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.

By the numbers

OF 88 COUNTIES:

1
in fiscal stress

3
early signs of stress

1
is an indicator from early signs of stress

OF 247 CITIES:

9
in fiscal stress

6
early signs of stress

13
are an indicator from early signs of stress

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

An overview (continued)

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).

How the indicators have changed

TOTAL CRITICAL INDICATORS

	2015	2016	up/down	%
Counties	36	64	up	78
Cities	275	301	up	9

TOTAL CAUTIONARY INDICATORS

	2015	2016	up/down	%
Counties	132	182	up	38
Cities	518	513	down	<1

AT LEAST ONE CRITICAL OR CAUTIONARY INDICATOR

	2015	2016	up/down	%
Counties	70	78	up	11
Cities	217	226	up	4

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 basis 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.