skills to enter new or supplemental income-generating occupations, and to help put their dependents through college with financial support that can no longer be solely derived from the growing of tobacco. The educational assistance program is an investment in Appalachian Ohio that will pay dividends well into the future. Award recipients are to apply their assistance toward tuition and fees in-state or out-of-state accredited institutions of higher education, or to receive specialized training at non-accredited institutions approved by the Board of SOACDF. Students may participate in certificate programs or other training that will provide them with employment opportunities. For the 2006-07 academic year, the SOACDF Educational Assistance Program will provide up to $3,000 in educational assistance per person for eligible tobacco growers, their spouses and immediate family dependents. Quota Owners, their spouses and immediate family dependents may each receive up to $1,000. The actual amount awarded to an individual may not exceed the calculated need determined by the educational institution. The total assistance provided to any family may not exceed $10,000 per academic year. $2 million is approved for the Educational Assistance Program in fiscal year 2007.

- **Agricultural Diversification Program:** $4.9 million is approved for fiscal year 2007. Ohio burley tobacco growers completing requirements set forth by the Board and certified by FSA county office including a Business plan, completed tobacco history, cash flow projections that qualify as Quota Owner/Growers or Grower Tenants can apply for 50% cost share up to a maximum of $40,000 and qualified Quota Owners can apply for 50% cost share up to a maximum of $15,000. These projects must be agriculturally based and go through a competitive review & score process by a review committee. Agriculture Diversification Projects are designed to help those who voluntarily decide to transition away from their dependence on tobacco or replace lost income from tobacco.

- **General Agricultural Projects:** The Foundation, formed five years ago with monies from the Tobacco Master Settlement Agreement, is charged with helping to create and enhance economic opportunities for tobacco farm families and rural communities. $3 million is approved for fiscal year 2007 for agricultural projects. Projects available this fiscal year for burley tobacco farmers include: Livestock Systems, Feeding Systems, Forage Handling Equipment, Forage Improvement (Lime & Seeding), Production Livestock Genetic Improvement, Grain Handling and Horticulture. These grant awards are $1,000 and $2,000 and are meant to supplement lost income for a majority of the burley tobacco producers who do not opt to apply for the larger agricultural diversification grants. These grants will assist producers in making capital investments to achieve improved efficiencies for additional income over time.

- **Economic Development:** $4 million for approved Economic projects and $500,000 for R&D projects is approved for FY2007 fiscal year for the Economic Development program. This program is designed to assist in strategic investments in communities that are affected by the reduction in the demand for tobacco. The emphasis of SOACDF's Economic Development program is to provide up to a maximum of 35% of a total project cost for projects that will create, retain, or expand job opportunities for residents in the traditional burley tobacco producing counties of southern Ohio. Both public and private sector businesses are eligible to apply in order to achieve those means. In the nine major burley tobacco producing counties, dollars are budgeted for use within those counties for projects that meet guideline criteria. An extensive review process which includes county, regional and final Board approval must be met before dollars are awarded.

- **Investment:** The SOACDF Board adopted an investment policy in fiscal year 2003 and $10 million dollars was budgeted for investment that began in fiscal year 2004. The investment managers which were chosen by the Treasurer of State were put in place and an additional $2 million was added to the investment program. At the end of fiscal year 2006, approximately $19.5 million resides in the Foundation's investment portfolio, which is currently overseen by Hartland & Company Investment Consultants. It is the Boards intention to continue to look for funds that can be placed into the investment program in order to extend the life line of the Foundation.

- **Loan Program:** The SOACDF Board budgeted $1.5 million for a loan program in fiscal year 2007.

CONTACTING THE FOUNDATION'S FINANCIAL MANAGEMENT

This financial report is designed to provide an overview of the Foundation's finances and its accountability for the money it receives. If you have questions about this report or need additional financial information, contact Soundra Weaver, Fiscal Officer, Southern Ohio Agricultural & Community Development Foundation, 100 South High St., PO Box 47, Hillsboro, Ohio 45133.

This page intentionally left blank.

SOUTHERN OHIO AGRICULTURAL AND COMMUNITY DEVELOPMENT FOUNDATION

GOVERNMENTAL FUND BALANCE SHEET / STATEMENT OF NET ASSETS

As of June 30, 2006

	Special Revenue Fund	Adjustments (See Note 11)	Statement of Net Assets
Assets:			
Cash	$ 628,371	$ —	$ 628,371
Investments	26,792,645	—	26,792,645
Interest Receivable	107,363	—	107,363
Collateral on Lent Securities	18,400	—	18,400
Tobacco Settlement Receivable	13,150,375	—	13,150,375
Prepaid Assets	3,171	—	3,171
Capital Assets, net of accumulated depreciation	—	53,450	53,450
Amount on Deposit for Compensated Absences	5,231	—	5,231
Total Assets	40,705,556	53,450	40,759,006
Liabilities:			
Accounts Payable	8,917	—	8,917
Wages Payable	22,375	—	22,375
Obligations under Lent Securities	18,400	—	18,400
Compensated Absences:			
Due in one year	—	13,914	13,914
Due in more than one year	—	44,269	44,269
Total Liabilities	49,692	58,183	107,875
Fund Balance/Net Assets:			
Reserved for Compensated Absences	5,231	(5,231)	—
Reserved for Prepaid Assets	3,171	(3,171)	—
Reserved for Indemnification Payments	163,312	(163,312)	—
Fund Balance Reserved	40,484,150	(40,484,150)	—
Total Fund Balance	40,655,864	(40,655,864)	—
Total Liabilities and Fund Balance	$ 40,705,556		
Net Assets:			
Invested in capital assets, net of related debt		53,450	53,450
Restricted for Indemnification Program		163,312	163,312
Unrestricted Net Assets		40,434,369	40,434,369
Total Net Assets		$ 40,651,131	$ 40,651,131

The notes to the financial statements are an integral part of this statement.

SOUTHERN OHIO AGRICULTURAL AND COMMUNITY DEVELOPMENT FOUNDATION

STATEMENT OF GOVERNMENTAL FUND REVENUES, EXPENDITURES AND CHANGE IN FUND BALANCE / STATEMENT OF ACTIVITIES

For the Year Ended June 30, 2006

	Special Revenue Fund	Adjustments (See Note 11)	Statement of Activities
Revenues:			
Tobacco Settlement Income from the State of Ohio	$13,150,375	—	$13,150,375
Interest Income	1,227,277	—	1,227,277
Other	—	—	—
Total Revenues	14,377,652	—	14,377,652
Expenditures/Expenses:			
Current:			
Salaries and Benefits	410,172	1,334	411,506
Purchased Services	296,222	—	296,222
Materials, Supplies, and Other	70,976	—	70,976
Depreciation	—	31,934	31,934
Grants	11,192,626	—	11,192,626
Indemnification Project	—	—	—
Capital Outlay	21,033	(21,033)	—
Total Expenditures/Expenses	11,991,029	12,235	12,003,264
Excess of Revenues Over Expenditures	2,386,623	(2,386,623)	—
Change in Net Assets	—	2,374,388	2,374,388
Fund Balance/Net Assets:			
Beginning of the year	38,269,241	7,502	38,276,743
End of the year	$ 40,655,864	$ (4,733)	$ 40,651,131

The notes to the financial statements are an integral part of this statement.

1. DESCRIPTION OF THE REPORTING ENTITY

Introduction

The Southern Ohio Agricultural and Community Development Foundation (the Foundation) was created by amended Senate Bill No. 192, effective June 2000, to "...endeavor to replace the production of tobacco in southern Ohio with the production of other agricultural products and to mitigate the adverse economic impact of reduced tobacco production in the region by preparing, implementing, and keeping current a plan to develop means for tobacco growers to grow other agricultural products voluntarily..." The Bill further describes a variety of means by which the Foundation is to develop its plan and carry out its charge.

Pursuant to its legislative mandate, the Foundation's Board is created in Ohio Rev. Code Section 183.12 and is enabled through Ohio Rev. Code Sections 183.11 to 183.17, inclusive. The Foundation's Board is composed of twelve voting members and four nonvoting members as set forth in Section 183.12 of the Ohio Rev. Code. Voting members include six active farmers and two persons with community development experience, all from Ohio's major tobacco growing counties, and four state officials sitting ex officio.

Method of Operation

The Foundation shall make grants or loans to individuals, public agencies, or privately owned companies to carry out the plan. The Foundation shall also adopt rules under Chapter 119 of the Ohio Rev. Code regarding conflicts of interest in the making of grants or loans.

To carry out the duties of the Foundation, a separate endowment fund was created in the custody of the Treasurer of State, but not part of the State Treasury. The Foundation is the trustee of the endowment fund. Disbursements from the fund shall be paid by the Treasurer of State only upon instruments duly authorized by the Board of Trustees of the Foundation or its designee. No disbursements shall be used for the direct production costs of growing tobacco.

The endowment fund is responsible for covering administrative expenditures such as staff salaries, equipment purchases, rental payments and program expenses. As a result of the legislation defining the Foundation's employees as state employees, the State established an appropriation to provide payroll for the Foundation, which is reimbursed by the Foundation's endowment fund.

At the request of the Foundation, the Treasurer of State shall select and contract with one or more investment managers to invest all money credited to the fund that is not currently needed for carrying out the functions of the Foundation. The eligible list of investments, as well as limitations and other requirements shall be the same as for the Public Employees Retirement System under Section 145.11 of the Revised Code.

Reporting Entity

Within the State of Ohio's Comprehensive Annual Financial Report, the Southern Ohio Agricultural and Community Development Foundation is included as part of the primary government. The Foundation's management believes these financial statements present all activities for which the Foundation is financially responsible.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements of the Southern Ohio Agricultural and Community Development Foundation present the financial position and results of operations of the Foundation. The financial statements, as of June 30, 2006, and for the year then ended, conform with accounting principles generally accepted in the United States of America as applied to governments. The Governmental Accounting Standards Board (GASB) is the standard-setting body for establishing governmental accounting and financial reporting principles. The GASB's Codification of Governmental Accounting and Financial Reporting Standards (GASB Codification) documents these principles.

The Foundation follows GASB Statement No. 34 "Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments." Under GASB Statement No. 34 the financial statements include separate Statement of Net Assets and Statement of Activities columns reporting the financial activities using the accrual basis of accounting, in addition to the Special Revenue Fund column reporting the financial activities using the modified accrual basis of accounting. The Foundation's other significant accounting policies are as follows.

A. Fund Accounting

The foundation uses a special revenue fund to report its financial position and results of operations. The special revenue fund is an independent fiscal and accounting entity with a self-balancing set of accounts. The special revenue fund is established to account for the proceeds of specific revenue sources that are legally restricted to expenditure for specified purposes.

B. Measurement Focus and Basis of Presentation

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (e.g., revenues) and decreases (e.g., expenditures) in net current assets, and unreserved fund balance is a measure of available expendable resources. This measurement focus has been applied to the "Special Revenue Fund" columns on the accompanying financial statements.

The "Statement of Net Assets" and "Statement of Activities" columns on the accompanying financial statements have been prepared using the economic resources measurement focus. This is the same approach used in the preparation of proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. The financial statements therefore present an adjustment column to identify reconciling items to arrive at the "Statement of Net Assets" and the "Statement of Activities" columns.

C. Basis of Accounting

Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements. The "Special Revenue Fund" columns on the accompanying financial statements were prepared using the modified accrual basis of accounting. Under the modified accrual basis of accounting, the Foundation recognizes revenues when susceptible to accrual (i.e., when they are "measurable and available"). "Measurable" means the amount of the transaction is determinable, and "available" means the amount is collectible within the current period or soon enough thereafter to pay liabilities of the current period. The Foundation considers revenues as available when collected within 60 days after year-end.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Under the modified accrual basis, expenditures are recorded when related fund liabilities are incurred, which are recognized as expenditures when due. Significant revenue sources susceptible to accrual under the modified accrual basis of accounting may include master settlement agreement revenues received from the State of Ohio and interest income.

The "Statement of Net Assets" and the "Statement of Activities" columns on the accompanying financial statements were prepared using the accrual basis of accounting. Under the accrual basis of accounting, expenses are recorded at the time they are incurred and revenues are recognized when measurable.

D. Budgetary Data

The majority of the Foundation's assets are maintained in unappropriated accounts requiring no budgetary monitoring or reporting. The remaining assets of the Foundation are maintained in two special revenue funds within the Central Accounting System (CAS), CAS Funds 5M9 and K87. Although appropriated, CAS Funds 5M9 and K87 are not major special revenue funds, and therefore, budgetary reporting is not required.

E. Cash

Cash of the Foundation includes amounts held in a custodial account with the Treasurer of State, CAS Funds 5M9 and K87, and petty cash.

F. Investments

Investments of the Foundation are reported at fair value. Fair value is the amount at which an investment could be exchanged in a current transaction between willing parties other than in a forced or liquidation sale. If quoted market price is available for an investment, the fair value to be used is the total number of trading units of the instrument times the market price per unit.

Ohio Revised Code Section 183.16 restricts the types of investments the Foundation may purchase to those types of investments permitted for the public employees retirement system under section 145.11 of the Ohio Revised Code. All investments shall be subject to the same limitations and requirements as the retirement system under that section and Sections 145.112 and 145.113 of the Ohio Revised Code.

The Foundation invests in the State Treasury Asset Reserve of Ohio (STAR Ohio), whereby the deposits are pooled with other deposits and reinvested daily. STAR Ohio investments are considered short-term and are reported at cost, which approximates market values. The pooled deposits at STAR Ohio have the general characteristics of a demand deposit account whereby additional cash can be deposited at any time and can also be effectively withdrawn at any time, without prior notice or penalty. The Treasurer of State is the investment advisor and administrator of STAR Ohio, a statewide external investment pool authorized under Section 135.45, Ohio Revised Code.

G. Securities Lending Transactions

GASB Statement No. 28, *Accounting and Financial Reporting for Securities Lending Transaction*s, requires disclosure of assets and liabilities arising from securities lending transactions. The Foundation's investments with the State's cash and investment pool are subject to lending transactions by the Treasurer of State. In accordance with paragraph 9 of GASB Statement No. 28, the Foundation's recording of assets and liabilities for securities lending transactions is based on their share of the cash and investment pool, as of the balance sheet date, as calculated by the Office of Budget and Management.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

H. Capital Assets and Depreciation

It is the Foundation's policy to capitalize all assets with an initial cost of $1,000 or more. Capital assets are reported in the "Statement of Net Assets" column, but are not reported in the "Special Revenue Fund" column on the accompanying Governmental Fund Balance Sheet/Statement of Net Assets. All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year.

All reported capital assets of the Foundation are depreciated. Depreciation is computed using the straight-line method of depreciation over the applicable useful life of the asset and commences the year after the asset is purchased. The useful life for each asset category noted in Note 5 is 5 years.

I. Revenues and Receivables

Master Settlement Agreement Income

Master settlement agreement income received from the State of Ohio comprises the Foundation's primary source of revenue. These revenues are derived from the 1998 Tobacco Master Settlement Agreement (the Agreement) that was entered into by the State of Ohio, along with numerous other states, against major tobacco product manufacturers. The Agreement stipulates the conditions and calculations to be applied in order for each state to receive its annual allotments. Ohio Rev. Code Section 183.02 requires all payments received by the State to be deposited into the Treasurer of State's Tobacco Master Settlement Agreement Fund (Fund 087) and the payments and related interest are to be distributed by the Office of Budget and Management in accordance with the distribution schedule.

Payments are credited to the Tobacco Master Settlement Agreement Fund in accordance with the following schedule stipulated by Ohio Rev. Code Section 183.02 (C), and subsequently transferred, though not necessarily in the same fiscal year, to the Southern Ohio Agricultural and Community Development Fund (Fund K87).

Year	Percentage
2000 (First Payment Credited)	5.00%
2000 (Net Amount Credited)	8.73%
2001	8.12%
2002	9.18%
2003	8.91%
2004	7.84%
2005	7.79%
2006	7.76%
2007	17.39%
2008 through 2011	17.25%

For fiscal year 2002 and 2003, the anticipated transfer to the Foundation, pursuant to the above schedule, was not received. Instead, in accordance with amended Senate Bill 242, other tobacco settlement monies, which were designated specifically for an Indemnification Payment Program, were transferred to the Foundation. Ohio Rev. Code Section 183.02 (C)(2), as amended, provides that amounts due under the above payment schedule for 2002 and 2003, shall be transferred to the Foundation in fiscal years 2013 and 2014, respectively. The fiscal year 2006 transfer, totaling $13,150,375, was received in July of 2006 and has been reported as a Tobacco Settlement Receivable on the Statement of Net Assets.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

I. Revenues and Receivables (Continued)

Before fiscal year 2011 begins, the Foundation must report to the Governor and Legislature the progress the Foundation has made towards its goals and whether a need for additional funding still exists. At this point, the Governor and Legislature will decide whether funding to the Foundation will be continued. Funding estimates for receiving monies under the Master Tobacco Settlement Agreement were only projected through the year 2025; however, under the terms of the Agreement payments from the tobacco product manufacturers are to continue into perpetuity. Ohio Rev. Code Section 183.02 (K) further states that future year revenues from the Agreement are contingent upon sufficient proceeds being received to cover designated revenue set asides for the Education Facilities Trust and Endowment Funds.

Interest Income

The Foundation receives interest income from investments with STAR Ohio, Mellon Bank, MDL Capital Management Inc., Boyd Watterson, and Fifth Third, deposits in CAS Funds 5M9 and K87, and custodial deposits with the Treasurer of State. In fiscal year 2006, the Foundation earned $1,227,277 in interest income.

J. Expenditures and Accounts Payable

Administrative expenditures

Administrative expenditures include operating and overhead items such as salaries and benefits, equipment purchases, and other miscellaneous expenditures. Ohio Rev. Code Section 183.30 (B) requires no more than five percent of total expenditures within a fiscal year shall be for administrative purposes.

Administrative expenditures for fiscal year 2006 were $798,403. Although this amount exceeds the 5% limitation noted above, the Foundation obtained Controlling Board approval of a spending plan and a waiver of the 5% limitation pursuant to Ohio Rev. Code Section 183.30.

K. Compensated Absences

The State of Ohio, which governs employee leave benefits and policies, pays compensation to separated employees for sick, vacation, and personal leave balances accumulated during the employee's term of service. The Foundation's compensated absences liability is calculated and reported in accordance with the guidance set forth in the Governmental Accounting Standards Board (GASB) Statement No. 16, "Accounting for Compensated Absences."

L. Fund Balance/Net Assets

Fund balance will be reported as reserved for making grants or loans to qualifying individuals, public agencies, or privately owned companies and covering administrative expenditures of the Foundation. In accordance with GASB Statements 34 and 46, net assets will be reported as unrestricted, except for the amount restricted for indemnification payments.

M. Self-Insurance

The State of Ohio serves as the Foundation's primary government and is self-insured for claims covered under its traditional healthcare, vehicle liability, public fidelity blanket bonds, property losses, and tort liability insurance plans. Additionally, the State of Ohio participates in a public entity risk pool that covers liabilities associated with claims submitted to the Bureau of Workers' Compensation.

3. DEPOSITS AND INVESTMENTS

Deposits - At fiscal year end, the carrying amount of the Foundation's deposits was $628,371 and the bank balance was the same. Of the bank balance, $27,303 was held on deposit by the State of Ohio, $600,568 was maintained in a custodial account held by the Treasurer of State. In addition to these deposits, the Foundation maintained a petty cash account totaling $500.

Investments **-** At fiscal year end, the fair values of investments were as follows:

Investment Type	Total Fair Value
U.S. Government Obligations	$ 1,801,857
U.S. Government Agency Obligations	3,340,283
Corporate Bonds and Notes	3,797,195
Domestic Equity	9,853,968
Money Market Funds	411,339
STAR Ohio	7,588,003
Total Investments	$ 26,792,645

Custodial Credit Risk – Custodial credit risk is the risk that, in the event of a failure of a depository institution or counterparty to a transaction, the Foundation will be unable to recover the value of deposits, investments, or collateral securities in the possession of an outside party. At June 30, 2006, the Foundation's deposits and investments, including the collateral on lent securities, had no exposure to custodial credit risk. The Foundation does not have a policy to limit custodial credit risk.

Foreign Currency Risk – Foreign currency risk is the risk that changes in exchange rates between the U.S. Dollar and foreign currencies could adversely affect an investment's fair value. Pursuant to the Foundation's investment policy, investment managers are prohibited from purchasing foreign securities, with the exception of American Depository Receipts. The Foundation had no exposure to foreign currency risk at fiscal year end.

Credit Risk – Credit risk is the risk that an issuer or counterparty to an investment will be unable to fulfill its obligations. Pursuant to the Foundation's investment policy, domestic fixed income investment managers must adhere to the following guidelines: (1) mortgage-backed and asset-backed securities not issued by an agency of the Federal Government must be rated A or better by a Nationally Recognized Statistical Rating Organization (NRSRO); (2) the average quality rating of the fixed income portfolio shall be AA or better by a NRSRO; and (3) only corporate debt issues that hold a rating in one of the four highest classifications by a NRSRO may be purchased.

3. DEPOSITS AND INVESTMENTS (Continued)

The Foundation's exposure to credit risk is as follows:

Quality Rating	STAR Ohio	Corporate Bonds and Notes	Total
AAA	$ 7,588,003	$ 356,266	$ 7,944,269
AA	-	419,686	419,686
A	-	2,964,843	2,964,843
BBB	-	56,400	56,400
Total	$ 7,588,003	$ 3,797,195	$ 11,385,198
U.S. Govt. Obligations and Guaranteed Securities			4,455,034
Fixed Income Security Pools - No Rating Available			687,106
Money Market Funds - No Rating Available			411,339
			$ 16,938,677

Concentration of Credit Risk – Concentration of credit risk is the risk of inability to recover the value of deposits, investments, or collateral securities in the possession of an outside party caused by a lack of diversification. Investment managers are expected to maintain diversified portfolios by sector and issuer. Pursuant to the Foundation's investment policy, investment managers can invest no more than five percent of the total market value of the domestic equity portfolio in any single company and no more than five percent of the total market value of the fixed income portfolio in the securities of any one issuer, other than direct issues of the U.S. Treasury, U.S. Government Agencies or Instrumentalities including Mortgage Backed Securities and their derivative products. At June 30, 2006, the Foundation had no concentration of credit risk.

Interest Rate Risk – Interest rate risk is the risk that an interest rate change could adversely affect an investment's fair value. The Foundation does not have a policy to limit interest rate risk.

The reporting of effective duration in the table below quantifies, to the fullest extent possible, the interest rate risk of the Foundation's fixed income assets.

	Investment Maturities (in years)				Total
Investment Type	Less than 1	1-5	6-10	More than 10	Fair Value
U.S. Government Obligations	$ -	$ 1,412,548	$ 389,309	$ -	$ 1,801,857
U.S Government Agency Obligations	438,102	1,274,671	940,404	687,106	3,340,283
Corporate Bonds and Notes	853,139	1,921,773	933,095	89,188	3,797,195
STAR Ohio	7,588,003	-	-	-	7,588,003
Money Market Funds	411,339	-	-	-	411,339
Total Investments	$ 9,290,583	$ 4,608,992	$ 2,262,808	$ 776,294	$ 16,938,677

4. SECURITIES LENDING TRANSACTIONS

The Foundation, through the Treasurer of State's Investment Department participates in a securities lending program for securities included in the "Equity in State of Ohio common cash and investments" and STAR Ohio accounts. These lending programs, authorized under Sections 135.143, 135.45 and 135.47, Ohio Revised Code, are administered by custodial agent banks, whereby certain securities are transferred to independent broker-dealers (borrowers) in exchange for collateral. The State has minimized its exposure to credit risk due to borrower default by requiring the custodial agent to ensure that the lent securities are collateralized at no less than 102 percent of the market value at the time of the loan. Furthermore, at no point in time can the value of the collateral be less than 100 percent of the value of the underlying securities on loan.

For State funds, the lending agent may not lend more than 75 percent of the total average portfolio and not more than 15 percent can be lent to a single broker-dealer. For the STAR Ohio program, not more than 25 percent of the STAR Ohio investment pool may be lent at any one time, and not more than 10 percent of the investment pool may be subject to term loans in excess of one business day.

During the fiscal year, the State funds lending program lent U.S. government and agency obligations in exchange for collateral consisting of cash and/or U.S. government obligations. The State cannot sell securities received as collateral unless the borrower defaults. At June 30, 2006 the collateral the State had received for securities lent consisted entirely of cash, some of which had been temporarily invested in various securities. For State funds, the weighted average maturity of all loans was 1 day while the weighted maturity of collateral was 12.8 days. The STAR Ohio lending program had no lent securities at June 30, 2006.

For State funds, the securities lending agent shall indemnify the Treasurer of State for any losses resulting from either the default of the borrower or any violations of the securities lending policy. For the STAR Ohio program, the agent agrees to indemnify the Treasurer for losses resulting from the failure of the borrower to return the loaned securities in accordance with the terms of the loan agreement, provided, however, that the agent's obligation to indemnify the Treasurer shall be limited to an indemnification amount equal to the difference between the market value of the loaned securities on the date that such loaned securities should have been returned to the agent and the greater of (1) the cash collateral received from the borrower or (2) the value of investments of collateral. There were no recoveries during fiscal year 2006 due to prior-period losses.

For the State funds lending program, since the lender owes the borrower more than the borrower owes the lender, there is no credit risk to the lender as of June 30, 2006. The State's Office of Budget and Management allocates the State's pooled cash collateral to various funds within the State's Central Accounting System (CAS) based on cash balances at June 30, 2006. The Foundations Allocated Collateral on Lent Securities and related Allocated Obligations Under Securities Lending as of June 30, 2006, was $18,400.

5. CAPITAL ASSETS

A summary of capital asset activity during the fiscal year follows:

Asset Category	Beginning Balance	Additions	Deletions	Ending Balance
Equipment	$ 55,180	$ -	$ -	$ 55,180
Vehicles	65,966	21,033	(24,390)	62,609
Computer Software	38,523	-	-	38,523
Subtotal	159,669	21,033	(24,390)	156,312
Accumulated Depreciation	(95,318)	(31,934)	24,390	(102,862)
Net Capital Assets	$ 64,351	$ (10,901)	$ -	$ 53,450

6. COMPENSATED ABSENCES

For the purpose of calculating the compensated absences liability, vacation, personal, sick, and compensatory leaves only are considered. The current portion of the liability consists of the amount of compensated absences that is due to be paid within one year of the balance sheet date, as estimated by the State of Ohio's Office of Budget and Management by analyzing trend data from the previous three fiscal years.

Changes in compensated absences for the year ended June 30, 2006, are as follows:

Beginning Balance	Increase	Decrease	Ending Balance	Amount Due in One Year
$ 56,849	$ 47,989	$ (46,655)	$ 58,183	$ 13,914

7. DEFINED BENEFIT PENSION PLANS

All full-time employees participate in the Ohio Public Employees Retirement System (OPERS). OPERS administers three separate pension plans as described below:

1. The Traditional Plan (TP) – a cost-sharing multiple-employer defined benefit pension plan.

2. The Member-Directed Plan (MD) – a defined contribution plan in which the member invests both member and employer contributions (employer contributions vest over five years at 20% per year). Under the Member-Directed Plan members accumulate retirement assets equal to the value of member and (vested) employer contributions plus any investment earnings.

3. The Combined Plan (CO) – a cost-sharing multiple-employer defined benefit pension plan. Under the Combined Plan, OPERS invests employer contributions to provide a formula retirement benefit similar in nature to the Traditional Pension Plan benefit. Member contributions, the investment of which is self-directed by the members, accumulate retirement assets in a manner similar to the Member-Directed Plan.

OPERS provides retirement, disability, and survivor and death benefits and annual cost-of-living adjustments to members of the Traditional and Combined Pension Plans. Members of the Member-Directed Plan do not qualify for ancillary benefits.

Authority to establish and amend benefits is provided by state statute per Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report. Interested parties may obtain a copy by making a written request to 277 East Town Street, Columbus, Ohio 43215-4642 or by calling (614) 222-6701 or 1-800-222-PERS(7377).

The Ohio Revised Code provides statutory authority for employee and employer contributions. For 2005, member and employer contribution rates were consistent across all three plans. For fiscal year 2006, the contribution rate for Foundation employees was 8.5% (increased to 9% effective January 1, 2006) of covered payroll and the employer contribution rate was 13.31% (increased to 13.54% effective January 1, 2006) of covered payroll. The Foundation's required contributions to OPERS for the years ended June 30, 2006, 2005, and 2004 were $40,466, $40,338, and $37,846, respectively. The full amount has been contributed for each year.

8. OTHER POST-EMPLOYMENT BENEFITS

The Ohio Public Employees Retirement System (OPERS) administers three separate pension plans: The Traditional Plan (TP) – a cost-sharing multiple-employer defined benefit plan; the Member-Directed Plan (MD) – a defined contribution plan; and the Combined Plan (CO) – a cost-sharing multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan.

OPERS provides retirement, disability, survivor and post-retirement health care benefits to qualifying members of both the Traditional and the Combined Plans; however, health care benefits are not statutorily guaranteed. Members of the Member-Directed Plan do not qualify for ancillary benefits, including post-employment health care coverage.

In order to qualify for post-retirement health care coverage, age and service retirees must have 10 or more years of qualifying Ohio service credit. Health care coverage for disability recipients and primary survivor recipients is available. The health care coverage provided by the Retirement System is considered an Other Post-employment Benefit (OPEB) as described in GASB Statement No. 12.

A portion of each employer's contribution to OPERS is set aside for the funding of post-retirement health care. The Ohio Revised Code provides statutory authority for employer contributions. The 2006 employer contribution rate for state employers was 13.31% of covered payroll, of which 4% was used to fund health care for the year.

The assumptions and calculations below were based on the Retirement System's latest Actuarial Review performed as of December 31, 2004.

An entry age normal actuarial cost method of valuation is used in determining the present value of OPEB. The difference between assumed and actual experience (actuarial gains and losses) becomes part of unfunded actuarial accrued liability. All investments are carried at market. For actuarial valuation purposes, a smoothed market approach is used. Under this approach assets are adjusted to reflect 25% of unrealized market appreciation or depreciation on investment assets annually.

The investment assumption rate for 2004 was 8%. An annual increase of 4%, compounded annually, is the base portion of the individual pay increase assumption. This assumes no change in the number of active employees. Additionally, annual pay increases, over and above the 4% base increase, were assumed to range from .5% to 6.3%. Health care costs were assumed to increase at the projected wage inflation rate plus an additional factor ranging from 1% to 6% for the next 8 years. In subsequent years (9 and beyond) health care costs were assumed to increase at 4% (the projected wage inflation rate) annually.

OPEB's are advance-funded on an actuarially determined basis. At year-end 2005, the number of active contributing participants in the Traditional and Combined Plans totaled 376,109. The number of active contributing participants for both plans used in the December 31, 2004, actuarial valuation was 355,287. The contribution rates stated above are the actuarially determined contribution requirements for OPERS. The portion of the Foundation's 2006 contributions that were used to fund post-employment benefits were $12,160.

The amount of $10.8 billion represents the actuarial value of the OPERS' net assets available for OPEBs at December 31, 2004. The Actuarial Valuation as of December 31, 2004, reported the actuarially accrued liability and the unfunded actuarially accrued liability for OPEB, based on the actuarial cost method used, were $29.5 billion and $18.7 billion, respectively.

On September 9, 2004 the OPERS Retirement Board adopted a Health Care Preservation Plan (HCPP) with an effective date of January 1, 2007. The HCPP restructures OPERS' health care coverage to improve the financial solvency of the fund in response to skyrocketing health care costs.

8. OTHER POST-EMPLOYMENT BENEFITS (Continued)

Under the HCPP, retirees eligible for health care coverage will receive a graded monthly allocation based on their years of service at retirement. The Plan incorporates a cafeteria approach, offering a broad range of health care options that allow benefit recipients to use their monthly allocation to purchase health care coverage customized to meet their individual needs. If the monthly allocation exceeds the cost of the options selected, the excess is deposited into a Retiree Medical Account that can be used to fund future health care expenses.

9. LEASES

On July 1, 2003, the Foundation amended their lease agreement for office space. In addition, the Foundation entered into an operating lease agreement for a Pitney Bowes postage machine. Leased properties not having elements of ownership are classified as operating leases and likewise are recorded as expenditures when payable. For fiscal year 2006, total operating lease expenses for the office space and the postage machine were $24,624 and $3,288, respectively. The following schedule details future lease payments of the Foundation.

Term	Office Space	Postage Machine
Fiscal year 2007	24,624	3,288
Fiscal year 2008	25,353	3,288
Fiscal year 2009	25,353	2,466
Fiscal year 2010	26,136	-
Fiscal year 2011	26,136	-

According to the Foundation's amended lease agreement for office space, provided the Foundation is in compliance with the existing terms of the contract, the Foundation has the option to renew the lease for up to four successive and continuous terms of two years each upon the same terms and conditions except that the base rent during said renewal terms be as noted above.

10. CONTINGENCIES

As of June 30, 2006, the Foundation's management, in consultation with the Ohio Attorney General's Office, was unaware of any pending litigation which could result in a material unfavorable outcome requiring amounts to be reported or disclosed in the Foundation's financial statements.

11. EXPLANATION OF ADJUSTMENTS

The following is a detailed description of the amounts included in the "Adjustments" column of the accompanying financial statements:

Governmental Fund Balance Sheet/Statement of Net Assets

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the special revenue fund; however, capital assets are reported in the Statement of Net Assets column	$53,450

Long-term liabilities, such as accounts payable and compensated absences, are not due and payable in the current period and, therefore, are not reported in the special revenue fund. However, long-term liabilities are reported in the Statement of Net Assets column.

Compensated Absences	($58,183)

Statement of Revenues, Expenditures, and Change in Fund Balance/Statement of Activities

Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. No depreciation expense is recorded in the Governmental funds.

Capital Outlay	$21,033
Depreciation	($31,934)
	($10,901)

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the special revenue fund.

Compensated Absences	($1,334)
	($12,235)

INDEPENDENT ACCOUNTANTS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS REQUIRED BY *GOVERNMENT AUDITING STANDARDS*

Southern Ohio Agricultural and Community Development Foundation
100 South High Street
Hillsboro, Ohio 45133

We have audited the financial statements the governmental activities and Special Revenue Fund of the Southern Ohio Agricultural and Community Development Foundation (the Foundation), State of Ohio, as of and for the year ended June 30, 2006, which collectively comprise the Foundation's basic financial statements and have issued our report thereon dated October 3, 2006, wherein we noted the Foundation adopted GASB Statement No. 46. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Foundation's internal control over financial reporting to determine our auditing procedures in order to express our opinions on the financial statements and not to opine on the internal control over financial reporting. Our consideration of the internal control would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts material to the financial statements we audited may occur and not be timely detected by employees when performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider material weaknesses. In a separate letter to the Foundation's management dated October 3, 2006, we reported other matters involving internal control over financial reporting which we did not deem reportable conditions.

Compliance and Other Matters

As part of reasonably assuring whether the Foundation's financial statements are free of material misstatement, we tested its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could directly and materially effect the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express an opinion. The results of our tests disclosed no instances of noncompliance or other matters we must report under *Government Auditing Standards*.

We intended this report solely for the information and use of the Foundation's management and the Ohio General Assembly. It is not intended for anyone other than these specified parties.

Betty Montgomery

Betty Montgomery
Auditor of State

October 3, 2006

Auditor of State
Betty Montgomery

88 East Broad Street
P.O. Box 1140
Columbus, Ohio 43216-1140

Telephone 614-466-4514
800-282-0370

Facsimile 614-466-4490

SOUTHERN OHIO AGRICULTURAL AND COMMUNITY DEVELOPMENT FOUNDATION

FRANKLIN COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

CERTIFIED
NOVEMBER 16, 2006