

*“Rock Solid Safety,  
Entrepreneurial Liquidity,  
and Wealth-Building Yield”*



# *Annual Report*

*June 30, 2004*

*Joseph T. Deters  
Treasurer of State*







**Auditor of State  
Betty Montgomery**

The Honorable Joseph T. Deters  
Treasurer of State  
Columbus, Ohio

We have reviewed the Independent Auditor's Report of the State Treasury Asset Reserve of Ohio, Franklin County, prepared by Deloitte & Touche LLP, for the audit period July 1, 2003 through June 30, 2004. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The State Treasury Asset Reserve of Ohio is responsible for compliance with these laws and regulations.

A handwritten signature in cursive script that reads "Betty Montgomery".

BETTY MONTGOMERY  
Auditor of State

November 18, 2004

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**A Message from Treasurer of State Joseph T. Deters**



Dear Shareholders:

It is a pleasure to present to you the STAR Ohio Annual Report for the fiscal year ended June 30, 2004.

Its 18<sup>th</sup> year of successful operation very much resembled the first 17 years in that STAR Ohio remained an effective investment tool for Ohio's public funds managers, delivering the same high levels of safety, liquidity, and yield that are its hallmark.

On-line ACH deposits and withdrawals became operational during Fiscal Year 2004. This new option is being put to good use, and the feedback we have received thus far has been quite positive. In addition, the program's commercial paper limit increase from five to ten percent has shown the potential to enhance yield without exposing shareholders to undue risk.

We remain committed to the same risk-averse policies that have made STAR Ohio such a rock-solid local government investment pool. As always, your continued support and cooperation are most appreciated.

Respectfully,

A handwritten signature in black ink that reads "Joseph T. Deters". The signature is written in a cursive, flowing style.

Joseph T. Deters  
Ohio Treasurer of State

## MANAGEMENT'S DISCUSSION & ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

### Background

The State Treasury Asset Reserve of Ohio ("STAR Ohio" or "the Pool") is a statewide investment pool managed and administered by the Treasurer of the State of Ohio. Participation is offered to Ohio political subdivisions as a means to invest in a portfolio of short-term investment securities. The investment objective of STAR Ohio is to seek as high a level of current income as is consistent with prudent investment management, the preservation of capital and the maintenance of liquidity. STAR Ohio seeks to achieve this objective by investing only in certain high-grade investment instruments. STAR Ohio is similar in concept to a registered investment company using redeemable securities, commonly called a "money market mutual fund". Our discussion and analysis below is based upon currently known facts and conditions that we judge to have had a material effect on STAR Ohio's financial condition and results of operations.

### Overview of Financial Condition

The targeted overnight federal funds rate remained at its historical low of 1.00% for the fiscal year ended June 30, 2004. Low interest rates and general economic conditions experienced by STAR Ohio participants during the year resulted in an approximate \$1.4 billion reduction in the investment portfolio due to a decline in net assets as shareholders redeemed funds.

### Overview of Operations

Net investment income as a percentage of average daily net assets declined to 1.00% in fiscal year 2004 from 1.44% in fiscal year 2003, resulting primarily from the federal funds targeted rate remaining at 1.00%. The weighted average yield of STAR Ohio's investment portfolio was 1.19% and 1.14% at June 30, 2004 and 2003, respectively.

## STATE TREASURY ASSET RESERVE OF OHIO FINANCIAL HIGHLIGHTS

Data for each share outstanding throughout the year

	Year ended June 30,				
	2004	2003	2002	2001	2000
Net asset value, beginning of year .....	\$1.00	\$1.00	\$1.00	\$1.00	\$1.00
Net investment income .....	.0100	.0144	.0256	.0566	.0557
Distributions from net investment income .....	(.0100)	(.0144)	(.0256)	(.0566)	(.0557)
Net asset value, end of year .....	<u>\$1.00</u>	<u>\$1.00</u>	<u>\$1.00</u>	<u>\$1.00</u>	<u>\$1.00</u>
Total return .....	1.00%	1.44%	2.56%	5.66%	5.57%
<b>Ratios/Supplemental Information</b>					
Expenses as a percentage of average net assets(1) .....	.082%	.077%	.072%	.050%	.054%
Net investment income as a percentage of average net assets(1) .....	1.00%	1.44%	2.56%	5.66%	5.57%
Net assets, at end of year .....	\$5,055,228,202	\$6,477,198,143	\$7,197,975,497	\$9,358,311,989	\$5,769,461,746

(1) These percentages should not be construed as representative of the yield or expenses related to further investments in the Pool.



## SCHEDULE OF INVESTMENTS

June 30, 2004

Principal Amount	Maturity Date (2004, unless otherwise noted)	Value (Note A)
<b>FEDERAL AGENCY ISSUES — 87%</b>		
\$1,400,000,000	Federal Home Loan Bank Discount Notes, .97-1.42% .....	7/1 - 9/15 \$1,398,833,764
1,554,786,000	Federal Home Loan Mortgage Corp. Discount Notes, 1.04-1.50% .....	7/6 - 4/5/05 1,551,869,965
1,475,000,000	Federal National Mortgage Association Discount Notes, 1.03-1.52% .....	7/7 - 4/1/05 <u>1,470,564,365</u>
	<b>Total Federal Agency Issues .....</b>	<b><u>4,421,268,094</u></b>
<b>COMMERCIAL PAPER — 12%</b>		
20,000,000	American General Finance Corp., 1.15% .....	8/4 19,978,278
50,000,000	Bank of America Corp., 1.30-1.47% .....	8/17 - 9/17 49,877,944
100,000,000	Citicorp, 1.06-1.08% .....	7/7 - 7/22 99,956,431
90,000,000	Edison Asset Securitization LLC, 1.05-1.48% ...	7/12 - 9/16 89,907,035
90,000,000	FCAR Owner Trust, 1.03-1.27% .....	7/6 - 9/3 89,946,554
40,000,000	General Electric Capital Corporation, 1.08-1.30% .....	8/3 - 8/17 39,953,328
80,000,000	General Electric Capital Services, 1.06-1.32% ..	7/9 - 8/24 79,918,078
115,000,000	Household Finance Corp., 1.08-1.47% .....	7/23 - 9/24 114,792,005
20,000,000	UBS Finance Delaware LLC, 1.44% .....	9/21 <u>19,934,400</u>
	<b>Total Commercial Paper .....</b>	<b><u>604,264,053</u></b>
<b>DAILY REPURCHASE AGREEMENTS — 1%</b>		
32,517,192	Fifth Third Bank, Cincinnati, 1.20% collateralized by \$35,552,000 Federal Home Loan Mortgage Corporation Note, 3.00% due 6/30/09, market value \$33,232,730 (repurchase proceeds \$32,518,276) .....	<u>32,517,192</u>
	<b>Total Daily Repurchase Agreement .....</b>	<b><u>32,517,192</u></b>
	<b>TOTAL INVESTMENTS — 100% .....</b>	<b>5,058,049,339</b>
	<b>Liabilities in excess of other assets .....</b>	<b><u>(2,821,137)</u></b>
	<b>NET ASSETS — 100% — equivalent to \$1.00 per share for 5,055,228,202 outstanding shares of the Pool .....</b>	<b><u>\$5,055,228,202</u></b>

See Accompanying Notes to Financial Statements.



**STATEMENT OF ASSETS & LIABILITIES**  
**JUNE 30, 2004**

**ASSETS**

Investments	
Federal Agency Issues .....	\$4,421,268,094
Commercial Paper .....	604,264,053
Daily Repurchase Agreement .....	<u>32,517,192</u>
Total Investments .....	5,058,049,339
Collateral on Securities Lent .....	<u>1,153,018,868</u>
Total Assets .....	<u>6,211,068,207</u>

**LIABILITIES**

Obligation Under Security Lending .....	1,153,018,868
Payable for Fund Shares Redeemed .....	2,399,913
Accrued Management fees .....	184,876
Accrued Co-Administrator fees .....	89,478
Accrued Custodian fees .....	80,564
Other Liabilities .....	<u>66,306</u>
Total Liabilities .....	<u>1,155,840,005</u>

<b>NET ASSETS</b> .....	<u>\$5,055,228,202</u>
<b>Participant Net Asset Value, Price Per Unit</b> .....	\$ 1.00

See Accompanying Notes to Financial Statements.





## STATEMENTS OF OPERATIONS

	Year ended June 30,	
	2004	2003
<b>INVESTMENT INCOME</b>		
Interest income .....	\$64,916,863	\$107,102,607
Securities lending income .....	1,043,169	63,401
Total investment income .....	65,960,032	107,166,008
<b>EXPENSES</b>		
Management fees .....	2,341,052	2,447,623
Co-administrator fees .....	1,252,850	1,462,404
Custodian and transfer agent fees .....	1,119,173	1,292,339
Security lending fees .....	218,046	18,245
Postage and printing fees .....	39,460	51,395
Audit fees .....	34,500	33,000
S & P analytical fees .....	33,000	33,000
Telephone response fees .....	28,220	31,445
Miscellaneous .....	96,260	71,240
Total expenses .....	5,162,561	5,440,691
<b>NET INVESTMENT INCOME</b> .....	<b>\$60,797,471</b>	<b>\$101,725,317</b>

## STATEMENTS OF CHANGES IN NET ASSETS

	Year ended June 30,	
	2004	2003
<b>DECREASE IN NET ASSETS</b>		
<b>Operations</b>		
Net investment income .....	\$ 60,797,471	\$ 101,725,317
<b>Distributions to shareholders from</b>		
Net investment income .....	(60,797,471)	(101,725,317)
<b>Capital share transactions net decrease</b> — Note E....	(1,421,969,941)	(720,777,354)
Decrease in net assets .....	(1,421,969,941)	(720,777,354)
<b>Net assets</b>		
Beginning of year .....	6,477,198,143	7,197,975,497
End of year .....	<b>\$ 5,055,228,202</b>	<b>\$6,477,198,143</b>

See Accompanying Notes to Financial Statements.



## NOTES TO FINANCIAL STATEMENTS

### NOTE A — SUMMARY OF ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Section 135.45 of the Ohio Revised Code (“ORC”) permits the state’s political subdivisions to pool their public funds into an investment fund managed by the State Treasurer and the State Treasurer’s staff of portfolio managers. The State Treasury Asset Reserve of Ohio (“STAR Ohio” or “the Pool”) provides units of local government with an alternative investment option for their public funds.

STAR Ohio is a statewide investment pool managed by the Treasurer of the State of Ohio. Participation is offered to Ohio political subdivisions as defined in Section 135.45(F)(2)(a) of the Ohio Revised Code. STAR Ohio offers these subdivisions a means of investing in a portfolio of investment instruments. STAR Ohio seeks to obtain as high a level of current income as is consistent with prudent investment management, the preservation of capital and maintenance of liquidity. There can be no guarantee that this will be achieved.

State Treasurer Joseph T. Deters, through the Investment Department, 30 East Broad Street, 9th Floor, Columbus, Ohio 43215-3461, serves as investment advisor and administrator to STAR Ohio. The advisor manages the investment and reinvestment of STAR Ohio’s assets in accordance with STAR Ohio’s investment objectives and policies, subject to the general limitations of Section 135.143 of the Ohio Revised Code. In addition, the advisor is responsible for the overall management of STAR Ohio’s business affairs. STAR Ohio compensates the advisor with a flat management fee of \$500,000 per year.

Carnegie Capital Management Company, Cleveland, Ohio, is the co-administrator and provides certain clerical and administrative services for STAR Ohio. Compensation is based on a percentage of daily net assets.

Provident Bank, Cincinnati, Ohio, is the dividend and transfer agent for STAR Ohio and also serves as investment consultant and custodian of its portfolio. Provident Bank was appointed investment consultant on July 1, 2001. Effective July 1, 2004, Provident Bank was acquired by National City Corporation, Cleveland, Ohio. United American Capital Corporation, Worthington, Ohio, and Meeder Asset Management Inc., Dublin, Ohio assist Provident Bank with investment consulting services. The investment consulting fees are reflected in the management fees in the Statement of Operations. Compensation is based on a percentage of daily net assets.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

Pursuant to the Government Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting*, STAR Ohio follows GASB guidance as applicable to proprietary funds and Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989 that do not conflict with or contradict GASB pronouncements.

During March 2003, the GASB issued Statement No. 40, *Deposit and Investment Risk Disclosures (an amendment of GASB Statement No. 3)*. This statement amends Statement No. 3 and addresses additional cash and investment risks to which governments are exposed. Generally, this statement requires that state and local governments communicate key information about such risks in four principal areas: investment credit risks, including credit quality information issued by rating agencies; interest rate disclosures that include investment maturity information; interest rate sensitivity for investments that are highly sensitive to changes in interest rates; and foreign exchange exposures that would indicate the foreign investment’s

denomination. The provisions of this statement are effective for financial statements for the fiscal year ended June 30, 2005. STAR Ohio does not believe the adoption of GASB No. 40 will have a material impact on its financial statement disclosures.

## **NOTE B — INVESTMENT SECURITIES**

Investment securities are valued using the amortized cost method (which approximates fair value) whereby a security is valued at cost adjusted for the amortization of any premiums or accretion of any discounts over the period until maturity.

Security transactions are accounted for on the trade date (date order to buy or sell is executed). Interest income is determined on an accrual basis with discounts earned (including original issue and market discount) being accreted and premiums paid being amortized. Realized gains and losses, if any, on sales of securities are calculated on the identified cost basis.

STAR Ohio is permitted to invest in commercial paper, but shall not exceed 10 percent of the average net assets on an annualized basis. Commercial paper holdings when purchased represent 10 percent or less of the average net assets on an annualized basis. As of June 30, 2004, commercial paper holdings represented 12 percent of the net assets, due to a decline in net assets by year end.

All repurchase agreements are fully collateralized by United States Government or Federal Agency securities, pursuant to Section 135.143 of the Ohio Revised Code, and such collateral is in the possession of STAR Ohio's custodian. STAR Ohio evaluates collateral daily to ensure its market value plus accrued interest exceeds the delivery value of the repurchase agreement at maturity. STAR Ohio does not enter into reverse repurchase (borrowing) agreements.

The Pool maintains a stable net asset value per share by using the amortized cost method of portfolio valuation. The Pool has established procedures, reasonably designed, taking into account current market quotations, to stabilize the net asset value per share, as computed for the purpose of purchase and redemption, at a single value of \$1.00. The mark-to-market of the portfolio is used to monitor the appropriateness of the amortized cost method and is calculated using available market quotations.

In accordance with GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, STAR Ohio is required to classify its investments into categories of custodial risk. Category 1 includes investments that are insured or registered for which the securities are held by STAR Ohio or by its agent in the name of STAR Ohio. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the name of STAR Ohio. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty or by its trust department or agent but not in STAR Ohio's name. All investments of STAR Ohio, including collateral on securities lent, meet the criteria of Category 1, except securities on loan, which by their nature are not required to be so categorized.

## **NOTE C — SECURITIES LENDING**

Pursuant to ORC 135.143, the Pool may lend up to 25 percent of its securities to any eligible financial institution that is a member of the Federal Reserve System or any recognized United States government securities dealer. Under the terms of the lending agreement, STAR Ohio lends securities and the eligible financial institution or primary dealer agrees to simultaneously exchange similar securities or cash. At June 30, 2004, collateral on securities lent consisted of commercial paper, repurchase agreements and variable rate notes. STAR Ohio may not pledge or sell the securities received in exchange. STAR Ohio receives payments from borrowers equivalent to the interest that would have been earned on securities lent while simultaneously seeking to earn interest on the investment of cash collateral. The income from this program is distributed daily. STAR Ohio calculates a mark-to-market review of collateral daily to ensure its market value is at least 100% of the underlying securities lent. At year-end, the Pool has no credit risk exposure to the borrowers because the amounts the Pool owes the borrower exceeds the amounts the borrowers owe the Pool.

The Pool follows strict levels of collateralization governed by daily mark-to-market analysis, a review of the credit worthiness of securities dealers and banks, and strict monitoring of their respective credit limits. This is done to control exposure due to possible credit loss resulting from a reduction in the underlying collateral value or non-performance by a security dealer or bank. Either the Pool or the borrower can terminate all security loans on demand.

As of June 30, 2004, the amortized cost and fair value of securities available for securities lending were \$4,246,477,219 and \$4,243,356,124 respectively, of which the following were actually lent:

	<u>Amortized Cost</u>	<u>Fair Value</u>
Federal Home Loan Bank Discount Notes .....	\$ 99,700,272	\$ 99,720,050
Federal Home Loan Mortgage Corp. Discount Notes .....	448,918,606	448,512,444
Federal National Mortgage Association Discount Notes .....	600,889,204	600,564,655
	<u>\$1,149,508,082</u>	<u>\$1,148,797,149</u>

The collateral at year-end for the lent securities included commercial paper, agency repurchase agreements and variable rate notes; the fair market values were \$120,038,429, \$789,655,570 and \$243,324,869, respectively. No losses were incurred during the year on the Pool's securities lending transactions from the default of a borrower or lending agent.

#### NOTE D — INCOME DISTRIBUTIONS

STAR Ohio declares a distribution each business day to distribute its net investment income and realized capital gains, if any. All such distributions are automatically reinvested in additional shares of the Pool.

STAR Ohio is not subject to income taxes.

#### NOTE E — CAPITAL SHARES

Transactions in capital shares (all at \$1.00 per share) were as follows:

	<u>Year ended June 30,</u>	
	<u>2004</u>	<u>2003</u>
Shares sold .....	35,330,565,501	34,471,966,637
Shares issued for reinvestment of distributions.....	60,797,471	101,725,317
	<u>35,391,362,972</u>	<u>34,573,691,954</u>
Shares redeemed .....	<u>(36,813,332,913)</u>	<u>(35,294,469,308)</u>
Capital shares transactions net decrease .....	<u>(1,421,969,941)</u>	<u>(720,777,354)</u>



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## INDEPENDENT AUDITORS' REPORT

The Honorable Betty Montgomery  
Auditor of State

The Honorable Joseph T. Deters  
Treasurer of State:

We have audited the statement of assets and liabilities, including the schedule of investments, of the State Treasury Asset Reserve of Ohio ("STAR Ohio") as of June 30, 2004, and the related statements of operations, changes in net assets and the financial highlights for the years ended June 30, 2004 and 2003. These financial statements are the responsibility of the management of STAR Ohio. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits. STAR Ohio's financial statements and financial highlights for the periods prior to the year ended June 30, 2001 were audited by other auditors whose report, dated July 21, 2000, expressed an unqualified opinion on those statements.

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

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of STAR Ohio as of June 30, 2004 and the results of its operations, the changes in its net assets and the financial highlights for the years ended June 30, 2004 and 2003 in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis on page 2 is not a required part of the basic financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 28, 2004 on our consideration of STAR Ohio's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

Cleveland, Ohio  
July 28, 2004



## APPENDIX

### STANDARD & POOR'S RATING OF STAR OHIO

Standard & Poor's has assigned an AAAm money market rating, its highest rating, to STAR Ohio. By obtaining a triple-A rating, STAR Ohio is considered to have a superior capacity to maintain principal (\$1.00 per share value) and limit exposure to loss. The rating is based on an analysis of the Pool's management, investment guidelines, portfolio holdings and market price exposure.

### SUMMARY OF INVESTMENT OBJECTIVES & ELIGIBLE INVESTMENTS

The investment objective of STAR Ohio is to seek as high a level of current income as is consistent with prudent investment management, the preservation of capital and maintenance of liquidity. STAR Ohio seeks to achieve this objective by investing only in certain high-grade short-term investment instruments, which are authorized for investment by the State of Ohio as specified in Section 135.143 of the Ohio Revised Code. Instruments in which STAR Ohio may invest include:

(1) United States Treasury bills, notes, bonds, or any other obligations or securities issued by the United States Treasury or any other obligation guaranteed as to principal and interest by the United States;

(2) Bonds, notes, debentures, or any other obligations or securities issued by any federal government agency or instrumentality;

(3)(a) Written repurchase agreements with any eligible Ohio financial institution that is a member of the Federal Reserve System or Federal Home Loan Bank or any recognized United States government securities dealer, under the terms of which agreement the Treasurer of State purchases and the eligible financial institution or dealer agrees unconditionally to repurchase any of the securities that are listed in items (1) or (2) above and that will mature or are redeemable within ten years from the date of purchase. The market value of securities subject to these transactions must exceed the principal value of the repurchase agreement by an amount specified by the Treasurer of State, and the securities must be delivered into the custody of the Treasurer of State or the qualified trustee or agent designated by the Treasurer of State. The agreement shall contain the requirement that for each transaction pursuant to the agreement, the participating institution or dealer shall provide all of the following information:

(i) The par value of the securities;

(ii) The type, rate, and maturity date of the securities;

(iii) A numerical identifier generally accepted in the securities industry that designates the securities.

(b) STAR Ohio does not invest in reverse repurchase agreements; which are securities sold to a broker-dealer under the provision that they will be bought back at a predetermined date for a specified price.

(4) The Treasurer of State also may sell any securities, listed in items (1) or (2) above, regardless of maturity or time of redemption of the securities, under the same terms and conditions for repurchase, provided that the securities have been fully paid for and are owned by the Treasurer of State at the time of the sale.

(5) Securities lending agreements with any eligible financial institution that is a member of the Federal Reserve System or Federal Home Loan Bank or any recognized United States government securities dealer, under the terms of which agreement the Treasurer of State lends securities and the eligible financial institution or dealer agrees to simultaneously exchange similar securities or cash, equal value for equal value;

(6) Various forms of commercial paper, maturing in 180 days or less, issued by any corporation that is incorporated under the laws of the United States or a state, which such notes are rated in the two highest categories by two nationally recognized rating agencies, provided that the total amount invested in commercial paper at any time shall not exceed ten percent of the average net assets on an annualized basis, as determined and calculated by the Treasurer of State;

(7) Banker's acceptances, maturing in 270 days or less, which are eligible for purchase by the Federal Reserve System, provided that the total amount invested in banker's acceptances at any time shall not exceed ten percent of the total average net assets, as determined and calculated by the Treasurer of State;

(8) Certificates of deposit in eligible institutions applying for interim moneys as provided in section 135.08 of the Ohio Revised Code.

(9) No-load money market mutual funds consisting exclusively of obligations described in (1) or (2) of this section and repurchase agreements secured by such obligations.

## **CERTIFICATES OF DEPOSIT**

Under Ohio law, financial institutions, which issue certificates of deposit to the state, must be eligible state depositories. An institution, which desires to be an eligible depository, must make an application therefore, in writing, to the State Board of Deposit, every two years in the even numbered years.

The State Board of Deposit consists of the Treasurer of State, as chairperson, the Auditor of State, and the Attorney General. The application shall specify the maximum amount of money which the applicant desires to receive and have on deposit and shall be accompanied by a financial statement of the applicant, under oath of an officer; in such detail as to show the capital funds of the applicant, as of the date of its latest report to the superintendent of banks, superintendent of savings and loan associations, office of thrift supervision, or comptroller of the currency. It is the responsibility of the financial institution to ensure that it shall not receive or have on deposit at any one time public moneys in excess of 30 percent of its total assets.

Certificates of deposit as described in item (8) above, must be fully collateralized for principal amounts in excess of the amount insured by the Federal Deposit Insurance Corporation or by any agency or instrumentality of the federal government. The Treasurer of State will strictly adhere to the provisions of Section 135.18 of the Ohio Revised Code, regarding the security for repayment of public deposits.

**STATE TREASURY ASSET RESERVE OF OHIO  
STAR Ohio**

30 East Broad Street, 9th Floor  
Columbus, Ohio 43215-3461  
<http://www.starohio.org>

**INVESTMENT ADVISOR AND ADMINISTRATOR**

Joseph T. Deters  
Treasurer of State

**Co-Administrator**

Carnegie Capital Management Company  
Cleveland, Ohio

**Custodian and Transfer Agent**

Provident Bank  
Cincinnati, Ohio

**Investment Consultant**

Provident Bank  
Cincinnati, Ohio

**For further information, current yields, or  
assistance in opening a STAR account,  
call toll-free: 1-800-648-7827 (STAR).**

Additional information regarding **STAR Ohio** and other  
Treasurer of State Programs may be accessed through the  
Treasury Web Site at:

<http://www.ohiotreasurer.org>  
and  
[www.starohio.org](http://www.starohio.org)

The Office of the State Treasurer, Carnegie Capital Management Company and Provident Bank  
are Equal Opportunity Employers and Service Providers.



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***State Treasury Asset  
Reserve of Ohio  
Investment Trust Fund***

*Financial Statements as of June 30, 2004 and  
for the Years Ended June 30, 2004 and 2003  
and Independent Auditors' Report*

# STATE TREASURY ASSET RESERVE OF OHIO INVESTMENT TRUST FUND

## TABLE OF CONTENTS

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	<b>Page</b>
INDEPENDENT AUDITORS' REPORT	1
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	2
FINANCIAL STATEMENTS:	
Statement of Assets and Liabilities as of June 30, 2004	3
Statements of Operations and Changes in Net Assets for the Years Ended June 30, 2004 and 2003	4
Notes to Financial Statements	5-8

## INDEPENDENT AUDITORS' REPORT

To the Treasurer of the State of Ohio:

We have audited the accompanying statement of asset and liabilities of the State Treasury Asset Reserve of Ohio Investment Trust Fund ("Trust Fund") as of June 30, 2004, and the related statements of operations and changes in net assets for the years ended June 30, 2004 and 2003. These financial statements are the responsibility of the Trust Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the State Treasury Asset Reserve of Ohio Investment Trust Fund and are not intended to present fairly the financial position of the State Treasury Asset Reserve of Ohio, and the results of its operations and changes in its net assets in conformity with accounting principles generally accepted in the United States of America.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the State Treasury Asset Reserve of Ohio Investment Trust Fund as of June 30, 2004, and the results of its operations and changes in its net assets for the years ended June 30, 2004 and 2003 in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis on page 2 is not a required part of the basic financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

This report is intended solely for the information and use of the Treasurer of the State of Ohio, the Auditor of the State of Ohio, and the Ohio Office of Budget and Management and is not intended to be and should not be used by anyone other than those specified parties.



July 28, 2004

# STATE TREASURY ASSET RESERVE OF OHIO INVESTMENT TRUST FUND

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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### Background

The State Treasury Asset Reserve of Ohio ("STAR Ohio" or "the Pool") is a statewide investment pool managed and administered by the Treasurer of the State of Ohio. Participation is offered to Ohio political subdivisions as a means to invest in a portfolio of short-term investment securities. The investment objective of STAR Ohio is to seek as high a level of current income as is consistent with prudent investment management, the preservation of capital and the maintenance of liquidity. STAR Ohio seeks to achieve these objectives by investing only in certain high-grade investment instruments. STAR Ohio is similar in concept to a registered investment company using redeemable securities, commonly called a "money market mutual fund."

The external portion of STAR Ohio, the State Treasury Asset Reserve of Ohio Investment Trust Fund ("Trust Fund"), is the portion that belongs to legally separate entities that are not part of the State of Ohio's financial reporting entity. STAR Ohio does not have separate investments or activities for the external portion of the investment pool. As a result, the financial condition and results of operations of the Trust Fund have been prepared by prorating the assets and liabilities related to the external portion. Our discussion and analysis below is based upon currently known facts and conditions that we judge to have had a material effect on the Trust Fund's financial condition and results of operations.

### Overview of Financial Condition

The targeted overnight federal fund rate remained at its historical low of 1.00% for the fiscal year ended June 30, 2004. Low interest rates and general economic conditions experienced by STAR Ohio participants during the year resulted in an approximate \$1.4 billion reduction in the investment portfolio due to a decline in net assets as shareholders redeemed funds.

### Overview of Operations

Net investment income as a percentage of average daily net assets declined to 1.00% in fiscal year 2004 from 1.44% in fiscal year 2003, resulting primarily from the federal funds targeted rate remaining at 1.00%. The weighted average yield of STAR Ohio's investment portfolio was 1.19% and 1.14% at June 30, 2004 and 2003, respectively.

\* \* \* \* \*

# STATE TREASURY ASSET RESERVE OF OHIO INVESTMENT TRUST FUND

## STATEMENT OF ASSETS AND LIABILITIES JUNE 30, 2004

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### ASSETS:

#### Investments:

Federal Agency issues	\$ 3,489,777,647
Commercial paper	476,955,285
Daily repurchase agreement	<u>25,666,340</u>
Total investments	3,992,399,272
Collateral on securities lent	<u>910,096,241</u>

Total assets 4,902,495,513

### LIABILITIES:

Obligation under security lending	910,096,241
Payable for fund shares redeemed	1,893,843
Accrued management fees	145,926
Accrued co-administrator fees	70,626
Accrued custodian fees	63,590
Other liabilities	<u>52,991</u>

Total liabilities 912,323,217

NET ASSETS \$ 3,990,172,296

See accompanying notes to financial statements.

# STATE TREASURY ASSET RESERVE OF OHIO INVESTMENT TRUST FUND

## STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

	2004	2003
STATEMENTS OF OPERATIONS:		
Investment income:		
Interest	\$ 52,598,921	\$ 92,385,410
Securities lending income	<u>843,065</u>	<u>56,562</u>
Total investment income	53,441,986	92,441,972
Investment expenses:		
Management fees	1,895,634	2,109,340
Co-administrator fees	1,015,131	1,260,267
Custodian and transfer agent fees	906,774	1,113,691
Security lending fees	176,169	15,118
Postage and printing fees	31,827	44,251
Audit fees	27,929	28,451
Standard & Poor's analytical fees	26,717	28,410
Telephone response fees	22,812	27,132
Miscellaneous	<u>77,976</u>	<u>61,544</u>
Total investment expense	<u>4,180,969</u>	<u>4,688,204</u>
NET INVESTMENT INCOME	<u>\$ 49,261,017</u>	<u>\$ 87,753,768</u>
STATEMENTS OF CHANGES IN NET ASSETS:		
OPERATIONS:		
Net investment income	\$ 49,261,017	\$ 87,753,768
DISTRIBUTIONS TO SHAREHOLDERS:		
Dividends to shareholders from net investment income	(49,261,017)	(87,753,768)
CAPITAL SHARE TRANSACTIONS—Net		
Decrease in net assets	<u>(1,376,733,630)</u>	<u>(914,964,728)</u>
NET ASSETS:		
Beginning of year	<u>5,366,905,926</u>	<u>6,281,870,654</u>
End of year	<u>\$ 3,990,172,296</u>	<u>\$ 5,366,905,926</u>

See accompanying notes to financial statements.

# STATE TREASURY ASSET RESERVE OF OHIO INVESTMENT TRUST FUND

## NOTES TO FINANCIAL STATEMENTS AS OF JUNE 30, 2004 AND FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

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### 1. SUMMARY OF ORGANIZATION

**Description of Fund**—The State Treasury Asset Reserve of Ohio (“STAR Ohio” or “Pool”) is a statewide investment pool managed by the Treasurer of the State of Ohio. Participation is offered to Ohio political subdivisions as defined in Section 135.45(F)(2)(a) of the Ohio Revised Code. STAR Ohio offers these subdivisions a means of investing in a portfolio of investment instruments. STAR Ohio seeks to obtain as high a level of current income as is consistent with prudent investment management, the preservation of capital, and maintenance of liquidity. There can be no guarantee that this will be achieved.

In accordance with Governmental Accounting Standards Board (“GASB”) Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, the State of Ohio (“State”) reports the external portion of STAR Ohio as a separate investment trust fund. The external portion of STAR Ohio (“Trust Fund”) is the portion that belongs to legally separate entities that are not part of the State’s financial reporting entity. The STAR Ohio investment pool does not have separate investments or activities for the external portion. The Statement of Assets and Liabilities of the Trust Fund has been prepared by prorating the assets and liabilities related to the external portion. Additionally, the Statements of Operations and Changes in Net Assets was prepared by prorating investment income and expenses related to the external portion using average daily balances.

**Legal Authority**—Section 135.45 of the Ohio Revised Code permits the State’s political subdivisions to pool their public funds into an investment fund managed by the State Treasurer and the State Treasurer’s staff of portfolio managers. STAR Ohio provides units of local government with an alternative investment option for their public funds.

**Investment Adviser and Administrator**—State Treasurer Joseph T. Deters, through the Investment Department, 30 East Broad Street, Ninth Floor, Columbus, Ohio 43215-3461, serves as investment adviser and administrator to STAR Ohio. The adviser manages the investment and reinvestment of STAR Ohio’s assets in accordance with STAR Ohio’s investment objectives and policies, subject to the general limitations of Section 135.143 of the Ohio Revised Code. In addition, the advisor is responsible for the overall management of STAR Ohio’s business affairs. STAR Ohio compensates the advisor with a flat management fee of \$500,000 per year.

**Co-Administrator**—Carnegie Capital Management Company, Cleveland, Ohio, is the co-administrator and provides certain clerical and administrative services for STAR Ohio. Compensation is based on a percentage of daily net assets.

**Custodian, Transfer Agent and Investment Consultant**—Provident Bank, Cincinnati, Ohio, is the dividend and transfer agent for STAR Ohio and also serves as custodian of its portfolio. All securities are held in the name of STAR Ohio on behalf of the Fund. Compensation is based on a percentage of net assets. Provident Bank was appointed investment consultant on July 1, 2001. Effective July 1, 2004,

Provident Bank was acquired by National City Corporation, Cleveland, Ohio. United American Capital Corporation, Worthington, Ohio, and Meeder Asset Management Inc., Dublin, Ohio assists Provident Bank with investment consulting services. The investment consulting fees are reflected in the management fees in the Statement of Operations. Compensation is based on a percentage of daily net assets.

## 2. SIGNIFICANT ACCOUNTING POLICIES

Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting*, the Trust Fund follows GASB guidance as applicable to proprietary funds and Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989 that do not conflict with or contradict GASB pronouncements.

***New Accounting Pronouncements***—During March 2003, the GASB issued Statement No. 40, *Deposit and Investment Risk Disclosures (an amendment of GASB Statement No. 3)*. This statement amends Statement No. 3 and addresses additional cash and investment risks to which governments are exposed. Generally, this statement requires that state and local governments communicate key information about such risks in four principal areas: investment credit risks, including credit quality information issued by rating agencies; interest rate disclosures that include investment maturity information; interest rate sensitivity for investments that are highly sensitive to changes in interest rates; and foreign exchange exposures that would indicate the foreign investment's denomination. The provisions of this statement are effective for financial statements for the fiscal year ended June 30, 2005. STAR Ohio does not believe the adoption of GASB No. 40 will have a material impact on its financial statement disclosures.

Effective July 1, 2003, the Trust Fund implemented GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*. The adoption of GASB Statement No. 39 did not have a material impact on the Trust Fund. As such, prior period financial statements have not been restated.

***Security Valuations***—Investment securities are valued using the amortized cost method (which approximates fair value) whereby a security is valued at cost adjusted for the amortization of any premiums or accretion of any discounts over the period until maturity.

***Security Transactions and Related Investment Income***—Security transactions are accounted for on the trade date (date order to buy or sell is executed). Interest income is determined on an accrual basis, with discounts earned (including original issue and market discount) being accreted and premiums paid being amortized. Realized gains and losses, if any, on sales of securities are calculated on the identified cost basis.

***Mark-to-Market Procedures***—The Pool maintains a stable net asset value per share by using the amortized cost method of portfolio valuation. The Pool has established procedures, reasonably designed, taking into account current market quotations, to stabilize the net asset value per share, as computed for the purpose of purchase and redemption, at a single value of \$1.00. The mark-to-market of the portfolio is used to monitor the appropriateness of the amortized cost method and is calculated using available market quotations.

***Federal Income Taxes***—STAR Ohio is not subject to income taxes.



*Use of Estimates*—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

### **3. INVESTMENT SECURITIES**

*Repurchase Agreements and Commercial Paper*—STAR Ohio is permitted to invest in commercial paper, but shall not exceed 10% of the average net assets on an annualized basis. Commercial paper holdings when purchased represent 10% or less of the average net assets on an annualized basis. As of June 30, 2004, commercial paper holdings represented 12% of the net assets, due to a decline in net assets by year end.

All repurchase agreements are fully collateralized by United States Government or Federal Agency securities, pursuant to Section 135.143 of the Ohio Revised Code, and such collateral is in the possession of STAR Ohio's custodian. STAR Ohio evaluates collateral daily to ensure its market value plus accrued interest exceeds the delivery value of the repurchase agreement at maturity. STAR Ohio does not enter into reverse repurchase (borrowing) agreements.

In accordance with GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, STAR Ohio is required to classify its investments into categories of custodial risk. Category 1 includes investments that are insured or registered for which the securities are held by STAR Ohio or by its agent in the name of STAR Ohio. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the name of STAR Ohio. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty or by its trust department or agent but not in STAR Ohio's name. All investments of STAR Ohio, including collateral on securities lent, meet the criteria of Category 1, except securities on loan, which by their nature are not required to be so categorized.

### **4. SECURITIES LENDING**

Pursuant to ORC 135.143, the Pool may lend up to 25% of its securities to any eligible financial institution that is a member of the Federal Reserve System or any recognized United States government securities dealer. Under the terms of the lending agreement, STAR Ohio lends securities and the eligible financial institution or primary dealer agrees to simultaneously exchange similar securities or cash. At June 30, 2004, collateral on securities lent consisted of commercial paper, repurchase agreements and variable rate notes. STAR Ohio may not pledge or sell the securities received in exchange. STAR Ohio receives payments from borrowers equivalent to the interest that would have been earned on securities lent while simultaneously seeking to earn interest on the investment of cash collateral. The income from this program is distributed daily. STAR Ohio calculates a mark-to-market review of collateral daily to ensure its market value is at least 100% of the underlying securities lent. At year-end, the Pool has no credit risk exposure to the borrowers because the amounts the Pool owes the borrower exceeds the amounts the borrowers owe the Pool.

The Pool follows strict levels of collateralization governed by daily mark-to-market analysis, a review of the credit worthiness of securities dealers and banks, and strict monitoring of their respective credit limits. This is done to control exposure due to possible credit loss resulting from a reduction in the underlying collateral value or non-performance by a security dealer or bank. Either the Pool or the borrower can terminate all security loans on demand.

As of June 30, 2004, the amortized cost and fair value of securities available for securities lending allocated to the Trust Fund were \$3,351,812,413 and \$3,349,348,882, respectively, of which the following were actually lent:

	<b>Amortized Cost</b>	<b>Fair Value</b>
Federal Home Loan Bank Discount Notes	\$ 78,695,020	\$ 78,710,631
Federal Home Loan Mortgage Corp. Discount Notes	354,338,638	354,018,048
Federal National Mortgage Association Discount Notes	<u>474,291,463</u>	<u>474,035,291</u>
Total	<u>\$ 907,325,121</u>	<u>\$ 906,763,970</u>

The collateral at year end for the lent securities included commercial paper, agency repurchase agreements, and variable rate notes; the Trust Fund's fair market values were \$94,748,253, \$623,287,776, and \$192,060,212, respectively. No losses were incurred during the year on the Pool's securities lending transactions from the default of a borrower or lending agent.

## 5. INCOME DISTRIBUTIONS

STAR Ohio declares a distribution each business day to distribute its net investment income and realized capital gains, if any. All such distributions are automatically reinvested in additional shares of the Pool.

## 6. CAPITAL SHARES

Transactions in capital shares (all at \$1.00 per share) were as follows:

	<u>Year Ended June 30,</u>	
	<b>2004</b>	<b>2003</b>
Shares sold	\$ 17,130,626,004	\$ 20,743,363,855
Shares issued for reinvestment of distributions	<u>49,261,017</u>	<u>87,753,768</u>
	17,179,887,021	20,831,117,623
Shares redeemed and other transactions	<u>(18,556,620,651)</u>	<u>(21,746,082,351)</u>
Capital share transactions—net decrease	<u>\$ (1,376,733,630)</u>	<u>\$ (914,964,728)</u>

\* \* \* \* \*

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON  
INTERNAL CONTROL OVER FINANCIAL REPORTING BASED  
ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN  
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

The Honorable Joseph T. Deters  
Treasurer of State

The Honorable Betty Montgomery  
Auditor of State:

We have audited the financial statements of the State Treasury Asset Reserve of Ohio ("STAR Ohio") as of and for the year ended June 30, 2004, and have issued our report thereon dated July 28, 2004. 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 *Governmental Auditing Standards*, issued by the Comptroller General of the United States.

### **Compliance**

As part of obtaining reasonable assurance about whether STAR Ohio's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on 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 such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

### **Internal Control Over Financial Reporting**

In planning and performing our audit, we considered STAR Ohio's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Treasurer of the State of Ohio and the Auditor of the State of Ohio and is not intended to be and should not be used by anyone other than these specified parties.

The logo for Deloitte & Touche LLP, featuring the company name in a stylized, handwritten-style script.

July 28, 2004





**Auditor of State  
Betty Montgomery**

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800-282-0370

Facsimile 614-466-4490

**STAR OHIO**

**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 7, 2004**