There are signs of heightened fiscal stress in Ohio’s cities and counties, the latest FHI tool shows. Enhanced functionality allows for deeper analysis into our largest governments.
When we introduced the Financial Health Indicators tool in January, we hoped local officials would use the information to help make difficult and potentially unpopular budgetary decisions. We also hoped the indicators would educate taxpayers on a sometimes confusing topic.

On Aug. 27, an article in the *Newark Advocate*, proved that the tool was working as intended.

Reporter Kent Mallett reported that Licking County Auditor Mike Smith “was concerned by the amount of borrowing by the county commissioners and would consider rejecting additional borrowing in the next two years.” Smith cited the Financial Health Indicators as the reason for his concern.

While meeting with business leaders in Cleveland not long ago, the executives wanted to discuss more fully the indicators for communities in Northeast Ohio. We heard this elsewhere in Ohio, too.

We’ve made some improvements to the functionality of the FHI tool, changes that will allow for enhanced analysis by government leaders, taxpayers and reporters across the Buckeye State.

Our cities and counties touch the lives of millions of Ohioans. We need to do everything possible to help the officials responsible for operating those governments make prudent decisions. If we’re successful, fewer cities and counties will end up in fiscal emergency and the need for drastic changes to local governments will be greatly reduced.

Sincerely,

Dave Yost
Auditor of State
FINANCIAL HEALTH INDICATORS UPDATE

An overview

When Ohio Auditor of State Dave Yost unveiled a new tool called “Financial Health Indicators” in January to gauge the fiscal health of Ohio’s largest local governments, his objective was two-fold: Help local officials avoid a fiscal crisis by identifying potential problems in their fiscal health, and to elevate the discussion around local government financing and budgeting.

Less than a year later, the FHI are having their desired effect. According to news reports, officials in communities across the Buckeye State have discussed the tool during budget deliberations.

The first iteration of FHI allowed Ohioans to understand more about the finances of their counties and cities, such as whether their capital assets – heavy equipment, infrastructure, buildings, etc. – were nearing the point of replacement, whether the entity’s spending was outpacing the money coming in, and whether an unhealthy percentage of city spending was devoted to paying off debts. In all, there are up to 17 indicators for each city and county.

The FHI are based on financial data provided by cities and counties in their financial statements and provide a snapshot of a community’s fiscal health based on a historical analysis of entities that have been declared in fiscal distress. The indicators generate outlooks that are either “critical,” “cautionary” or “positive,” represented by the colors red, yellow and green.

“We were very satisfied with the effectiveness of the Financial Health Indicators, but we wanted to make the tool even more useful by increasing its analytical capabilities,” Auditor Yost explained.

When discussing the FHI across Ohio during the past year, Auditor Yost was frequently asked by business leaders, legislators and journalists for the data to be summarized by county and regionally. Associations representing cities and counties also asked for varying subsets of the data.

At Auditor Yost’s direction, new functionality was added to allow users – citizens, business leaders, associations and policymakers – to deepen their analysis. Now, users can compare cities based on their populations, their overall spending or by geography. Additionally, users can zero in on specific indicators to better understand statewide trends.

While they have responsibility for balancing the books, local governments cannot always control major funding streams they depend on, such as income tax revenues from local employers who may relocate or downsize, or policy changes made by state or federal officials that result in reduced funding for local governments.

A snapshot of 2016’s ‘fiscal physical’

The 2016 “Financial Health Indicators” indicate nine cities and one county are showing signs of financial stress for fiscal year 2016, with nearly two-thirds of Ohio’s county governments showing an increase in the number of “critical” or “cautionary” benchmarks.

For 2015, no counties triggered enough cautionary or critical indicators to suggest fiscal stress occurring. For 2016, Morgan County met the threshold for showing fiscal stress, based on historic trends. Three counties (Hocking, Jackson and Vinton) are showing early signs of fiscal stress and may be two to three years away from experiencing fiscal stress based on current conditions.

For 2016, the cities of Akron, Canton, East Cleveland, Fostoria, Girard, Lorain, Maple Heights, Norwood and Parma Heights met the threshold for showing fiscal stress. Six cities (Alliance, Martins Ferry, North College Hill, Upper Sandusky, Warren and Zanesville) are showing signs of stress and may be two to three years away from experiencing fiscal stress, based on their current financial data and trends.

Another way of looking at the data: According to data provided by county financial officers for 2016, the number of critical and cautionary indicators for 55 of the 88 counties (62.5%) increased between 2015 and 2016. Another 23 percent of counties (20 of 88) showed improvement, while fiscal stress for 10 counties, or 11 percent, was unchanged, and data for three counties were incomplete because of inconsistent accounting bases in financial
statement presentation. The financial stress on Ohio cities did not change significantly between 2015 and 2016. Data show 111 (45 percent) had more critical and cautionary outlook indicators, while 107 (43 percent) had a reduction in the number of those indicators. FHI for 21 cities were unchanged, and data for eight were incomplete.

While counties combined for 36 critical outlook indicators in 2015, they had 64 in 2016 – an increase of 78 percent. Cautionary indicators increased 38 percent for counties, from 132 to 182. Another way to look at it: While 70 of 88 counties had at least one cautionary or critical outlook in 2015, 78 had at least one cautionary or critical indicator in 2016 – an increase of 11 percent.

Cities combined for 301 critical FHI in 2016, up from 275 in 2015, for an increase of 9 percent. Cities collectively had 513 cautionary indicators in 2016, which was less than a 1 percent decrease from 518 the prior year. The number of cities with at least one critical or cautionary indicator grew 4 percent between 2015 and 2016, from 217 to 226.

There was a change regarding how pension liabilities are reported by the entities in 2016 that could have generated a false “negative” for some entities in Indicator 1 and possibly Indicators 3 and 13.

Taken as a whole, the FHI provide insights into what areas are causing the greatest challenges for both cities and counties. Among them:

- Capital assets and infrastructure (No. 11) for the age of and replacement of capital assets.
- Spending near or above annual revenues (Nos. 8 and 9).
- The available (unrestricted) balance of all government-type activity funds, the trend of that balance and the number of days of available funding (Nos. 1, 3 and 13).
- The available (unassigned) balance of the general fund, the trend of the general fund balance and number of days of available funding (Nos. 2, 4 and 14).
- Percentage of revenues used to pay debt (No. 12).

What history tells us

Staff from the Auditor of State’s office used historical data for entities that had been declared in fiscal distress to create the indicators. Using that data, the Auditor’s office developed a set of Financial Health Indicators to recognize early signs of fiscal stress for cities and counties.

The indicators – 17 for entities who report financial statements using the Generally Accepted Accounting Principles (GAAP) and 15 for those who use a cash basis or modified cash basis of accounting – are a collection of financial information, percentages and ratios gathered from annual financial statements filed by local governments with the Auditor’s office in addition to their audit reports. The indicators are useful in predicting both financial stability and stress.

Historical data indicate that entities with at least six “critical” indicators are in a state of fiscal stress. (For cities and counties using a cash or modified cash basis of accounting, four critical indicators is the threshold.) Historical data indicate that entities with a combination of eight critical and cautionary indicators may experience fiscal stress in two to three years. (For cities and counties using a cash or modified cash basis of accounting, a combination of six critical and cautionary indicators is the threshold.)

However, having a high number of indicators which suggest fiscal stress does not mean a community will fall into fiscal emergency, nor does it mean local officials have failed to properly manage their finances. It does mean, however, that barring a course correction, the finances of these entities are such that the community is at higher risk of being declared in fiscal distress by the Auditor in the future.

It is important to note that no individual financial indicator is of use in identifying overall fiscal stress or predicting that an entity will fail. While individual indicators do point to specific areas of concern, the indicators should be considered together to obtain an insight as to whether or not an entity is experiencing early signs of fiscal stress.

### How the indicators have changed

#### TOTAL CRITICAL INDICATORS

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#### TOTAL CAUTIONARY INDICATORS

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<tr>
<td>Cities</td>
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#### AT LEAST ONE CRITICAL OR CAUTIONARY INDICATOR

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FINANCIAL HEALTH INDICATORS UPDATE

A closer look

Increased search functionality

The enhancements for 2017 allow a user to look at the indicators in different ways. Go to ohioauditor.gov/fhi to do a search.

Selecting all cities in a county
Under the “entity type” tag, click on “city.” Under “County(s),” either type the name of the county(s) you’re interested in or follow the drop down window and click on the county(s) of interest. Click “search.” This allows for someone to look at cities or counties in a region.

Selecting specific cities or counties
Under the “City or County Name(s)” tab, click on all entities to compare and click “search.”

Comparing an entity for one or two years
The search results will default to two years. If you only want to review a single year’s FHI report, click the preferred year under the “Filing Year” tab.

Grouping by like size
The FHI tool now allows users to compare similarly sized cities or counties. Under the “search” button, a user can limit the results to those entities whose budgets fall within specific parameters or based on a population range. Under either tab, type in the ranges (population or budget) and click on “search.” The results can be sorted by any of the indicators or data points (population or budget).

Reviewing the details of an entity’s FHI report
Under the “City or County Name(s)” tab, click on the entity name for the report you are interested in and click “search.” On the results page, click on the “report” hyperlink on the right side of the entity’s report. To see the underlying data used to calculate the FHI, click on “data.”

Sorting by Indicator
Any search result can be sorted based on a specific Indicator. To sort by Indicator, click on the arrow next to the Indicator number. To sort by another Indicator, simply click on the arrow next to that Indicator.

Narrowing results to a single indicator
Under the “trend search” button on the home page, click on a specific indicator under the “Indicator Number” tab. To view all counties, click on “County” and search. To view all cities, click “City” and search. The results will default to two years. To narrow to one year only, click the tab for “Select Output Years” and modify to reflect the proper year.
Leaders of Ohio’s counties and cities have great responsibility for managing the financial affairs of their governments even though they do not always control key factors that drive their budgets.

In January 2017, Auditor of State Dave Yost released the Financial Health Indicators — a series of indexes that show how much fiscal stress a city or county is under — and updated the indicators with additional functionality in December 2017.

▶ UNDERSTANDING THE FHI
Each indicator (up to 17) shows whether a particular measure has a critical, cautionary or positive outlook, with the status designated by a color: red, yellow or green.

The more red and yellow indicators, the greater the stress on the entity’s financial health.

▶ HOW MANY ARE TOO MANY?
Historically, entities in fiscal distress (fiscal caution, watch or emergency) had at least six indicators with “critical outlook” or colored red. Those with a combination of at least eight “critical” and “cautionary” outlooks were two to three years from experiencing fiscal stress.

▶ WHAT THE FHI MEASURE
Each indicator is a reflection of different financial information. The indicators sometimes can be challenging because multiple data points are typically needed to illustrate what the indicator is measuring. For ease of understanding each indicator, it is best to begin by reading the description of the indicator and why it is important. Before analyzing the graphic, it is helpful to read the requirements of the “critical outlook” and “cautionary outlook” to understand what is being reflected in each indicator.

No single indicator should be interpreted to signal overall fiscal distress. The FHI should be considered as a group to determine an entity’s fiscal health. A single indicator can point to a trend or issue in a certain fiscal measurement, but an indicator could have been triggered to a critical outlook because officials decided, for example, to pay down debt and significantly reduce a fund balance. While a declining fund balance isn’t usually positive, paying off debt is a sound financial reason to do so.
FHI FREQUENCY
The FHI reports are generated via an automated reporting process twice for each reporting year. A preliminary FHI report is generated at the time the city or county submits its annual filing of its financial statements with the AOS. The preliminary report is based on the current year’s unaudited financial statement and the audited financial data from previous years. The final FHI report for each reporting year is generated when the audit has been completed for the reporting year.

PRELIMINARY vs. FINAL
It is important to note that an entity’s FHI may change between the initial filing and after the audit is completed. All entities must file their financial data by the end of May (specific date varies by year, and financial basis of reporting).

THE INDICATORS
Each indicator is explained in full detail at www.ohioauditor.gov/fhi. In short:

● Nos. 1 & 3
Identify when an entity has a zero, negative or declining balance in governmental type activities assets that are unrestricted. This applies to the balance at the end of a reporting year as well as a declining trend over multiple years. These are signs of fiscal stress because balances may not be available for unexpected expenses.

● Nos. 2 & 4
Identify when an entity has a zero, negative or declining unassigned General Fund balance at the end of the reporting year and/or a declining trend over multiple years. These are signs of fiscal stress because balances may not be available for unexpected expenses.

● No. 5
Identifies reserves available in the General Fund.

● No. 6
Reflects the percentage change from year to year for property tax revenue in the General Fund.

● No. 7
Reflects the percentage change from year to year for sales tax revenue for counties and income tax revenue for cities in the General Fund.

● No. 8
Provides an indication of operating deficits and the size of the operating deficit compared to the current year budget.

● No. 9
Determines if, on a government-wide basis, expenses are exceeding revenues.

● No. 10
Reflects reliance on intergovernmental revenues which are subject to state and federal budget cuts.

● No. 11
Identifies situations in which repair or replacement of the local government’s capital assets will be necessary. A high percentage indicates capital assets replacement is imminent and the entity may be delaying replacement of capital assets or significant repairs for cash flow purposes.

● No. 12
Identifies the percentage of the revenues used/needed for repayment of debt.

● Nos. 13-15
Represents how long balances could sustain the entity based on average daily expenses.

● No. 16
Is the ratio of total liabilities of governmental type activities divided by total net assets/position of GTA and indicates the percentage of every dollar of resources, available for providing public services, that is owed by the entity.

● No. 17
Identifies if an entity’s recent audit reports include budgetary non-compliance and/or unreconciled/unauditable financial records.

MORE INFORMATION
Go to www.ohioauditor.gov/fhi for more, including a report on each of Ohio’s 88 counties and 247 cities, as well as heat maps showing overall trends across Ohio and to use new tools to analyze city and county financial data.