

MANAGEMENT'S DISCUSSION AND ANALYSIS



STATE OF INDIANA
Management's Discussion and Analysis
June 30, 2013

The following discussion and analysis of the State of Indiana's financial performance provides an overview of the State's financial activities for the fiscal year ended June 30, 2013. Please read it in conjunction with the transmittal letter at the front of this report and the State's financial statements, which follow this section. Because of prior period adjustments and reclassifications as described in Note IV(G) in the Notes to the Financial Statements, fiscal year (FY) 2012 numbers have been restated.

Financial Highlights

- For FY 2013, on a government-wide basis, the assets of the State of Indiana exceeded its liabilities by \$18.7 billion. This compares with \$17.7 billion for FY 2012, as restated. Of this amount, \$4.4 billion may be used to meet the government's ongoing obligations to citizens and creditors.
- At the end of the current fiscal year, unassigned fund balance for the general fund was \$1.8 billion, or 14.5% of the total general fund expenditures.
- On a government-wide basis for the primary government, the State incurred expenses net of program revenue of \$14.1 billion, which are offset by general revenues totaling \$15.1 billion, giving an increase in net position of \$1.0 billion.
- General revenue for the primary government increased by \$0.3 billion, or 1.9%, from FY 2012. Sales tax revenues increased by \$324.6 million indicating the Indiana economy continued to recover from the recession.
- Combined budget balances for FY 2013 were maximized at \$1,943.1 million. A transfer to the Pension Stabilization Fund would have been triggered had the combined balances reached \$1,944.1 million. Reaching \$1,944.1 would have reduced balances back to \$1,894.1 million. The balance of \$1,943.1 million consists of \$1,428.0 million in the General Fund, \$145.0 million in the Medicaid Contingency Reserve Fund, and \$370.1 million in the Rainy Day Fund.
- Indiana's debt has decreased by over 50% since FY 2005. In FY 2013, \$163 million of bonds were defeased, and \$91.2 million of loans for charter schools were paid back.
- Indiana is one of only nine states with the top bond rating from all three major credit rating agencies. According to the independent credit rating agency Standard & Poor's Ratings Service (S&P), the rating "reflects the state's continued strong management that has led to the property tax reform that has realigned state and local spending and is not expected to impact the state's long-term financial performance. As well, the state's commitment to attract diverse jobs through its economic development efforts has translated into a shift away from traditional manufacturing employment." The report said the administration has made significant financial management changes and strengthened budgeting practices.

Key Economic Indicators

	<u>Dec. 31, 2012</u>	<u>Dec. 31, 2011</u>	<u>% Change</u>
Total Employed Labor Force	3,131,947	3,148,639	-0.5%
Total Goods and Service Employment	2,936,600	2,893,000	1.5%
Service-Providing Employment	2,325,700	2,293,700	1.4%
Goods-Producing Employment	610,900	599,300	1.9%
Unemployment Rate	8.5%	8.6%	-1.2%
Median Household Income	46,974	46,438	1.2%

Sources: Indiana Department of Workforce Development, Bureau of Labor Statistics, and U.S. Census Bureau.

Salaries and benefits for State employees represent approximately 8.0% of governmental fund expenditures. The following table shows a ten year history of the count of full time State employees.

Full Time State Employees Paid Through The Auditor of State's Office

	<u>Governor's Authority</u>	<u>Judiciary</u>	<u>Other Elected Officials</u>	<u>On Disability Leave - In Pay Status</u>	<u>On Disability Leave - Not in Pay Status</u>	<u>Total</u>
2013	28,398	831	1,049	511	345	31,134
2012	28,485	835	1,049	545	349	31,263
2011	28,472	830	1,067	610	351	31,330
2010	29,911	846	1,056	647	341	32,801
2009	31,254	835	1,093	624	358	34,164
2008	32,606	811	1,139	727	339	35,622
2007	31,524	772	1,123	789	313	34,521
2006	31,822	753	1,102	941	279	34,897
2005	34,673	743	1,058	1,077	269	37,820
2004	35,794	756	1,020	1,012	266	38,848

For more information on personnel paid through the Auditor of State's Office, please read the Statistical Section.

Overview of the Financial Statements

This Financial Section consists of four parts: management's discussion and analysis (this part), the basic financial statements, required supplementary information, and other supplementary information. The basic financial statements include two kinds of statements that present different views of the State. The first two statements are government-wide financial statements that provide both long-term and short-term information about the State's overall financial status.

The remaining statements are fund financial statements that focus on individual parts of the State government, reporting the State's operations in more detail than the government-wide statements.

- The governmental fund statements tell how general government services such as public safety, education, and welfare were financed in the short term as well as what remains for future spending.
- Proprietary fund statements offer short and long-term financial information about the activities the government operates like businesses, such as the Unemployment Compensation Fund.
- Fiduciary fund statements provide information about the financial relationships in which the State acts solely as a trustee or agent for the benefit of others, to whom the resources in question belong, such as the retirement plan for the State's employees.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of *required supplementary information* and *other supplementary information* that further explain and support the information in the financial statements.

Government-wide Financial Statements

The government-wide financial statements report information about the State as a whole using accounting methods similar to those used by private-sector companies. The statement of net position includes all the government's assets, deferred outflows of resources, liabilities, and deferred inflows of resources. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the State's net position and how they have changed. Net position which equals the State's assets, plus deferred outflows of resources, less liabilities, less deferred inflows of resources, is one way to measure

the State's financial health, or position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the State of Indiana is improving or deteriorating. To assess the overall health of the State, additional non-financial factors should be considered, such as changes in the State's tax base, the condition of the State's roads and the State's student population. The government-wide financial statements of the State are divided into three categories:

- **Governmental activities.** Most of the State's basic services are included here, such as the State's roads and bridges, and health and environmental programs. State sales and income taxes and federal grants finance most of these activities.
- **Business-type activities.** The State provides goods and services through these activities that are financed or recovered primarily through fees and user charges. The Unemployment Compensation Fund, the Inns and Concessions Fund, the Indiana Residual Malpractice Insurance Authority, and the Wabash Memorial Bridge Fund are included here.
- **Discretely Presented Component Units.** These are legally separate discretely presented entities for which the State is financially accountable. These include, among others, the Indiana Finance Authority, the State Lottery Commission of Indiana, the Indiana Bond Bank, the Indiana Housing and Community Development Authority, and colleges and universities that receive State funding.

Fund Financial Statements

The fund financial statements provide more detailed information about the State's most significant funds, not the State as a whole. Funds are accounting devices that the State uses to keep track of specific sources of funding and spending for particular purposes. The State of Indiana uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The State has three kinds of funds: governmental funds, proprietary funds, and fiduciary funds.

1. **Governmental funds.** Most of the State's basic services are included in governmental funds, which focus on (1) cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a

detailed short-term view that helps the reader determine whether there are more or fewer financial resources that can be spent in the near future to finance the State's programs.

Relationship and Reconciliation. Because the information provided in the governmental funds statements does not encompass the additional long-term focus of the government-wide statements, reconciliation pages are provided. On the page following each governmental fund's financial statement, these reconciliations explain the differences between the government-wide and the fund financial statement. Government-wide statements use full accrual accounting. Revenues are recognized when they are earned and expenses are recognized as soon as the liability is incurred, regardless of the timing of related cash inflows and outflows. Governmental fund financial statements use the modified accrual basis of accounting. Revenues are recognized when earned so long as they are collectible within the current period or soon enough afterwards to pay liabilities of the current period. Debt service payments and a number of specific accrued liabilities are recognized as expenditures when payment is due because that is when they are normally liquidated with expendable available financial resources.

Non-current assets such as infrastructure, land, and property, plant and equipment appear on the government-wide statements but not on the governmental fund statements where they are expensed as acquired rather than capitalized. Non-current liabilities such as revenue bonds payable and net pension obligations also appear on the government-wide statements but not on the fund statements. Internal service funds are

included as part of the governmental activities in the government-wide statements but not the governmental fund financial statements because they provide services to the governmental funds.

2. **Proprietary funds.** Services for which the State charges customers a fee are generally reported in proprietary funds. These funds use the economic resources measurement focus and the accrual basis of accounting. Proprietary funds, like the government-wide statements, provide both long-term and short-term financial information. In fact, the State's enterprise funds (one type of proprietary fund) are the same as its business-type activities, but provide more detail and additional information such as cash flows. The State uses internal service funds (the other type of proprietary fund) to report activities that provide supplies and services for the State's other programs and activities. An example would be the State Employee Health Insurance Fund.
3. **Fiduciary funds.** The State is the trustee, or fiduciary, for its employees' pension plans. It is also responsible for other assets that, because of a trust arrangement, can be used only for the trust beneficiaries. The State is responsible for ensuring that the assets reported in these funds are used for their intended purposes. Fiduciary funds use the economic resources measurement focus and the accrual basis of accounting. All of the State's fiduciary activities are reported in a separate statement of fiduciary net position and a statement of changes in fiduciary net position. These activities are excluded from the State's government-wide financial statements because the State cannot use these assets to finance its operations.

Financial Analysis of the State as a Whole

Net Position

The following is condensed from the Statement of Net Position:

State of Indiana Condensed Schedule of Net Position (in millions of dollars)						
Primary Government						
	Governmental Activities		Business-type Activities		Total Primary Government	
	2013	2012	2013	2012	2013	2012
Current and other assets	\$ 10,856.6	\$ 11,289.2	\$ 238.9	\$ 251.3	\$ 11,095.5	\$ 11,540.5
Capital assets	14,526.2	13,385.4	0.7	0.7	14,526.9	13,386.1
Total assets	<u>25,382.8</u>	<u>24,674.6</u>	<u>239.6</u>	<u>252.0</u>	<u>25,622.4</u>	<u>24,926.6</u>
Current liabilities	2,842.2	2,661.2	1,421.7	1,776.3	4,263.9	4,437.5
Long-term liabilities	2,671.1	2,795.1	29.1	26.6	2,700.2	2,821.7
Total liabilities	<u>5,513.3</u>	<u>5,456.3</u>	<u>1,450.8</u>	<u>1,802.9</u>	<u>6,964.1</u>	<u>7,259.2</u>
Net position:						
Net investment in capital assets	13,373.2	12,175.4	0.7	0.7	13,373.9	12,176.1
Restricted	899.2	883.9	-	-	899.2	883.9
Unrestricted	5,597.1	6,158.9	(1,211.9)	(1,551.5)	4,385.2	4,607.4
Total net position	<u>\$ 19,869.5</u>	<u>\$ 19,218.2</u>	<u>\$ (1,211.2)</u>	<u>\$ (1,550.8)</u>	<u>\$ 18,658.3</u>	<u>\$ 17,667.4</u>

At the end of the current fiscal year, net position for the primary government was \$18.7 billion as compared to \$17.7 billion in 2012. There was an increase of \$1.0 billion.

Current and other assets decreased by \$445.0 million with decreases in cash making up the bulk of this. Statutory automatic taxpayer refunds of \$360.6 million and distributions to pension funds of \$360.6 million were made in fiscal year 2013 due to the State's budgetary reserve balance at the end of fiscal year 2012.

Capital assets increased by \$1,140.8 million. The principal reason for the increase in capital assets was the increase in land, infrastructure, and construction in progress at the Indiana Department of Transportation of \$816.2 million primarily due to the State's Major Moves initiative. In addition, assets were acquired through the defeasance of bonds in the amount of \$345.7 million.

Total liabilities decreased by \$295.1 million. This decrease is due to the reduction of the amount due to the federal government for unemployment compensation benefits of \$339.5 million.

Changes in Net Position

The following is condensed from the Statement of Activities:

State of Indiana Condensed Schedule of Change in Net Position (in millions of dollars)						
	Primary Government					
	Governmental Activities		Business-type		Total Primary	
	Activities	Activities	Activities	Activities	Government	Government
	2013	2012	2013	2012	2013	2012
Revenues						
Program revenues:						
Charges for services	\$ 2,299.4	\$ 2,252.6	\$ 857.0	\$ 1,010.7	\$ 3,156.4	\$ 3,263.3
Operating grants and contributions	11,607.7	11,065.6	670.5	1,043.9	12,278.2	12,109.5
Capital grants and contributions	-	-	0.1	-	0.1	-
General revenues:						
Individual and corporate income taxes	5,371.0	5,424.3	-	-	5,371.0	5,424.3
Sales taxes	6,845.3	6,520.7	-	-	6,845.3	6,520.7
Other	2,906.4	2,892.7	-	3.8	2,906.4	2,896.5
Total revenues	29,029.8	28,155.9	1,527.6	2,058.4	30,557.4	30,214.3
Program Expense						
General government	1,476.1	2,642.9	-	-	1,476.1	2,642.9
Public safety	1,526.6	1,330.3	-	-	1,526.6	1,330.3
Health	409.3	305.2	-	-	409.3	305.2
Welfare	12,546.9	11,157.8	-	-	12,546.9	11,157.8
Conservation, culture and development	555.7	589.3	-	-	555.7	589.3
Education	10,136.8	10,277.5	-	-	10,136.8	10,277.5
Transportation	1,729.7	1,533.6	-	-	1,729.7	1,533.6
Interest expense	0.2	0.7	-	-	0.2	0.7
Unemployment compensation fund	-	-	1,160.6	1,893.9	1,160.6	1,893.9
Other	-	-	24.6	22.7	24.6	22.7
Total expenses	28,381.3	27,837.3	1,185.2	1,916.6	29,566.5	29,753.9
Excess (deficiency) before transfers	648.5	318.6	342.4	141.8	990.9	460.4
Transfers	2.8	2.1	(2.8)	(2.1)	-	-
Change in net position	651.3	320.7	339.6	139.7	990.9	460.4
Beginning net position, as restated	19,218.2	18,897.5	(1,550.8)	(1,690.5)	17,667.4	17,207.0
Ending net position	\$ 19,869.5	\$ 19,218.2	\$ (1,211.2)	\$ (1,550.8)	\$ 18,658.3	\$ 17,667.4

Governmental Activities

Program expenses exceeded program revenues by \$14.5 billion. General revenues and transfers were \$15.1 billion. The increase in net position was \$.7 billion, which is 2.2% of total revenues and 2.3% of total expenses.

The increase to excess (deficiency) before transfers was \$648.5 million.

Revenues increased mainly because of the increase in program revenues from operating grants and contributions (PR-OGC) of \$542.1 million. Medicaid PR-OGC revenues increased \$703.8 million from an increase in federal grant revenues as a result of the leveraging effect on funding from increases in fees

paid by providers. This was partially offset by a decrease in grant revenue of \$164.2 million from the U.S. Department of Education. Also contributing to the increase in revenues was the increase in sales tax revenues of \$324.6 million.

Expenses increased by \$0.5 billion or 2.0%. General Government expenses decreased by \$1.2 billion. Some reasons for this decrease were reductions of \$695.2 million for accruals and distributions to local governments, \$346.1 million due to reclassification of local government distributions from general government to the transportation function, \$288.1 million from capital assets acquired as a result of bond defeasance, and from other

accruals and adjustments such as for intergovernmental payables, \$35.5 million, and accounts payable, \$32.9 million.

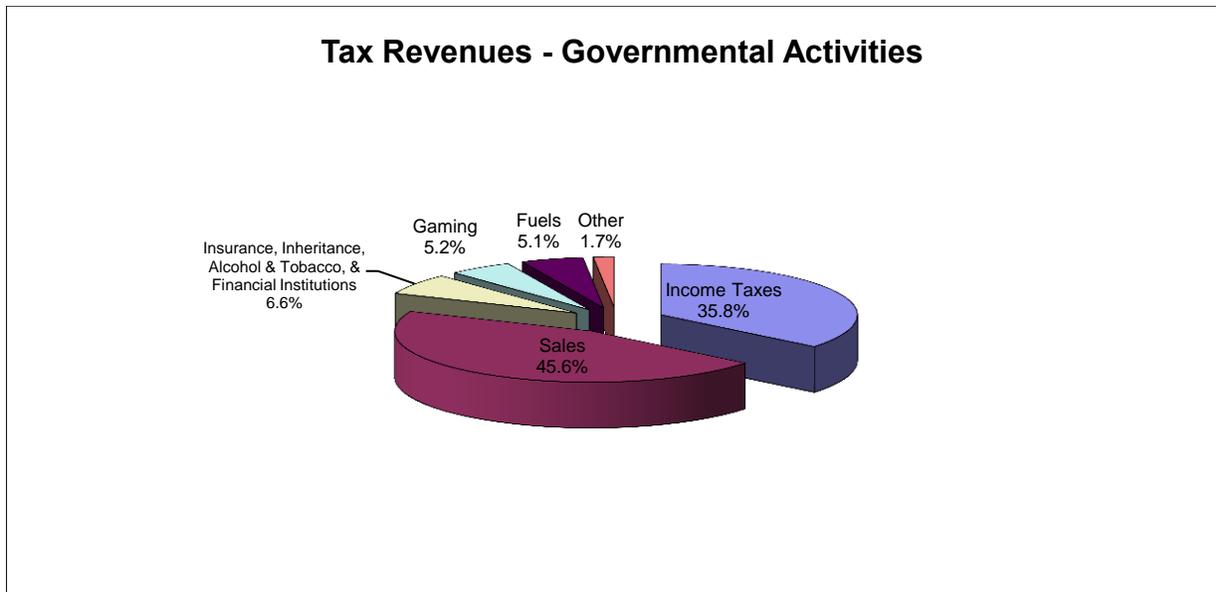
Welfare expenses increased by \$1.4 billion due to increases in hospital payments (including managed care payments for the hospital portion of the capitation payment) and nursing facility payments due to rate increases as part of provider assessment programs and increases in Supplemental payments of the Public Welfare-Medicaid Assistance Fund.

Public safety expenditures increased by \$196.3 million primarily because of increases of \$41.3 million in the Adjutant General's U.S. Department of

Defense programs, \$41.1 million in claims and judgments for the Patients Compensation Fund, and \$20.7 million for payment relating to the usage contract for the New Castle Correctional Facility.

Transportation expenditures increased by \$196.1 million primarily due to a reclassification of local government distributions from general government to the transportation function.

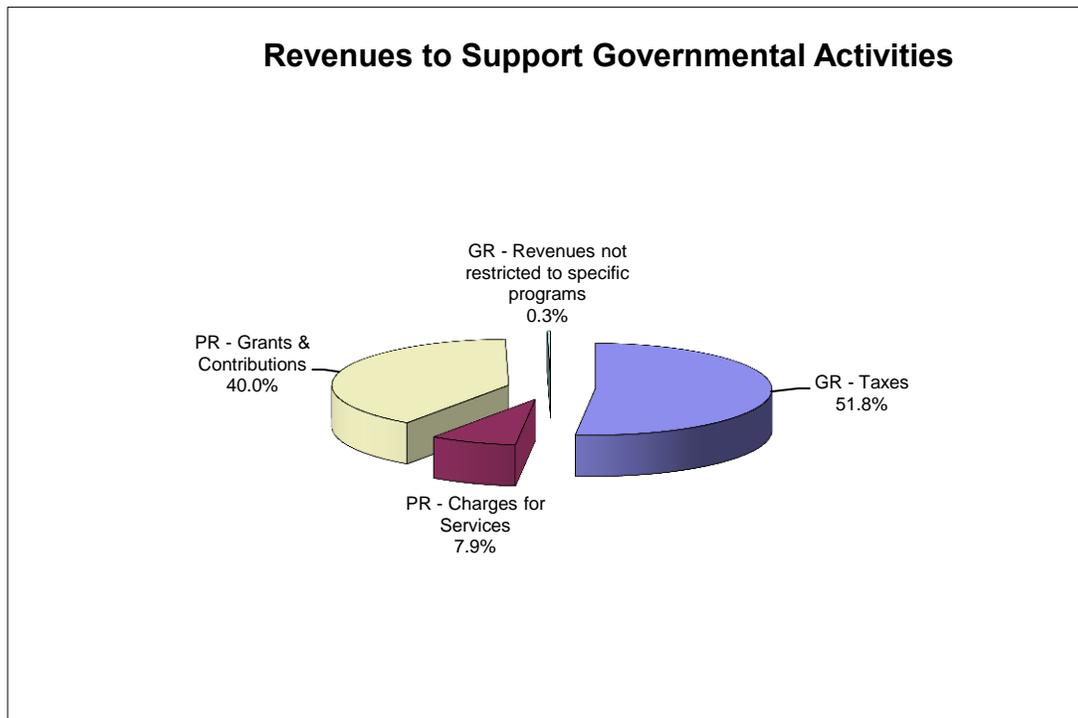
Tax revenues for governmental activities were broken down as follows:



Tax revenues of \$15.0 billion represent 51.8% of total revenues for governmental activities. This compares to \$14.7 billion in FY 2012 or 52.3% of total revenues in FY 2012. Program revenues accounted for \$13.9 billion or 47.9% of total revenues. In FY 2012, program revenues accounted for \$13.3 billion or 47.3% of total revenues. General revenues other than tax revenues were \$86.9 million or 0.3% of total

revenues. Of this \$28.0 million was investment earnings. This compares to 2012, when general revenues other than taxes were \$106.4 million or 0.4% of total revenues and \$16.3 million was investment earnings. Investment earnings increased by \$11.6 million from FY 2012 to FY 2013 or 71.2% due to higher interest rates and increased securities lending activity.

Total revenues for governmental activities were broken down as follows:



PR = program revenues
GR = general revenues

Total revenues were 102.3% of expenses which was an increase from 101.1% in FY 2012. Total revenues increased 2.8% from \$28.2 billion in FY 2012 to \$29.0 billion in FY 2013. Expenses grew 2.2% from \$27.8 billion in FY 2012 to \$28.4 billion in FY 2012.

The largest portion of the State's expenses is for Welfare, which is \$12.5 billion, or 44.2% of total expenses. This compares with \$11.2 billion, or 40.1% of total expenses in FY 2012. The change in expenses was an increase of \$1.4 billion or 12.4%. \$3.1 billion of Welfare expenses in FY 2013 were funded from general revenues.

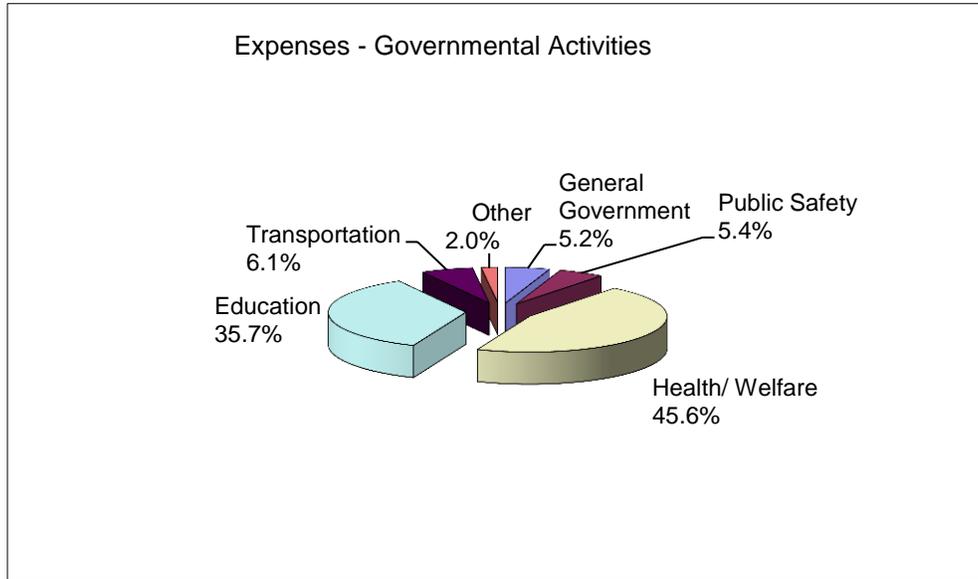
Some of the major expenses were Medicaid assistance, \$8.3 billion, the federal food stamp program in the U.S. Department of Agriculture Fund, \$1.6 billion, and the U.S. Department of Health and Human Services Fund, \$1.3 billion.

Education comprises 35.7%, or \$10.1 billion of the State's expenses. In FY 2012, Education accounted for 36.9%, or \$10.3 billion, of expenses. The change in expenses was a decrease of \$0.1 billion, or 1.4%. Some of the major expenses were tuition support,

\$6.3 billion, General Fund appropriations for State colleges and universities, \$1.4 billion, Teachers' Retirement Pension, \$700.0 million, federal grant programs from the U.S. Department of Education Fund, \$654.2 million, federal grant programs from the U.S. Department of Agriculture Fund, \$359.8 million, full day kindergarten, \$190.2 million, and post-retiree pensions, \$67.2 million.

\$1.5 billion, or 5.2% of expenses, was spent for General Government. General Government comprised \$2.6 billion or 9.5% of expenses in FY 2012. General Government includes local distributions and money for State administration and those functions that serve the State as a whole. Some reasons for the decrease were decreases in expenditures for local government distributions, capital assets, prepaid expenses, intergovernmental payables, accounts payable, and capital leases. In addition, transportation expenditures were reclassified from general government to transportation during FY 2013.

Total expenses for governmental activities were broken down as follows:



Business-type Activities

Business-type activities represent 5.0% of the Primary Government’s revenues and 4.0% of the expenses. The Unemployment Compensation Fund accounts for 98.3% of business-type activities’ operating revenues and 98.3% of operating expenses. The change in net position for business-type activities was an increase of \$339.5 million.

The Unemployment Compensation Fund collects employer taxes and the federal share of unemployment compensation. Benefits are paid to eligible individuals and the fund covers general and administrative expenses. Revenue in the fund exceeded benefits and administrative expenses paid by \$340.5 million. This compares to FY 2012 when this fund’s revenues exceeded expenses by \$133.4 million. Employer contributions into the fund

decreased by \$0.2 billion, from \$1.0 billion in FY 2012 to \$.8 billion in FY 2013. Federal revenues into the fund decreased by \$0.3 billion, from \$1.0 billion in FY 2012 to \$0.7 billion in FY 2013. The increase in the net position is due to three main factors. FUTA credit reduction revenues increased 61% from FY 2012 as the credit reduction for Indiana employers increased by 0.3%. Additional revenue received by the U.S. Treasury as a result of this credit reduction is deposited into Indiana’s UI trust fund as principal repayment on the title XII loan. Additionally, the surcharge collections from Indiana employers necessary to pay the accrued interest on the title XII loan were decreased by 27% as a result of reduced interest expense. Finally, State UI benefit expenses decreased by 21% in FY 2013.

The following schedule shows the net expense (revenue) attributable to each function of government. Each function of Indiana government is either self-supporting (a negative number) or requires additional general revenues to cover expenses (a positive number).

Net Cost of Primary Government (in millions of dollars)			
	June 30, 2013	June 30, 2012	% Change
Governmental Activities:			
General government	\$ 846.2	\$ 1,606.7	-47.3%
Public safety	851.9	698.0	22.0%
Health	87.9	53.5	64.3%
Welfare	3,095.8	2,654.1	16.6%
Conservation, culture, and development	136.1	160.5	-15.2%
Education	9,094.1	9,092.0	0.0%
Transportation	361.9	253.6	42.7%
Unallocated interest expense	0.2	0.7	-71.4%
Business-type Activities:			
Unemployment Compensation Fund	(340.5)	(133.4)	155.2%
Malpractice Insurance Authority	0.7	(0.1)	-800.0%
Inns and Concessions	(3.0)	(4.5)	-33.3%
Wabash Memorial Bridge	0.5	-	100.0%
Total	\$ 14,131.8	\$ 14,381.1	-1.7%

Financial Analysis of the State's Funds

The following is an analysis of the State's major governmental funds. Please note that transfers in and transfers out for these funds are explained in much greater detail in note IV(B) in the Notes to the Financial Statements.

General Fund

The General Fund is maintained to account for resources obtained and used for those services traditionally provided by State government which are not required to be accounted for in another fund. The fund balance of the General Fund at June 30, 2013 was \$3.3 billion, which is 73.3% of assets. This compares to a fund balance at June 30, 2012 of \$3.4 billion, which was 79.9% of assets. This indicates that the State's financial position in the General Fund decreased from the prior year by \$52.9 million. The fund balance of \$3.3 billion is composed of restrictions of \$378.6 million, commitments of \$6.0 million, and assignments of \$1.2 billion, leaving an unassigned balance of \$1.8 billion. The restricted amount consists of the State's Rainy Day Fund. For more information on the components of fund balance, see the chart in the Notes to the Financial Statements III(B).

The General Fund's revenues decreased 1.6%, or \$220.8 million, from FY 2012, because of the decrease in total tax revenue which included a \$381.5 million (5.7%) decrease in income tax offset by a \$167.9 million (2.5%) increase in sales tax. The decrease in tax revenues is explained by a decrease in income tax revenue due to the statutory automatic taxpayer refund.

General Fund expenditures increased \$350.0 million, or 3.0% from FY 2012. Statutory distributions to pension funds was the reason for the increase in expenditures.

General Fund transfers in held steady at \$1.7 billion for both FY 2012 and FY2013. Transfers out were \$3.2 billion in FY 2013 as compared to \$3.4 billion in

FY 2012. More detail on these transfers can be found in the Notes to the Financial Statements IV(B).

Overall, the net position of the General Fund decreased by \$52.9 million.

Public Welfare-Medicaid Assistance Fund

Medicaid is an insurance program for low-income people. It is jointly funded by the Federal government and the State. The Medicaid Assistance Fund received \$5.7 billion in Federal revenue as compared to \$5.0 billion in FY 2012. State funding comes through the \$2.0 billion of transfers in from the General Fund and was the same in FY 2012. Transfers out were \$565.3 million compared with \$177.7 million in FY 2012. The Fund distributed \$8.3 billion in Medicaid assistance during the year, which is an increase of \$1.0 billion over FY 2012. The change in fund balance decreased by \$39.2 million from FY 2012 to FY 2013.

Major Moves Construction Fund

The Major Moves Construction Fund was created in fiscal year 2006 as part of the leasing of the Indiana Toll Road to Cintra-Macquarie, a private company. This fund distributes money received from the Toll Road lease for new constructions and major preservation of highways and bridges throughout Indiana.

The Major Moves Construction Fund transferred \$412.7 million to the State Highway Fund. The fund received \$15.8 million in investment income and made a distribution of \$10.0 million to the Northwest Indiana Regional Development Authority. The change in fund balance from FY 2012 to FY 2013 was a decline of \$407.4 million.

General Fund Budgetary Highlights

Actual State general fund revenue collections increased by \$337.0 million, or 2.4%, in FY 2013. Actual expenditure growth was 3.7% in FY 2013 compared with growth of nearly 5.9% between FY 1996 and FY 2004. At year-end, the State had \$1.9 billion in reserves, with \$1.4 billion residing in the

general fund, \$145 million in the Medicaid Reserve Fund, and \$370.1 million residing in the Rainy Day Fund.

Capital Asset and Debt Administration

Capital Assets

Capital assets were \$14.5 billion, which was 57.1% of total assets for the primary government. Related debt was \$1.1 billion. Net investment in capital assets for the primary government was \$13.4 billion. Related debt was 7.6% of capital assets. Total capital assets increased by \$1.1 billion or 8.5% and is attributable to increases in the Indiana Department of Transportation's land, infrastructure, and construction in progress (CIP). The net increase in capital assets is comprised of increases for INDOT's capital assets of \$816.2 million, software in development of \$5.7

million, capital assets of the primary government of \$314.0 million, and with decreases of \$12.3 million in capital lease assets, \$1.9 million in DOA Public Works CIP, and \$1.9 million in internal service funds' capital assets. INDOT's \$816.2 million increase is comprised of CIP consisting of right of way and work in progress, \$388.7 million, infrastructure consisting of interstate roads, non-interstate roads, and bridges, \$343.7 million, and land, \$83.8 million. More detailed information about the State's capital assets is presented in Note IV(D) to the Financial Statements.

The following table shows the percentage change from fiscal year 2012 to fiscal year 2013.

State of Indiana Capital Assets (in millions of dollars)							
	Governmental Activities		Business-type Activities		Total Primary Government		Total % Change
	2013	2012	2013	2012	2013	2012	
Land	\$ 1,854.9	\$ 1,734.2	\$ -	\$ -	\$ 1,854.9	\$ 1,734.2	7.0%
Infrastructure	9,290.0	8,946.8	-	-	9,290.0	8,946.8	3.8%
Construction in Progress	2,193.0	1,779.5	-	-	2,193.0	1,779.5	23.2%
Property, plant and equipment	2,669.1	2,150.7	1.1	1.3	2,670.2	2,152.0	24.1%
Computer software	45.8	40.1	-	-	45.8	40.1	14.1%
Less accumulated depreciation	(1,526.6)	(1,265.9)	(0.4)	(0.6)	(1,527.0)	(1,266.5)	20.6%
Total	\$ 14,526.2	\$ 13,385.4	\$ 0.7	\$ 0.7	\$ 14,526.8	\$ 13,386.1	8.5%

Long-term Obligations

Major long-term obligations items are included in the following table. These items comprised 100% of total long-term liabilities and 38.8% of total liabilities.

The following table shows the percentage change from fiscal year 2012 to fiscal year 2013.

State of Indiana Long-term Liabilities (in millions of dollars)							
	Governmental Activities		Business-type Activities		Total Primary Government		Total % Change
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>	
Accrued liability for compensated absences	\$ 148.6	\$ 138.4	\$ 0.5	\$ 0.5	\$ 149.1	\$ 138.9	7.3%
Intergovernmental payable	20.0	30.0	-	-	20.0	30.0	-33.3%
Capital lease payable	1,156.9	1,210.0	-	-	1,156.9	1,210.0	-4.4%
Claims payable	-	-	28.6	30.2	28.6	30.2	-5.3%
Net pension obligations	1,166.8	1,344.3	-	-	1,166.8	1,344.3	-13.2%
Other postemployment benefits	134.1	119.6	-	-	134.1	119.6	12.1%
Pollution remediation	44.7	46.0	-	-	44.7	46.0	-2.8%
Total	<u>\$ 2,671.1</u>	<u>\$ 2,888.3</u>	<u>\$ 29.1</u>	<u>\$ 30.7</u>	<u>\$ 2,700.2</u>	<u>\$ 2,919.0</u>	<u>-7.5%</u>

Total long-term liabilities decreased by 7.5% or \$218.8 million. The largest decrease was in net pension obligations of \$177.4 million. Other long-term liabilities to decrease were capital leases by \$53.1 million, and intergovernmental payables by \$10.0 million.

The decrease in net pension obligations is due to the statutory transfer of \$360.6 million from the State's General Fund.

The decrease in capital leases was mainly due to the payments on the direct financing lease between INDOT and IFA and the early buy out of a warehouse maintained by the Department of Administration.

Infrastructure

As required by GASB Statement No. 34, the State has capitalized its infrastructure. This amounts to \$9.3 billion in roads and bridges using the modified approach, \$1.6 billion in right of way classified as land, and \$22.1 million in property (septic, sewer, and water systems; and streets/sidewalks/curbs) and dams being depreciated. In order to utilize the modified approach, the State is required to:

- Maintain an asset management system that includes an up-to-date inventory of eligible infrastructure assets.

A significant increase in long-term liabilities was for other postemployment benefits which increased by \$14.5 million. This increase in OPEB liability is based on the OPEB financial report for the fiscal year ending June 30, 2013.

Claims payable for business activities decreased by \$1.6 million. This was the amount of decrease in claims payable for the Indiana Residual Malpractice Insurance Authority.

More detailed information about the State's long term obligations is presented in Note IV(F) to the Financial Statements.

- Perform condition assessments of eligible assets and summarize the results using a measurement scale.
- Estimate each year the annual amount to maintain and preserve the assets at the condition level established and disclosed by the State.
- Document that the assets are being preserved approximately at or above the established condition level.

Under the modified approach, the State expends certain maintenance and preservation costs and does not report depreciation expense. Assets accounted for under the modified approach include approximately 11,000 centerline road miles of pavement along 214 routes and approximately 5,500 bridges that the State is responsible to maintain.

The State has consistently maintained the assessed conditions of roads over the past three years. It is the State's policy to maintain a network average International Roughness Index (IRI) of no more than 95 for Interstate Roads, NHS Non-Interstate and Non-NHS Roads (a good rating is in the range of 80–115). The most recent condition assessment, completed for FY 2013, indicated that the average IRI for roads was in an acceptable range.

Economic Factors

The economic and revenue forecasts upon which the FY 2012 – FY 2013 State budget was based were presented to the State Budget Committee on April 15, 2011. At that time, real Gross Domestic Product (real GDP) was forecast to increase by 3.7% in FY 2013, while nominal GDP was forecast to increase by 4.5%. Corporate profits were forecast to increase by 1.8% and the S&P 500 was forecast to increase by 5.9%. Indiana personal income and Indiana personal income net of transfer payments were forecast to increase by 3.9% and 4.1%, respectively. The Indiana unemployment rate was forecast to average 8.2% for FY 2012.

With a 2012 Gross Domestic Product of \$298.6 billion, Indiana's economy ranked 16th largest in the U.S. in terms of the value of goods and services.

The State has maintained the assessed conditions of bridges at levels which are above the established benchmarks. It is the State's policy to maintain Interstate bridges at an average sufficiency rating of 87%, NHS Non-Interstate bridges at an average sufficiency rating of 85%, and Non-NHS bridges at an average sufficiency rating of 83% (a good rating is 80% - 90%). The most recent condition assessment, completed in FY 2013, indicated that the average sufficiency rating for bridges exceeded the minimum acceptable standard.

Total actual maintenance and preservation costs for roads were less than planned because some interstate projects were delayed as priorities changed. However, the average IRI condition rating for interstate roads increased into the excellent condition rating range.

Total actual maintenance and preservation costs for bridges were lower than planned including on the interstate and NHS road classes. Some planned projects were delayed until future periods. Total actual maintenance and preservation costs for bridges on the non-NHS road class exceeded plan. Bridge sufficiency ratings were within the State's policy for the maintenance of bridges in all road classes.

Indiana's largest contributor to GDP growth was the manufacturing sector, which accounted for 15.3% of Indiana's GDP in 2012. The durable goods subset of the manufacturing sector caused more than half of Indiana's GDP growth in 2012.

In 2012, the manufacturing sector accounted for 13.6% of the jobs in Indiana compared to 20.3% in 2002. The share of employment accounted for by the health care and social services sector increased from 10.2% in 2002 to 11.2% in 2012. Per capita personal income was \$38,119 for 2012. In 2012, the State's unemployment rate averaged 8.4%.

Contacting the Auditor of State

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the State's finances and to demonstrate the State's accountability for the money it receives. If you have questions about this report or need additional

financial information, contact the Auditor of State, Room 240 State House, 200 West Washington Street, Indianapolis, Indiana 46204-2793, telephone (317) 232-3300.

