



OHIO AIR QUALITY DEVELOPMENT AUTHORITY

REGULAR AUDIT

FOR THE YEAR ENDED DECEMBER 31, 2006



Mary Taylor, CPA
Auditor of State

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

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Mary Taylor, CPA

Auditor of State

INDEPENDENT ACCOUNTANTS' REPORT

Ohio Air Quality Development Authority
50 W. Broad Street, Suite 1718
Columbus, Ohio 43215

To the Authority:

We have audited the accompanying financial statements of the governmental activities and business-type activities of the Ohio Air Quality Development Authority (the Authority), a component unit of the State of Ohio, as of and for the year ended December 31, 2006, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Authority'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 our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the Authority's financial statements are intended to present the financial position and the changes in financial position and, where applicable, cash flows of only that portion of the governmental funds and business-type activities of the Authority that are attributable to the transactions of the Authority. They do not purport to, and do not, present fairly the financial position of the State of Ohio as of June 30, 2007 and the changes in its financial position or, where applicable, its cash flows 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 business-type activities of the Ohio Air Quality Development Authority as of December 31, 2006, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 13, 2007, on our consideration of the Ohio Air Quality Development Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements 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 of 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.

Management's discussion and analysis and the budgetary comparison information are not required parts of the financial statements, but are supplementary information 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 measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink that reads "Mary Taylor". The signature is written in a cursive, flowing style.

Mary Taylor, CPA
Auditor of State

November 13, 2007

OHIO AIR QUALITY DEVELOPMENT AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2006
(Unaudited)

This discussion and analysis section of the Ohio Air Quality Development Authority (OAQDA) annual financial report provides an overall review of OAQDA's financial activities for the year ended December 31, 2006. The intent of this discussion and analysis is to look at OAQDA's financial performance as a whole; readers should also review the financial statements and the notes to the basic financial statements to enhance their understanding of OAQDA's financial performance.

OAQDA is responsible for the administration of three programs: Facility Development and Financing; the Clean Air Resource Center; and, the Ohio Coal Development Office. Both the Facility Development and the Clean Air Resource Center are combined in the air quality development activity. Facility Development and Financing is a self-supporting activity which provides for the acquisition, construction, maintenance, repair, and operation of air quality projects within the State of Ohio. The Clean Air Resource Center provides assistance to small businesses as they comply with requirements of the Clean Air Act; it is supported through a transfer of funds from the Ohio Environmental Protection Agency. Those funds are from Title V air permit fees. The coal development activity is a State sponsored activity which provides funding for research and development projects to develop suitable uses for coal mined within the State. The aggregate of these two activities is reported as a discretely presented component unit in the State of Ohio's comprehensive annual financial report (CAFR). Funding for the coal development activity is provided through the proceeds of general obligation bonds of the State of Ohio. These bonds, and annual debt service payments required to retire these bonds, are reported by the State of Ohio and therefore not included within the financial statements of OAQDA's coal development activity.

Financial Highlights

Key financial highlights for the year ended December 31, 2006 are as follows:

- Total net assets of OAQDA decreased by \$2.6 million in 2006 due to the utilization of bond proceeds provided in a prior year to fund grant programs and projects in the coal development activity. During 2006 the air quality activity continued to show strong revenues associated with bond issues while operating costs remain lower than revenues reported.
- The Coal Development activity received \$13.0 million in State assistance revenue in 2004 to finance research and development projects related to more effective and efficient uses for Ohio coal. During 2005 and 2006, grant payments of \$6.1 million and \$3.7 million, respectively, have been made to various programs and projects. Another \$9.4 million in program and projects have been approved and funding will occur as cash is needed.
- During 2006 the Air Quality Development activity report total program revenues of \$1.5 million, which is \$400,000 less than the program revenue reported for 2005. As fee revenues from the issuance of bonds is directly related to the number of bonds issued during the year as well as the dollar amount of the various bond issues, it is expected that revenues will vary from year to year.

Using this Annual Financial Report

This annual report consists of a series of financial statements and notes to those statements. These statements are organized so the reader can understand the OAQDA as a financial whole. The statements then proceed to provide an increasingly detailed look at specific financial activities.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2006
(Unaudited)

The Statement of Net Assets and Statement of Activities provide information about the activities of OAQDA as a whole, presenting both an aggregated view of OAQDA's finances and a longer-term view of those statements. Fund financial statements provide the next level of detail. For the governmental fund, these financial statements tell how services were financed in the short-term as well as the amount of funds available for future spending.

Reporting OAQDA as a Whole

Statement of Net Assets and the Statement of Activities

The statements of net assets and activities look at OAQDA as a whole, including all financial transactions, and answer the question, "How did we do financially during 2006?" These statements include all assets and liabilities using the accrual basis of accounting similar to the accounting used by most private-sector companies. All current year revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report OAQDA's net assets and changes in those assets. This change informs the reader whether OAQDA's financial position, as a whole, has improved or diminished. In evaluating the overall financial health, the reader of these financial statements should take into account non-financial factors that also impact the OAQDA's financial well being.

In the Statement of Net Assets and the Statement of Activities, the financial information of the OAQDA is divided into two kinds of activities:

- Governmental Activity – The financial activity of the coal development activity is reported as a governmental activity since the funding for this activity is provided by the State of Ohio.
- Business-Type Activities – The financial activity of the air quality development activity is reported as an enterprise fund as the intent of the program is to recoup operational costs through the user fees.

Reporting OAQDA's Funds

Fund Financial Statements

The activities of OAQDA are reported in two separate funds, one governmental fund and one enterprise fund, which are described in more detail below:

Governmental Fund

The coal development activity is reported as a governmental fund, which focuses on how money flows into and out of those funds and the balances left at year-end available for spending in future periods. These funds are reported using an accounting method called modified accrual, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the coal development activity. The relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is reconciled in the financial statements, however since the coal development activity has no long term assets or liabilities, no such reconciliation is necessary.

Proprietary Fund

Since the air quality development activity charges its clients for the services it provides, with the intent of recouping operating costs, this activity is reported as an enterprise fund. Enterprise funds use the same basis of accounting as business-type activities; therefore, these statements will essentially match.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2006
(Unaudited)

The OAQDA as a Whole

Recall that the Statement of Net Assets provides the perspective of the OAQDA as a whole. In the case of the OAQDA, assets exceeded liabilities by a total of \$11.2 million at December 31, 2006.

Table 1 provides a summary of the OAQDA's net assets for 2006 compared to 2005:

TABLE 1
NET ASSETS (in 000s)

	Governmental Activities		Business-Type Activities		Total	
		Restated		Restated		Restated
	2006	2005	2006	2005	2006	2005
<i>Assets:</i>						
Current and Other Assets	\$ 4,177	\$ 8,222	\$ 7,234	\$ 6,447	\$ 11,411	\$ 14,669
Capital Assets, Net	-	-	19	18	19	18
Total Assets	<u>4,177</u>	<u>8,222</u>	<u>7,253</u>	<u>6,465</u>	<u>11,430</u>	<u>14,687</u>
<i>Liabilities</i>						
Current and Other Liabilities	<u>47</u>	<u>801</u>	<u>142</u>	<u>82</u>	<u>189</u>	<u>883</u>
Total Liabilities	<u>47</u>	<u>801</u>	<u>142</u>	<u>82</u>	<u>189</u>	<u>883</u>
<i>Net Assets:</i>						
Invested in Capital Assets	-	-	19	18	19	18
<i>Restricted:</i>						
Coal Research & Development	4,130	7,421	-	-	4,130	7,421
Unrestricted	<u>-</u>	<u>-</u>	<u>7,092</u>	<u>6,365</u>	<u>7,092</u>	<u>6,365</u>
Net Assets	<u>\$ 4,130</u>	<u>\$ 7,421</u>	<u>\$ 7,111</u>	<u>\$ 6,383</u>	<u>\$ 11,241</u>	<u>\$ 13,804</u>

As displayed in Table 1, the OAQDA reported \$11.2 million in total net assets at December 31, 2006 compared with the \$13.8 million reported for the prior year. Of the \$11.2 million of net assets, \$4.1 million was attributed to State of Ohio financed coal development grant programs and the remaining \$7.1 million is reported in conjunction with the Air Quality Development activity. The decrease in net assets of the Coal Development – governmental activity – is due to the OAQDA paying on approved grant projects during the year. The financing for these grant projects was provided in a previous fiscal year by the State of Ohio issuing general obligation debt. Debt is issued as needed and therefore the cash balance and net assets associated with the Coal Development Grant funds will fluctuate as grant payments are made or bonds are issued. The increase in the Air Quality Development net assets was due to revenues, primarily fees issued in conjunction with bond issuance, exceeding expenses for 2006.

Current assets of the OAQDA decreased by \$3.3 million due the decrease in the cash on hand for the Coal Development activity as noted above. Current and other liabilities decreased by \$694,000 from those reported for the prior year as OAQDA recognized several large grants payable amounts at December 31, 2005 related to research projects but the amounts owed at December 31, 2006 was significantly lower. While the Coal Development activity reports \$4.2 million of current assets, approved grant obligations total \$9.4 million. The State of Ohio will provide the funding for these projects when cash is needed for payment as opposed to when the obligation is made.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2006
(Unaudited)

Table 2 shows the changes in net assets for the years ended December 31, 2006 and 2005.

TABLE 2
CHANGE IN NET ASSETS (in 000s)

	Governmental Activities		Business-Type Activities		Total	
	Restated		Restated		Restated	
	2006	2005	2006	2005	2006	2005
<i>Program Revenue:</i>						
Charges for services	\$ -	\$ -	\$ 1,025	\$ 1,421	\$ 1,025	\$ 1,421
Operating grants	552	612	503	524	1,055	1,136
<i>General Revenue:</i>						
Investment earnings	426	328	140	69	566	397
Miscellaneous	-	-	41	3	41	3
Total Revenue	<u>978</u>	<u>940</u>	<u>1,709</u>	<u>2,017</u>	<u>2,687</u>	<u>2,957</u>
<i>Program Expenses:</i>						
Community and economic development	4,269	6,598	-	-	4,269	6,598
Air quality development	-	-	980	679	980	679
Total Program Expenses	<u>4,269</u>	<u>6,598</u>	<u>980</u>	<u>679</u>	<u>5,249</u>	<u>7,277</u>
Increase (Decrease) in Net Assets	<u>\$ (3,291)</u>	<u>\$ (5,658)</u>	<u>\$ 729</u>	<u>\$ 1,338</u>	<u>\$ (2,562)</u>	<u>\$ (4,320)</u>

The Air Quality Development activity collects administrative fees when it issues revenue bonds; those fees are intended to cover administrative expenses over the life of each bond issue and are based upon the size of the issue. During 2006, the revenue from the administrative fees decreased by \$396,000 due to the timing associated when the revenue bonds were issued and the size of the bonds issued during the year. Operating grants are provided by the Ohio EPA for the Small Business Assistance and Ombudsman programs based on a fee imposed by the Ohio EPA. The amount of grant funding OAQDA receives correlates to the amount collected by the Ohio EPA. The intergovernmental revenue received from the Ohio EPA decreased \$21,000 in 2006 compared with the amounts received in 2005.

The Coal Development activity continues to fund research and development projects throughout the State of Ohio. To finance these projects, the State of Ohio issues general obligation bonds and passes the proceeds thru to OAQDA to administer the programs. As the general obligation bonds and the subsequent debt service requirements on those bonds are direct obligations of the State of Ohio, not OAQDA, the outstanding debt and debt service payments are reported in the financial statements of the State of Ohio, not within these financial statements. In 2004, the State of Ohio provided \$13 million to finance research and development projects. During 2005 and 2006, the OAQDA made grant payments totaling approximately \$6.1 million and \$3.7 million, respectively, to the various programs and projects. At December 31, 2006 there was another \$9.4 million of approved projects with committed funds. The State of Ohio will provide additional funds when cash is needed to pay on these projects, not when the project is approved.

Operating costs of the Air Quality Development activity reported for 2006 increased by approximately \$301,000 when compared with the prior year. In 2006 there were additional research monies paid to various institutions, increased professional service fees and the purchase of pension service credit for a retiring employee, all these contributed to the increased expense amount reported for 2006.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2006
(Unaudited)

Capital Assets

At December 31, 2006, the OAQDA had a total of \$85,033 invested in capital assets less accumulated depreciation of \$66,395 resulting in total capital assets, net of accumulated depreciation of \$18,638.

During the year ended December 31, 2006 the OAQDA purchased several pieces of office equipment and furniture which totaled \$5,061. Additional information on the OAQDA's capital assets can be found in Note 9 to the basic financial statements.

Contacting the OAQDA

This financial report is designed to provide Ohio citizens and our customers and clients with a general overview of OAQDA's finances and to demonstrate OAQDA's accountability for the money it receives. If you have questions about this report or need additional financial information contact the Ohio Air Quality Development Authority at 50 West Broad Street, Suite 1718, Columbus, Ohio 43215.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY
STATEMENT OF NET ASSETS
DECEMBER 31, 2006

	<u>Governmental Activity</u>	<u>Business-Type Activity</u>	<u>Total</u>
Assets:			
Cash and cash equivalents	\$ 4,162,968	\$ 7,087,101	\$ 11,250,069
Receivables:			
Accounts	-	121,000	121,000
Intergovernmental	34,603	-	34,603
Internal balances	(23,111)	23,111	-
Prepaid items	2,266	3,670	5,936
Capital assets, net of accumulated depreciation	<u>-</u>	<u>18,638</u>	<u>18,638</u>
 Total Assets	 <u>4,176,726</u>	 <u>7,253,520</u>	 <u>11,430,246</u>
Liabilities:			
Accounts payable	208	45,008	45,216
Grants payable	35,274	4,586	39,860
Accrued wages and benefits	11,506	17,953	29,459
Accrued retirement incentive	-	72,324	72,324
Intergovernmental payable	<u>-</u>	<u>2,306</u>	<u>2,306</u>
 Total Liabilities	 <u>46,988</u>	 <u>142,177</u>	 <u>189,165</u>
Net Assets:			
Invested in capital assets	-	18,638	18,638
Restricted for:			
Coal research and development programs	4,129,738	-	4,129,738
Unrestricted	<u>-</u>	<u>7,092,705</u>	<u>7,092,705</u>
 Total Net Assets	 <u>\$ 4,129,738</u>	 <u>\$ 7,111,343</u>	 <u>\$ 11,241,081</u>

See accompanying notes to the basic financial statements.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2006

	<u>Program Revenues</u>			<u>Net (Expense) Revenue and Changes in Net Assets</u>		
	<u>Expenses</u>	<u>Charges for services</u>	<u>Operating Grants</u>	<u>Governmental Activity</u>	<u>Business-Type Activity</u>	<u>Total</u>
Governmental Activity:						
Community and economic development	<u>\$ 4,268,853</u>	<u>\$ -</u>	<u>\$ 551,593</u>	<u>\$ (3,717,260)</u>		<u>\$ (3,717,260)</u>
Business-Type Activity:						
Air quality development	<u>980,376</u>	<u>1,025,077</u>	<u>502,556</u>		<u>547,257</u>	<u>547,257</u>
Total	<u>\$ 5,249,229</u>	<u>\$ 1,025,077</u>	<u>\$ 1,054,149</u>	<u>(3,717,260)</u>	<u>547,257</u>	<u>(3,170,003)</u>
General Revenues:						
Investment earnings				426,272	140,347	566,619
Miscellaneous				<u>-</u>	<u>41,049</u>	<u>41,049</u>
Total General Revenues				<u>426,272</u>	<u>181,396</u>	<u>607,668</u>
Changes in net assets				(3,290,988)	728,653	(2,562,335)
Net assets at beginning of year - Restated				<u>7,420,726</u>	<u>6,382,690</u>	<u>13,803,416</u>
Net assets at end of year				<u>\$ 4,129,738</u>	<u>\$ 7,111,343</u>	<u>\$ 11,241,081</u>

See accompanying notes to the basic financial statements.

**OHIO AIR QUALITY DEVELOPMENT AUTHORITY
BALANCE SHEET - GOVERNMENTAL FUND
DECEMBER 31, 2006**

	<u>Coal Development</u>
Assets:	
Cash and cash equivalents	\$ 4,162,968
Intergovernmental receivable	34,603
Prepaid items	<u>2,266</u>
Total Assets	<u>\$ 4,199,837</u>
Liabilities:	
Accounts payable	\$ 208
Grants payable	35,274
Accrued wages and benefits	11,506
Due to other funds	<u>23,111</u>
Total Liabilities	<u>70,099</u>
Fund Balances:	
Reserved for encumbrances	9,423,137
Unreserved	<u>(5,293,399)</u>
Total Fund Balance	<u>4,129,738</u>
Total Liabilities and Fund Balance	<u>\$ 4,199,837</u>

See accompanying notes to the basic financial statements.

**OHIO AIR QUALITY DEVELOPMENT AUTHORITY
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - GOVERNMENTAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Coal Development
Revenues:	
State assistance	\$ 551,593
Investment earnings	426,272
Total revenues	977,865
Expenditures:	
Current:	
Community and economic development:	
Salaries and employee benefits	283,685
Professional fees	55,742
Travel	4,069
Research	85,224
Coal development grants	3,734,303
Office supplies and other administrative expenditures	71,310
Rental payments	34,520
Total expenditures	4,268,853
Change in fund balance	(3,290,988)
Fund balances, January 1, 2006 - Restated	7,420,726
Fund balances, December 31, 2006	\$ 4,129,738

See accompanying notes to the basic financial statements.

**OHIO AIR QUALITY DEVELOPMENT AUTHORITY
STATEMENT OF NET ASSETS - ENTERPRISE FUND
DECEMBER 31, 2006**

	<u>Air Quality Development</u>
Assets:	
Current Assets:	
Cash and cash equivalents	\$ 7,087,101
Accounts receivable	121,000
Due from other funds	23,111
Prepaid items	3,670
Noncurrent Assets:	
Capital assets, net of accumulated depreciation	<u>18,638</u>
 Total Assets	 <u>7,253,520</u>
 Liabilities:	
Current Liabilities:	
Accounts payable	45,008
Grant payable	4,586
Accrued wages and benefits	17,953
Accrued retirement incentive	72,324
Intergovernmental payable	<u>2,306</u>
 Total Liabilities	 <u>142,177</u>
 Net Assets:	
Invested in capital assets	18,638
Unrestricted	<u>7,092,705</u>
 Total Net Assets:	 <u><u>\$ 7,111,343</u></u>

See accompanying notes to the basic financial statements.

**OHIO AIR QUALITY DEVELOPMENT AUTHORITY
STATEMENT OF REVENUES, EXPENSES AND CHANGES
IN NET ASSETS - ENTERPRISE FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Air Quality Development
Operating Revenues:	
Project administration fees	\$ 1,025,077
Small business ombudsman fees	289,130
Small business assistance program fees	213,426
Investment earnings	140,347
Miscellaneous	41,049
 Total operating revenues	 1,709,029
 Operating Expenses:	
Salaries and employee benefits	448,874
Professional fees	197,145
Travel	23,388
Research	132,117
State assistance	31,358
Office supplies and other administrative expenses	99,994
Depreciation	4,679
Rental expense	42,759
Miscellaneous expense	62
 Total operating expenses	 980,376
 Change in net assets	 728,653
 Net assets, January 1, 2006 - Restated	 6,382,690
 Net assets, December 31, 2006	 \$ 7,111,343

See accompanying notes to the basic financial statements.

**OHIO AIR QUALITY DEVELOPMENT AUTHORITY
STATEMENT OF CASH FLOWS - ENTERPRISE FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Air Quality Development
Cash flows from operating activities:	
Receipts from customers	\$ 1,066,126
Cash received from OEPA	502,556
Interest received	140,347
Payments to suppliers and vendors	(523,294)
Payments to employees	(376,176)
Net cash provided by operating activities	809,559
Net cash flows from capital and related financing activities:	
Purchase of capital assets	(5,061)
Net cash used by capital and related financing activities	(5,061)
Net increase in cash and cash equivalents	804,498
Cash and cash equivalents - beginning of year	6,282,603
Cash and cash equivalents - end of year	\$ 7,087,101
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 728,653
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	4,679
Decrease in due from other funds	14,554
Decrease in prepaid expense	1,230
Decrease in accounts payable	(17,364)
Increase in grants payable	4,586
Increase in wages and benefits payable	374
Increase in accrued retirement incentive payable	72,324
Increase in intergovernmental payable	523
Net cash provided by operating activities	\$ 809,559

See accompanying notes to the basic financial statements.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements

For the Year Ended December 31, 2006

1. GENERAL INFORMATION

Introduction

The Ohio Air Quality Development Authority (the Authority) was created by amended House Bill No. 963, effective June 1, 1970, to provide for the conservation of air as a natural resource of the State and to prevent or abate the pollution thereof, to provide for the comfort, health, safety, and general welfare of all employees, as well as other inhabitants of the State, to create jobs and employment opportunities, and to improve the economic welfare of the people by providing for the acquisition, construction, maintenance, repair, and operation of air quality projects. The Authority is a body corporate and politic in the State of Ohio and has neither stockholders nor equity holders. The governing body consists of seven members. Five public members, of which no more than three can be from the same political party, are appointed by the Governor with the advice and consent of the Senate. The two remaining members are the directors of the Ohio Environmental Protection Agency (Ohio EPA) and the Ohio Department of Health and serve in an ex-officio capacity. Under the provisions of the act, air quality revenue bonds shall not be deemed to constitute a debt or a pledge of the faith and credit of the State or any political subdivision thereof.

On August 1, 1975, Senate Bill No. 104 amended the Ohio Revised Code to allow the Authority to issue revenue bonds for public utilities and other facilities for control of air and thermal pollution whether or not such facilities result in the creation or preservation of jobs. This bill also provides that conditional or installment sales may be authorized and permit that the revenue bonds or notes bear a variable rate of interest changing from time to time according to a formula prescribed in the bond or note agreement.

Conduit Debt Obligations

The Ohio Air Quality Development Authority may at any time issue revenue bonds and notes of the State in such principal amounts as, in the opinion of the Authority, are necessary for the purpose of paying any part of the cost of one or more air quality projects or parts thereof. The Authority may at any time issue renewal notes, issue bonds to pay such notes and, whenever it deems refunding expedient, refund any bonds by the issuance of air quality revenue refunding bonds of the State, whether the bonds to be refunded have or have not matured, and issue bonds partly to refund bonds then outstanding, and partly for any other authorized purpose. The renewal notes, bonds, and air quality revenue refunding bonds are issued under the Authority's name; however, they are not obligations of the Authority or the State of Ohio, but are backed by specific streams of revenue and additional collateralization as deemed necessary at the time of issuance. The unaudited aggregate amount of principal outstanding as of December 31, 2006 was approximately \$1.3 billion.

Agreements between the borrower, the Authority and the purchaser determine the retirement period of the bonds. Interest rates are determined by existing bond market conditions at the time of sale.

Small Business Programs

During fiscal year 1995, the Authority began two operations, both of which were created by Senate Bill No. 153, effective October 19, 1993. The operations are described in Ohio Revised Code Section 3706.19.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2006

The first operation is the office of Ombudsman for the small business stationary source technical and environmental compliance assistance program that was created in Ohio Revised Code Section 3704.18. The Ombudsman's duties include facilitating and promoting the participation of small businesses in compliance with the Federal Clean Air Act, provide and disseminate information about air pollution requirements and control technologies, conduct studies to evaluate the impacts of the Federal Clean Air Act on Ohio's economy, and other related duties. The Executive Director of the Authority and the director of the Ohio EPA establish annual budgets which are funded by monies set aside in the Ohio EPA's budget.

The second operation is the Small Business Assistance Fund (SBAF) that was authorized by Ohio Revised Code Section 3704.19. The SBAF is funded by monies set aside in the Ohio EPA's budget. The Ombudsman may use the monies in the SBAF solely to provide financial assistance to small businesses that have one hundred or fewer employees and that are having financial difficulty complying with the Clean Air Act Amendments of 1990.

Coal Development Program

Effective July 1, 2003, legislation transferred the Ohio Coal Development Office, its staff and programs to the Ohio Air Quality Development Authority. The Coal Development Office co-funds the development and implementation of technologies that can use Ohio's vast reserves of high sulfur coal in an economical, environmentally sound manner. Funding for the operations of the Coal Development Office is provided by the State of Ohio through its general operating fund. Financing for the co-funding of the various research projects as well as the implementation of technologies is provided by the sale of general obligation bonds by the State of Ohio. The repayment of these bonds is not included within the Authority's financial statements; these payments are included within the State of Ohio's comprehensive annual financial report.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The coal development activity (governmental activity) and the air quality development activity (business-type activity) administered by the Ohio Air Quality Development Authority are aggregated and included in the comprehensive annual financial report of the State of Ohio as a discretely presented component unit. The Authority's management believes these financial statements present all activities for which the Authority is financially responsible.

B. Basis of Presentation

The Authority's basic financial statements consist of government-wide statements, including a statement of net assets and a statement of activities, and fund financial statements that provide a more detailed level of financial information.

Government-wide Financial Statements

The Statement of net assets and the statement of activities display information about the Authority as a whole. These statements include all of the financial activities of the Authority. The statements distinguish between those activities of the Authority that are governmental and those that are considered business-type activities.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2006

The statement of net assets presents the financial condition of the governmental and business-type activities of the Authority at year-end. The statement of activities presents a comparison between direct expenses and program revenues for each program or function of the Authority's governmental activities and for the business-type activities of the Authority. Direct expenses are those that are specifically associated with a service, program or department and therefore clearly identifiable to a particular function. Program revenues include charges paid by a recipient of the goods or services offered by the program, grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues not classified as program revenues are presented as general revenues of the Authority, with certain limited exceptions. The comparison of direct expenses with program revenues identifies the extent to which each governmental function or business-type activity is self-financing or draws from the general revenues of the Authority.

Fund Financial Statements

During the year, the Authority segregates transactions related to certain functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. Fund financial statements are designed to present financial information of the Authority at this more detailed level. At December 31, 2006, the Authority had one governmental fund (coal development) and one enterprise fund (air quality development).

C. Fund Accounting

The Authority uses funds to maintain its financial records during the year. A fund is defined as a fiscal and accounting entity with a self balancing set of accounts. There are three categories of funds: governmental, proprietary and fiduciary. The Authority reports no fiduciary funds.

Governmental Funds

Governmental funds are those through which most governmental functions typically are financed. Governmental fund reporting focuses on the sources, uses and balances of current financial resources. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used. Current liabilities are assigned to the fund from which they will be paid. The difference between governmental fund assets and liabilities is reported as fund balance. The following is the Authority's only governmental fund:

Coal Development - This fund is used to account for state revenue received for the operation of the Coal Development Office as well as bond proceeds used to finance the research and implementation of new technology designed to enhance the use of Ohio coal in industry.

Proprietary Funds

The proprietary fund reporting focuses on the determination of operating income, changes in net assets, financial position and cash flows. Proprietary funds are classified as either enterprise or internal service. The Authority has no internal service funds.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2006

Enterprise Funds – Enterprise funds may be used to account for any activity for which a fee is charged to external users for goods or services. The following is the Authority’s only enterprise fund:

Air Quality Development – This fund accounts for the activities of the air quality development office as well as the small business programs where the fees charged to the users are intended to cover the operating costs of the programs.

D. Measurement Focus

Government-wide Financial Statements

The government-wide financial statements are prepared using the economic resources measurement focus. All assets and all liabilities associated with the operations of the Authority are included on the statement of net assets. The statement of activities presents increases (i.e., revenues) and decreases (i.e., expenses) in total net assets.

Fund Financial Statements

The governmental fund is 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. The statement of revenues, expenditures and changes in fund balances report the sources (i.e., revenues and other financing sources) and uses (i.e., expenditures and other financing uses) of current financial resources. This approach differs from the manner in which the governmental activity of the government-wide financial statements is prepared. Governmental fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for the governmental fund. Since the governmental fund does not have any long term assets or liabilities, no reconciliation to the government-wide financial statements is necessary.

Like the government-wide statements, the enterprise fund is accounted for on a flow of economic resources measurement focus. All assets and all liabilities associated with the operation of these funds are included on the statement of net assets. The statement of changes in fund net assets presents increases (i.e., revenues) and decreases (i.e., expenses) in total net assets. The statement of cash flows provides information about how the Authority finances and meets the cash flow needs of its enterprise activity.

E. Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting; proprietary funds also use the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting. Differences in the accrual and modified accrual basis of accounting arise in the recognition of revenue and in the presentation of expenses versus expenditures.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2006

Revenues – Exchange and Non-exchange Transaction

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. The available period for the Authority is thirty-one (31) days after year-end.

Non-exchange transactions, in which the Authority receives value without directly giving equal value in return, include the state assistance revenue received by the Authority. Revenue from state assistance is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted. On a modified accrual basis, revenue from non-exchange transactions must also be available before it can be recognized.

Expenses/Expenditures

On the accrual basis of accounting, expenses are recognized at the time they are incurred.

The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are recorded when the related fund liability is incurred, if measurable. Allocation of costs, such as depreciation and amortization, are not recognized in governmental funds.

F. Application of Financial Accounting Standards Board (FASB) Statements

Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20: Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting, the Authority follows GASB guidance as applicable to proprietary funds and Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board (APB) Opinions and Accounting Research Bulletins issued on or before November 30, 1989 that do not conflict with or contradict GASB pronouncements. The Authority has elected not to adopt any FASB Statements and Interpretations issued after November 30, 1989.

G. Cash and Cash Equivalents

Cash and cash equivalents of the Authority include amounts on deposit in several separate accounts with the Treasurer of State and funds held in a money market account at a financial institution. For the purpose of the Statement of Cash Flows, the Authority considers all deposits with a maturity of three months or less when purchased, which includes all of the above accounts, to be cash equivalents, as defined in GASB Statement No. 9.

H. Capital Assets

Capital assets are recorded at cost and capitalized if the purchase price is \$300 or more. Depreciation is computed using the straight-line method over lives ranging from three to eight years. The Authority's capital assets and accumulated depreciation balances at December 31, 2006, was \$85,033 and \$66,395, respectively.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2006

I. Enterprise Fund Revenue

Administrative Fees

The Authority charges the borrower an administrative fee based on the size of the bond issue. From these administrative fees, the Authority pays all operating expenses for maintaining an office and full-time staff. In addition, the Authority engages in a research and development program that is funded from these administrative fees. The Authority recognizes the fees as revenue on the date the bond or note is sold which approximates the date the fee is received, since the fee is not legally due the Authority until that time.

Other Fees and Income

The Authority receives reimbursements from the Ohio Environmental Protection Agency for the cost of operating the two small business programs described earlier. In addition, the Authority earns interest income from money market and other funds held in trust or on deposit with the Treasurer of State. The Authority recognizes this revenue in the period in which it is earned.

Classification

The Authority considers bond administrative fees, interest earned from money market accounts and reimbursements from the Ohio Environmental Protection Agency as operating revenues.

J. Accrued Wages and Benefits

Accrued wages consists of wages payable to Authority employees as of December 31, 2006. The accrued wages balance consists of \$29,459 owed to employees for worked performed during the fiscal year.

K. Accrued Retirement Incentive

As part of the retirement package for an employee, the Authority agreed to purchase additional service time for that employee in the retirement system. While the employee retired as of December 31, 2006, the payment of the purchased service time did not take place until January 2007. Therefore, the amount of this payment \$72,324 was recognized as accrued retirement incentive as of December 31, 2006 as approval for the payment had occurred.

L. Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Authority carries commercial insurance for employee theft in the amount of \$250,000 per occurrence.

There have been no significant reductions in insurance coverage from the prior year. The amount of settlements has not exceeded insurance coverage in each of the past three fiscal years.

M. Interfund Activity

As a general rule, the effect of interfund (internal) activity has been eliminated from the government-wide statement of activities. The interfund services provided and used are not eliminated through the process of consolidation.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements

For the Year Ended December 31, 2006

3. PRIOR PERIOD ADJUSTMENTS

In prior years, the Authority had been reporting a liability associated with the leave time earned and maintained by its employees at the end of each year. However, as the State of Ohio is responsible for paying all leave time and severance payments (funded through a fee assessed to the Authority each pay-period) from a separate fund, it was determined reporting this liability was not appropriate. In addition, it was determined that an amount that should have been recorded as a receivable in FY2005 was not properly identified and ending net assets recognized in the business-type activity at June 30, 2005 were understated by \$121,000. These adjustments had the following effect on the Authority's ending net assets and fund balances previously reported at December 31, 2005:

	Governmental Activities	Business-Type Activities	Total
Net Assets reported at 12/31/05	\$ 7,352,477	\$ 6,203,829	\$ 13,556,306
Corrections:			
Compensated Absences	68,249	57,861	126,110
Accounts Receivable	-	121,000	121,000
Adjusted Net Assets at 12/31/05	<u>\$ 7,420,726</u>	<u>\$ 6,382,690</u>	<u>\$ 13,803,416</u>
		Coal Development	
Fund Balance reported at 12/31/05		\$ 7,419,078	
Corrections:			
Compensated Absences		<u>1,648</u>	
Adjusted Fund Balance at 12/31/05		<u>\$ 7,420,726</u>	

4. CASH AND CASH EQUIVALENTS

At fiscal year end, the carrying amount of the Authority's deposits was \$11,250,069 and the bank balance was \$11,250,069. The bank balance consists of the following:

Deposits with Treasurer of State: The Authority deposits cash with the Treasurer of State for purposes of reimbursement of the Authority's payroll costs which are paid through the State of Ohio's central accounting system. At December 31, 2006 the Authority had \$16,103 on deposit with the Treasurer of State.

Small Business Deposits with Treasurer of State: The Authority maintains small business funds with the Treasurer of State for the purpose of funding the Small Business Ombudsman and the Small Business Assistance programs described in the General Information section of the Notes. At December 31, 2006, the balances for the Small Business Ombudsman and the Small Business Assistance programs were \$691,140 and \$2,108,700, respectively.

Coal Development Deposits with Treasurer of State: Coal development grants are funded through the proceeds from the sale of State of Ohio's bonds. Bond proceeds which have not been distributed are on deposit with the Treasurer of State. At December 31, 2006, the Authority's cash balance in the coal research and development fund was \$4,162,968.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2006

Bank Money Market Funds: Cash not deposited with the Treasurer of State were held in a money market account that invests in U.S. Treasury instruments (bills, notes, bonds). At December 31, 2006, the Authority had \$4,271,158 in money market funds held in a trust account in the name of the Authority. The money market funds are not categorized by risk since they are not evidenced by securities that exist in physical or book entry form.

5. PENSION PLAN

All full-time employees participate in the Ohio Public Employees Retirement System (OPERS). OPERS administers three separate pension plans. The traditional plan is a cost-sharing, multiple-employer defined benefit pension plan. The member-directed plan is 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 the member and vested employer contributions plus any investment earnings.

The combined plan is a cost-sharing, multiple-employer defined benefit pension plan that has elements of both a defined benefit and a defined contribution plan. Under the combined plan, employer contributions are invested by the retirement system to provide a formula retirement benefit similar to the traditional plan benefit. Member contributions, whose investment is self-directed by the member, accumulate retirement assets in a manner similar to the member-directed plan.

OPERS provides retirement, disability, survivor and death benefits and annual cost of living adjustments to members of the traditional and combined plans. Members of the member-directed plan do not qualify for ancillary benefits. Authority to establish and amend benefits is provided by Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report that may be obtained by writing to OPERS, 277 E. Town St., Columbus, OH 43215-4642 or by calling (614) 222-5601 or 800-222-7377.

For the year ended December 31, 2006, the members of all three plans were required to contribute 9.0% of their annual covered salaries. The total employer's contribution rate for pension benefits for 2006 was 13.54%, of which 9.04% was used to fund pension obligations. The Ohio Revised Code provides statutory authority for member and employer contributions. Total required employer contributions were \$43,323, \$44,864 and \$45,785 for the years ending December 31, 2006, 2005, and 2004, respectively, and are equal to 100% of the amount billed to, and paid by, the Authority.

6. OTHER POST-EMPLOYMENT BENEFITS

The Ohio Public Employees Retirement System (OPERS) provides postretirement health care coverage to age and service retirees with ten or more years of qualifying Ohio service credit with either the traditional or combined plans. Health care coverage for disability recipients and primary survivor recipients is available. Members of the member-directed plan do not qualify for postretirement health care coverage. The health care coverage provided by the retirement system is considered an Other Postemployment Benefit (OPEB) as described in *GASB Statement No. 12*. A portion of each employer's contribution to the traditional or combined plans is set aside for the funding of postretirement health care based on authority granted by State statute. The portion of the state government employer contribution rate used to fund health care in 2006 was 4.50%.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2006

Benefits are advance-funded using the entry age normal actuarial determined basis. Significant actuarial assumptions, based on OPERS's latest actuarial review performed as of December 31, 2005, include:

Fund Method – the individual entry age actuarial cost method of valuation is used in determining the present value of the OPEB. The difference between assumed and actual experience (actuarial gains and losses) becomes part of unfunded actuarial accrued liability.

Assets Valuation Method - all investments are carried at market. For actuarial valuation purposes, a smoothed market approach is used. Assets are adjusted to reflect 25% of unrealized market appreciation or depreciation on investment assets annually, not to exceed a 12% corridor.

Investment Return – the investment assumption rate for 2005 was 6.5%.

Active Employee Total Payroll - an annual increase in active employee total payroll of 4.00% compounded annually (assuming no change in the number of active employees) and an additional increase in total payroll of between .50% and 6.30% based on additional annual pay increases.

Health Care - health care costs were assumed to increase at the projected wage inflation rate plus an additional factor ranging from 0.5% to 6% for the next 9 years. In subsequent years (10 and beyond), health care costs were assumed to increase at 4% (the projected wage inflation rate).

The number of active contributing participants in the traditional and combined plans was 369,214 as of December 31, 2006. The number of active contributing participants for both plans used in the December 31, 2005 actuarial valuation was 358,804. Actual employer contributions for 2006 which were used to fund postemployment benefits were \$21,565. The actual contribution and the actuarially required contribution amounts are the same. The amount of \$11.1 billion represents the actuarial value of OPERS's net assets available for OPEB at December 31, 2005. Based on the actuarial cost method used, the Actuarial Valuation as of December 31, 2005, reported the actuarial accrued liability and unfunded actuarial accrued liability for OPEB at \$31.3 billion and \$20.2 billion, respectively.

The Health Care Preservation Plan (HCPP) adopted by the OPERS Retirement Board on September 9, 2004, is effective January 1, 2007. OPERS took additional actions to improve the solvency of the Health Care Fund in 2005 by creating a separate investment pool for health care assets. Member and employer contribution rates increased as of January 1, 2006, and January 1, 2007, which will allow additional funds to be allocated to the health care plan.

7. OPERATING LEASES

The Authority has entered into lease agreements for office space, computers, copier and a postlink system. Leased properties not having the elements of ownership are classified as operating leases and are recorded as expenses when payable. Total operating lease expense for 2006 was \$76,711. The terms of the leases are not anticipated to change significantly in future fiscal years.

8. COMMITMENTS

As of December 31, 2006 the Authority had commitments of approximately \$9.4 million for research grants due on coal research and development agreements. These grants will be paid from proceeds of debt issued by the State of Ohio.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2006

9. CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2006 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
<u>Capital Assets:</u>				
Office Equipment	\$ 79,972	\$ 5,061	\$ -	\$ 85,033
Less accumulated depreciation for:				
Office Equipment	<u>(61,716)</u>	<u>(4,679)</u>	<u>-</u>	<u>(66,395)</u>
Total capital assets, net	<u>\$ 18,256</u>	<u>\$ 382</u>	<u>\$ -</u>	<u>\$ 18,638</u>

10. INTERFUND ACTIVITY

At December 31, 2006, the coal development activity owed the air quality development activity \$23,111 for its share of the overhead operating expenses for the fourth quarter of 2006. This amount was paid in the early 2007.

**OHIO AIR QUALITY DEVELOPMENT AUTHORITY
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - BUDGET (NON-GAAP) AND ACTUAL
COAL DEVELOPMENT
FOR THE YEAR ENDED DECEMBER 31, 2006**

	<u>Budgeted Amounts</u>		<u>Actual</u>	Variance with Final Budget
	<u>Original</u>	<u>Final</u>		Positive (Negative)
Revenues:				
State assistance	\$ 335,058	\$ 621,965	\$ 543,834	\$ (78,131)
Interest	<u>-</u>	<u>-</u>	<u>426,275</u>	<u>426,275</u>
Total Revenues	<u>335,058</u>	<u>621,965</u>	<u>970,109</u>	<u>348,144</u>
Expenditures:				
Current:				
General fund	335,058	621,965	537,266	84,699
Coal research and development	<u>14,718,763</u>	<u>18,976,099</u>	<u>13,926,757</u>	<u>5,049,342</u>
Total Expenditures	<u>15,053,821</u>	<u>19,598,064</u>	<u>14,464,023</u>	<u>5,134,041</u>
Change in Fund Balance	<u>(14,718,763)</u>	<u>(18,976,099)</u>	<u>(13,493,914)</u>	<u>5,482,185</u>
Fund Balance at Beginning of Year	2,978,451	2,978,451	2,978,451	-
Prior Year Encumbrances Appropriated	<u>5,717,392</u>	<u>5,717,392</u>	<u>5,717,392</u>	-
Fund Balance at End of Year	<u>\$ (6,022,920)</u>	<u>\$ (10,280,256)</u>	<u>\$ (4,798,071)</u>	<u>\$ 5,482,185</u>

See accompanying notes to the required supplementary information.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

Notes to the Required Supplementary Information
For the Year Ended December 31, 2006

Basis of Budgeting

The basis of budgeting differs from generally accepted accounting principles (GAAP) used for the Authority's year-end statements contained within the basic financial statements. Under that basis of accounting, revenues are generally recognized when the obligation to the Authority arises; the budget basis however, recognized revenue only when cash has been received. Under GAAP, expenditures are generally recognized in the period in which they are incurred. Under the budget basis, expenditures are recognized when cash has been disbursed or when an encumbrance has been placed against an appropriation.

Budgeting Policies

The coal development program is budgeted through the State of Ohio. Program allocations are contained within the biennium budget bill approved by the General Assembly. Since the State of Ohio is on a fiscal year which ends on June 30 and the Authority reports on a calendar year-end, there will be timing difference between the amount appropriated (authorized spending levels) and the estimated revenues.

Original budget amounts in the accompanying budgetary schedule was taken from the budget for the last half of the fiscal year 2006 State budget. The final budgetary amounts incorporate the first half of the fiscal year 2007 State budget. An appropriated budget is the expenditure authority created by appropriations bills that are signed into law and related estimated revenues. The budget also includes actual appropriation amounts automatically carried over from prior years by law, including the automatic rolling forward of appropriations to cover prior-year encumbrances.

Final budget amounts represent original appropriations modified by authorized transfers, supplemental and amended appropriations, and other legally authorized legislative and executive changes applicable to the period ending December 31, 2006, whenever signed into law or otherwise legally authorized.

A reconciliation of the fund balance reported under the GAAP basis and budgetary basis for the coal development program is presented below:

Reconciliation of GAAP Basis Change in Fund Balance
to Non-GAAP Budgetary Basis Change in Fund Balance
For the Coal Development Program
As of December 31, 2006

GAAP Basis	\$ (3,290,988)
Revenue Accruals	(7,759)
Expenditure Accruals	(753,256)
Encumbrances	<u>(9,441,911)</u>
Budgetary Basis	<u>\$ (13,493,914)</u>

Due to the timing differences between the State's fiscal year and the calendar year reporting period utilized by the Authority, various budgetary deficits will occur. These deficits will eventually be eliminated as the timing differences pass. In no event is the Authority entitled to spend or obligate State funds for which appropriations do not exist.



Mary Taylor, CPA

Auditor of State

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

Ohio Air Quality Development Authority
50 W. Broad Street, Suite 1718
Columbus, Ohio 43215

To the Authority:

We have audited the accompanying financial statements of the governmental activities and business-type activities of the Ohio Air Quality Development Authority (the Authority), a component unit of the State of Ohio, as of and for the year ended December 31, 2006, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated November 13, 2007. 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 Authority's internal control over financial reporting as a basis for designing our audit procedures for expressing our opinion on the financial statements, but not to opine on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we have not opined on the effectiveness of the Authority's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Authority's ability to initiate, authorize, record, process, or report financial data reliably in accordance with its applicable accounting basis, such that there is more than a remote likelihood that the Authority's internal control will not prevent or detect a more-than-inconsequential financial statement misstatement.

We consider the following deficiency described in the accompanying schedule of findings to be a significant deficiency in internal control over financial reporting: finding number 2006-001.

A material weakness is a significant deficiency, or combination of significant deficiencies resulting in more than a remote likelihood that the Authority's internal control will not prevent or detect a material financial statement misstatement.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and accordingly, would not necessarily disclose all significant deficiencies that are also material weaknesses. However, regarding the significant deficiency described above, we believe finding number 2006-001 is also a material weakness.

We noted certain matters that we reported to the Authority's management in a separate letter dated November 13, 2007.

Compliance and Other Matters

As part of reasonably assuring whether the Authority'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 affect 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 that we must report under *Government Auditing Standards*.

The Authority's response to the finding identified in our audit is described in the accompanying schedule of findings. We did not audit the Authority's response and, accordingly, we express no opinion on it.

We intend this report solely for the information and use of the Authority's management and governing board. We intend it for no one other than these specified parties.

A handwritten signature in cursive script that reads "Mary Taylor".

Mary Taylor, CPA
Auditor of State

November 13, 2007

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

SCHEDULE OF FINDINGS
JANUARY 1, 2006 TO DECEMBER 31, 2006

FINDINGS RELATED TO THE FINANCIAL STATEMENTS
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

FINDING NUMBER 2006-001

SIGNIFICANT DEFICIENCY / MATERIAL WEAKNESS

FINANCIAL REPORTING

Effective internal controls over financial reporting help to prevent or detect misstatements in the accounting records and financial statements and reasonably ensure compliance with laws, regulations and current governmental accounting standards. As described in AICPA's Codification of Auditing Standards AU Section 339, paragraph .15, footnote 5, "the term *those charged with governance* means the person(s) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting and disclosure process." As such, it is the Authority's responsibility to implement procedures, devise control activities, and provide for effective oversight of financial reporting, all of which promote the accuracy, completeness and reliability of data reported in the financial statements.

The American Institute of Certified Public Accountants issued Statement on Auditing Standards (SAS) number 112, titled *Communicating Internal Control Related Matters Identified in an Audit*, codified as AU Section 325 of AICPA's Auditing Standards, effective for audits of financial statements for periods ending on or after December 15, 2006. AU Section 325, paragraph .19 indicates eight separate indicators of a control deficiency that should be regarded as at least a significant deficiency and a strong indicator of a material weakness in internal control. Two of these indicators are "ineffective oversight of the entity's financial reporting and internal control by those charged with governance" and "identification by the auditor of a material misstatement in the financial statements for the period under audit that was not initially identified by the entity's internal control".

In addition, Ohio Revised Code (ORC) Section 3706.13, relating to the Ohio Air Quality Development Authority, states in part:

...

On or before the twentieth day of April in each year, the authority shall make a report of its activities for the preceding calendar year to the governor and the general assembly. Each such report shall set forth a complete operating and financial statement covering the authority's operations during the year....

The Authority has attempted to implement a system of internal controls for their accounting and financial reporting processes, but the controls they have in place have proven to be ineffective. As a result, numerous errors were noted in the original financial statements presented to the auditor, including one that involved a material misstatement. Specifically, the Authority did not maintain a complete and accurate Recent Bond Summary which resulted in a significant amount of project administration fees which should have been reported in the financial statements as revenue and a corresponding receivable. In addition, many other errors of varying magnitude were noted in the accounting records, original statements, and supplementary information during the audit process.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

**SCHEDULE OF FINDINGS
JANUARY 1, 2006 TO DECEMBER 31, 2006
(Continued)**

**FINDINGS RELATED TO THE FINANCIAL STATEMENTS
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS (Continued)**

FINDING NUMBER 2006-001 (Continued)

SIGNIFICANT DEFICIENCY / MATERIAL WEAKNESS (Continued)

FINANCIAL REPORTING (Continued)

The Authority has contracted with outside professional assistance for financial statement preparation and various accounting functions. However, although outside accountants may prepare the Authority's basic financial statements, management is ultimately responsible for the presentation of the statements as well as compliance with applicable laws, regulations and accounting principles. While the statements are reviewed by the Authority's Executive Director, the Authority's governing board does not play an active role in the financial reporting process, and in fact does not even see the financial statements until the final audited statements are presented to the board by the Auditor of State's office at one of their monthly meetings. In addition, it is uncertain that financial reporting is a priority at the Authority, given that the first draft of the financial statements, which contained the aforementioned errors, was not presented to the auditor until June 11, 2007, well after the date established by ORC Section 3706.13. Lastly, errors contained in the financial statements and underlying accounting records, as well as the additional time needed to produce these records, indicates that the Authority's current procedures over financial reporting are ineffective.

The failure to implement effective controls or oversight of the accounting and financial reporting processes increases the risk that the accounting records of the Authority are inaccurate, that errors will occur and not be detected, and that significant errors that are detected will require adjustment to the accounting records and financial statements. Inaccurate financial statements provide state government and external parties erroneous information about the Authority, resulting in reduced confidence in the Authority's functions.

To enhance financial accountability, we recommend the Authority review their current financial reporting process, as well as errors detected during the audit process, and actively re-design and implement formal policies and procedures specifically addressing the timely and accurate completion and review of the basic financial statements, including Management's Discussion and Analysis and related footnotes. Such policies and procedures should be designed so that the Authority has the opportunity to detect errors and potential modifications that may be necessary before submitting the final financial statements for the auditor's review prior to the statutory deadline. We further recommend the Authority implement appropriate monitoring controls so that management can more effectively oversee the agency's fiscal function to help ensure the accounting system is providing complete, accurate and timely information for inclusion in the Authority's financial statements. This may include the hiring of additional personnel experienced with financial reporting, as well as additional training in accounting functions and financial reporting for Authority employees involved in the accounting process.

OFFICIALS' RESPONSE

On November 13, 2007 your audit team conducted the exit interview for the 2006 audit of the Ohio Air Quality Development Authority (OAQDA). The exit interview was conducted as part of the OAQDA's regularly scheduled public meeting; five members, as well as staff, were present. I am writing at the direction of the members of OAQDA and in response to 1) finding No. 2006-001 and 2) to report on discussion and actions taken by OAQDA immediately following the exit interview.

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

SCHEDULE OF FINDINGS
JANUARY 1, 2006 TO DECEMBER 31, 2006
(Continued)

FINDINGS RELATED TO THE FINANCIAL STATEMENTS
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS (Continued)

FINDING NUMBER 2006-001 (Continued)

OFFICIALS' RESPONSE (Continued)

The current and prior members of the OAQDA have always taken their responsibilities for governance and oversight seriously. Each month, members receive a report on all OAQDA expenditures for the previous month; expenditures of more than \$1,000 (beyond a range of approved normal operating expenses such as rent, telephones, etc.) require prior approval (by resolution) of the OAQDA in public meeting. OAQDA appreciates the advice given by your audit team over the last several years and fully recognizes that the OAQDA budget has grown in amount and complexity, and consequently OAQDA will continue to improve its financial management systems.

Although OAQDA members believe some of the characterizations of systems weakness are overstated, there is no disagreement that an accounting error was made that resulted in inaccurate reporting of part of a complex schedule relating to receivable project administration fees. As pointed out in the exit interview, all project administration fees were collected; there was no misappropriation of funds; and, there is no allegation of unauthorized or illegal activity. We agree the accounting error should not have occurred and appreciate the value of an audit in uncovering, and correcting, it.

In specific response to finding No. 2006-001, immediately after the exit interview, the OAQDA by unanimous vote directed the Executive Director to create and fill the position of fiscal officer. This action will implement your audit team's recommendation to reduce OAQDA reliance upon the services of an outside independent accounting firm. Included in the job description of the fiscal officer to OAQDA will be to review any accounting errors identified through the audit process and to continue OAQDA efforts to identify and eliminate any procedures, or lack thereof, that may have contributed to this accounting error.

This action will continue the OAQDA's pattern of carefully reviewing recommendations received from the Auditor of State's audit team and implementing the same as our fiscal resources allow and the members deem appropriate. I would be glad to answer any questions you or your audit team may have.

Sincerely,

Mark R. Shanahan, Ph.D.
Executive Director



Mary Taylor, CPA
Auditor of State

OHIO AIR QUALITY DEVELOPMENT AUTHORITY

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
DECEMBER 24, 2007