MANAGEMENT’S DISCUSSION AND ANALYSIS

STATE OF INDIANA
Management's Discussion and Analysis
June 30, 2014

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, 2014. 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) 2013 numbers have been restated.

Financial Highlights

- For FY 2014, on a government-wide basis, the assets of the State of Indiana exceeded its liabilities by $19.7 billion. This compares with $18.5 billion for FY 2013, as restated. Of this amount, $4.8 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 $1.3 billion, or 11.1% of the total general fund expenditures.
- On a government-wide basis for the primary government, the State incurred expenses net of program revenue of $14.2 billion, which are offset by general revenues totaling $15.4 billion, giving an increase in net position of $1.2 billion.
- General revenue for the primary government increased by $0.3 billion, or 1.7%, from FY 2013. Sales tax revenues increased by $150.4 million and individual and corporate income tax revenue increased $440.8 million indicating the Indiana economy continued to recover from the recession.
- Combined budget balances for FY 2014 were $2,005.3 million. The balance of $2,005.3 million consists of $1,036.4 in the General Fund, $445.0 million in the Medicaid Contingency Reserve Fund, $150.0 million in the Tuition Reserve Fund, and $373.9 million in the Rainy Day Fund.
- $2,005.3 million represents 13.3% of the General Fund appropriations for FY 2015. These reserve balances will protect the state's critical operations during the next economic downturn.
- 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

	Dec. 31, 2013	Dec. 31, 2012	% Change
Total Employed Labor Force	3,160,697	3,157,751	0.1%
Total Goods and Service Employment	2,980,600	2,942,800	1.3%
Service-Providing Employment	2,355,700	2,325,500	1.3%
Goods-Producing Employment	624,900	617,300	1.2%
Unemployment Rate	6.3%	8.1%	-22.2%
Median Household Income	47,529	46,974	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

Year	Governor's Authority	Judiciary	Other Elected Officials	On Disability Leave - In Pay Status	On Disability Leave - Not in Pay Status	Total
2014	28,279	845	1,065	471	312	30,972
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

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. 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 capital lease 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	
	2014	2013	2014	2013	2014	2013
Current and other assets	$ 11,952.6	$ 10,852.8	$ 201.9	$ 237.1	$ 12,154.5	$ 11,089.9
Capital assets	14,982.4	14,456.3	0.5	0.7	14,982.9	14,457.0
Total assets	26,935.0	25,309.1	202.4	237.8	27,137.4	25,546.9
Current liabilities	3,771.7	2,898.4	974.4	1,421.7	4,746.1	4,320.1
Long-term liabilities	2,649.8	2,671.1	29.0	29.1	2,678.8	2,700.2
Total liabilities	6,421.5	5,569.5	1,003.4	1,450.8	7,424.9	7,020.3
Net position:						
Net investment in capital assets	13,873.8	13,303.4	0.5	0.7	13,874.3	13,304.1
Restricted	1,000.3	961.1	-	-	1,000.3	961.1
Unrestricted	5,639.4	5,475.1	(801.5)	(1,213.7)	4,837.9	4,261.4
Total net position	$ 20,513.5	$ 19,739.6	$ (801.0)	$ (1,213.0)	$ 19,712.5	$ 18,526.6

At the end of the current fiscal year, net position for the primary government was $19.7 billion as compared to $18.5 billion in 2013. There was an increase of $1.2 billion.

Current and other assets increased by $1.1 billion with increases in securities lending collateral making up the bulk of this. Statutory automatic taxpayer refunds of $360.6 million expired in FY 2014 leaving more cash on hand.

Capital assets increased by $525.9 million. The principal reason for the increase in capital assets was the increase in land and infrastructure at the Indiana Department of Transportation of $658.6 million primarily due to the State's Major Moves initiative.

Total liabilities increased by $404.6 million. This increase is due to increases in securities lending collateral of $717.7 million and accounts payables of $82.7 million. These increases are partially offset by the reduction of the amount due to the federal government for unemployment compensation benefits of $454.7 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 Activities		Business-type Activities		Total Primary Government	
	2014	2013	2014	2013	2014	2013
Revenues						
Program revenues:						
Charges for services	$ 2,418.4	$ 2,227.9	$ 976.7	$ 857.0	$ 3,395.1	$ 3,084.9
Operating grants and contributions	10,393.2	10,336.0	135.0	668.8	10,528.2	11,004.8
Capital grants and contributions	1,180.1	1,270.8	0.2	0.1	1,180.3	1,270.9
General revenues:						
Individual and corporate income taxes	5,811.8	5,371.0	-	-	5,811.8	5,371.0
Sales taxes	6,995.7	6,845.3	-	-	6,995.7	6,845.3
Other	2,580.4	2,917.0	1.1	-	2,581.5	2,917.0
Total revenues	29,379.6	28,968.0	1,113.0	1,525.9	30,492.6	30,493.9
Program Expense						
General government	1,449.9	1,473.9	-	-	1,449.9	1,473.9
Public safety	1,425.3	1,525.5	-	-	1,425.3	1,525.5
Health	350.6	409.1	-	-	350.6	409.1
Welfare	12,493.3	12,557.8	-	-	12,493.3	12,557.8
Conservation, culture and development	523.5	536.6	-	-	523.5	536.6
Education	10,568.1	10,136.6	-	-	10,568.1	10,136.6
Transportation	1,797.7	1,809.7	-	-	1,797.7	1,809.7
Interest expense	-	0.2	-	-	-	0.2
Unemployment compensation fund	-	-	674.8	1,160.6	674.8	1,160.6
Other	-	-	23.5	24.7	23.5	24.7
Total expenses	28,608.4	28,449.4	698.3	1,185.3	29,306.7	29,634.7
Excess (deficiency) before transfers	771.2	518.6	414.7	340.6	1,185.9	859.2
Transfers	2.7	2.8	(2.7)	(2.8)	-	-
Change in net position	773.9	521.4	412.0	337.8	1,185.9	859.2
Beginning net position, as restated	19,739.6	19,218.2	(1,213.0)	(1,550.8)	18,526.6	17,667.4
Ending net position	$ 20,513.5	$ 19,739.6	$ (801.0)	$ (1,213.0)	$ 19,712.5	$ 18,526.6

Governmental Activities

Program expenses exceeded program revenues by $14.6 billion. General revenues and transfers were $15.4 billion. The increase in net position was $0.8 billion, which is 2.6% of total revenues and 2.7% of total expenses.

The increase to excess (deficiency) before transfers was $252.6 million.

Revenues increased mainly because of the increase in general revenues from individual and corporate income taxes and sales taxes. Individual income taxes increased $440.8 million in FY 2014 due to the expiration of the automatic taxpayer rebate program of FY 2013. Also contributing to the increase in revenues was the increase in sales tax revenues of $150.4 million. These increases were partially offset by a decrease in gaming tax revenues of $107.3 million due to increased competition from surrounding states. In addition, inheritance tax revenues decreased $104.7 million as this tax is being eliminated.

Expenses increased overall by $159.0 million or 0.6%.

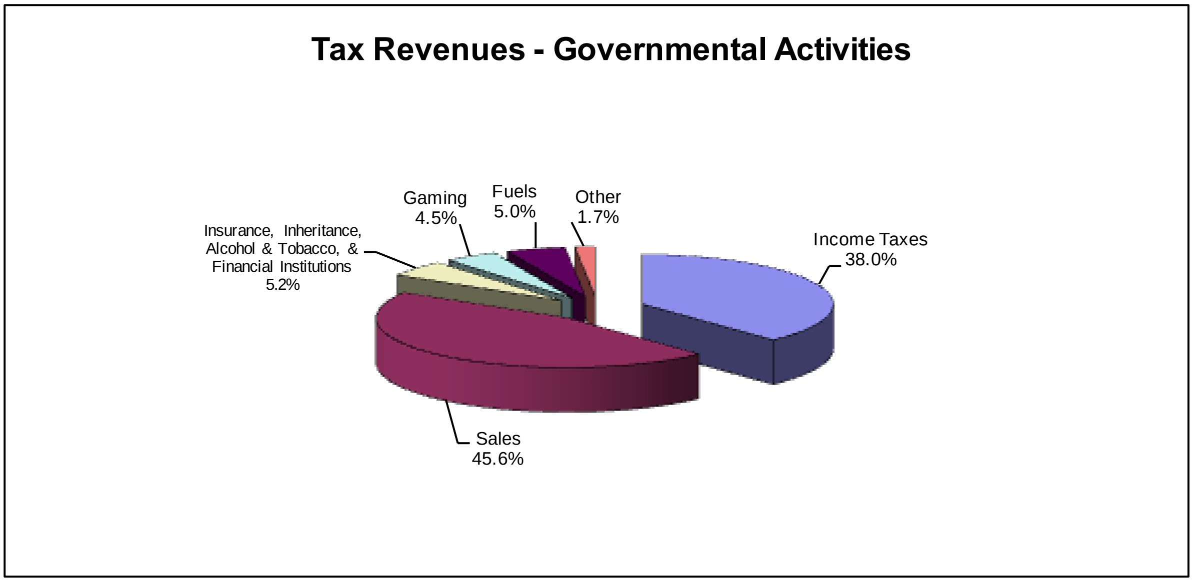
Education expenditures increased $431.5 million because the State increased its funding to schools for tuition support and full day kindergarten.

Welfare expenses decreased by $64.6 million primarily due to decreases in State funding for the DCS Family and Children Fund.

Public safety expenditures decreased by $100.1 million. The majority of this decrease is due to the settlement of a specific malpractice claim in FY 2013 from the Patients Compensation Fund.

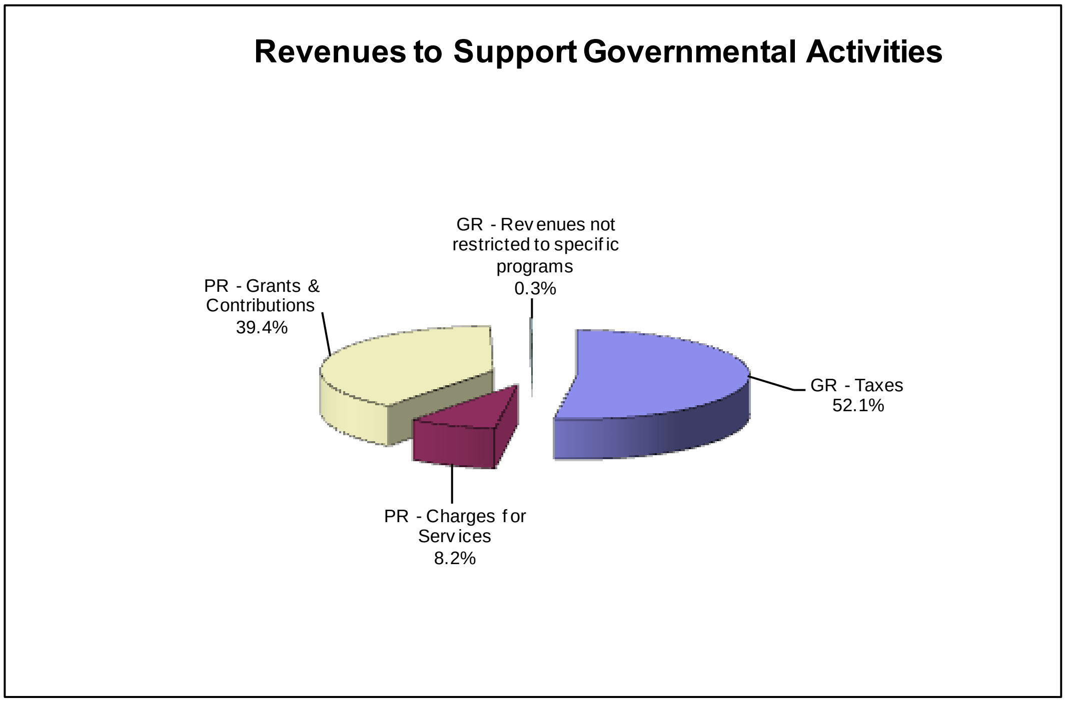
Health expenditures decreased $58.2 million due to decreases in spending in the Indiana State Department of Health's Federal Department of Agriculture and Health and Human Services Funds of $19.7 million, Indiana Check-up Plan of $11.8 million, and Tobacco Use Prevention and Cessation Fund of $5.7 million.

Tax revenues for governmental activities were broken down as follows:



Tax revenues of $15.3 billion represent 52.1% of total revenues for governmental activities. This compares to $15.0 billion or 51.9% of total revenues in FY 2013. Program revenues accounted for $14.0 billion or 47.6% of total revenues. In FY 2013, program revenues accounted for $13.8 billion or 47.8% of total revenues. General revenues other than tax revenues were $81.4 million or 0.3% of total revenues. Of this $19.8 million were investment earnings. This compares to 2013, when general revenues other than taxes were $89.7 million or 0.3% of total revenues and $28.0 million was investment earnings. Investment earnings decreased by $8.2 million from FY 2013 to FY 2014 or 29.4% due to slightly lower interest rates.

Total revenues for governmental activities were broken down as follows:



PR = program revenues
GR = general revenues

Total revenues were 102.7% of expenses which was an increase from 101.8% in FY 2013. Total revenues increased 1.4% from $29.0 billion in FY 2013 to $29.4 billion in FY 2014. Expenses grew 0.7% from $28.4 billion in FY 2013 to $28.6 billion in FY 2014.

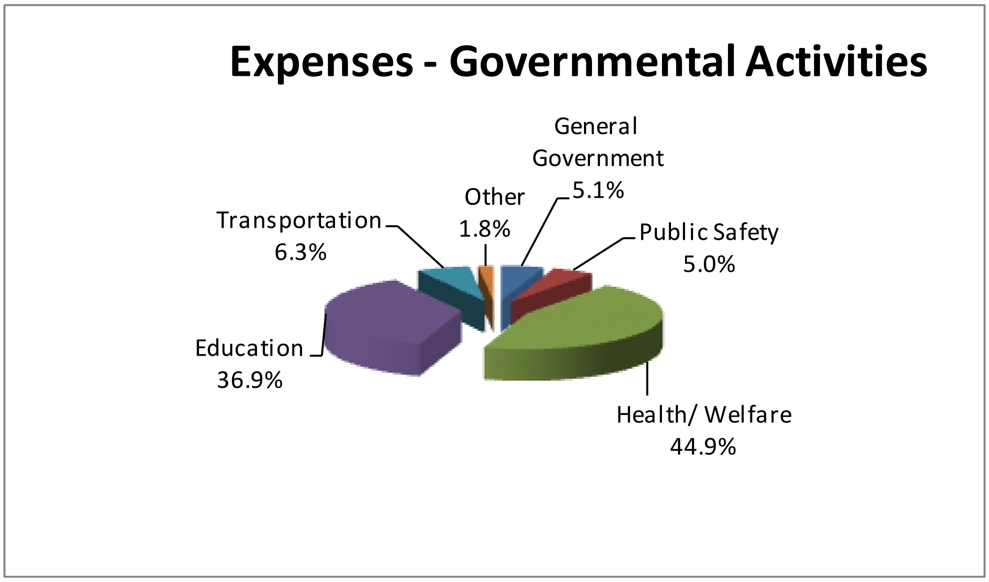
The largest portion of the State's expenses is for Welfare, which is $12.5 billion, or 43.7% of total expenses. This compares with $12.6 billion, or 44.1% of total expenses in FY 2013. The change in Welfare expenses was a decrease of $0.1 billion or 0.8%. $2.8 billion of Welfare expenses in FY 2014 were funded from general revenues.

Some of the major expenses were Medicaid assistance, $8.5 billion, the federal food stamp program in the U.S. Department of Agriculture Fund, $1.5 billion, and the U.S. Department of Health and Human Services Fund, $1.4 billion.

Education comprises 36.9%, or $10.6 billion of the State's expenses. In FY 2013, Education accounted for 35.6%, or $10.1 billion, of expenses. The change in Education expenses was an increase of $0.5 billion, or 5.0%. Some of the major expenses were tuition support and full day kindergarten, $6.6 billion, General Fund appropriations for State colleges and universities, $1.5 billion, Teachers' Retirement Pension, $719.7 million, federal grant programs from the U.S. Department of Education Fund, $633.8 million, federal grant programs from the U.S. Department of Agriculture Fund, $381.4 million, and post-retiree pensions, $69.3 million.

$1.4 billion, or 5.1% of expenses, was spent for General Government. General Government comprised $1.5 billion or 5.2% of expenses in FY 2013. General Government includes local distributions and money for State administration and those functions that serve the State as a whole. General government expenditures held steady from FY 2013 to FY 2014.

Total expenses for governmental activities were broken down as follows:



Business-type Activities

Business-type activities represent 3.7% of the Primary Government's revenues and 2.4% of the expenses. The Unemployment Compensation Fund accounts for 97.6% of business-type activities' operating revenues and 97.1% of operating expenses. The change in net position for business-type activities was an increase of $412.0 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 $443.4 million. This compares to FY 2013 when this fund's revenues exceeded expenses by $384.9 million. Employer contributions into the fund increased by $0.2 billion, from $0.8 billion in FY 2013 to $1.0 billion in FY 2014. Federal revenues into the fund decreased by $0.5 billion, from $0.7 billion in FY 2013 to $0.2 billion in FY 2014. The increase in the net position is primarily due to the reduction in the principal of the title XII loan from the federal government.

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, 2014	June 30, 2013	% Change
Governmental Activities:			
General government	$ 842.0	$ 980.3	-14.1%
Public safety	743.4	850.8	-12.6%
Health	51.4	23.7	116.9%
Welfare	2,763.0	3,106.8	-11.1%
Conservation, culture, and development	151.4	117.0	29.4%
Education	9,486.8	9,093.9	4.3%
Transportation	578.6	441.8	31.0%
Unallocated interest expense	-	0.2	-100.0%
Business-type Activities:			
Unemployment Compensation Fund	(410.5)	(338.7)	21.2%
Malpractice Insurance Authority	-	0.7	-100.0%
Inns and Concessions	(3.1)	(3.0)	3.3%
Wabash Memorial Bridge	-	0.5	100.0%
Total	$ 14,203.0	$ 14,274.0	-0.5%

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, 2014 was $3.5 billion, which is 65.3% of assets. This compares to a fund balance at June 30, 2013 of $3.3 billion, which was 73.3% of assets. This indicates that the State's financial position in the General Fund increased from the prior year by $134.8 million. The fund balance of $3.5 billion is composed of restrictions of $379.6 million, commitments of $5.6 million, and assignments of $1.7 billion, leaving an unassigned balance of $1.3 billion. The restricted amount consists of the State's Rainy Day Fund, which is accounted for in the General 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 increased 3.4%, or $456.0 million, from FY 2013, because of the increase in total tax revenue which included a $449.7 million (8.3%) increase in income tax and a $147.3 million (2.2%) increase in sales tax. The increase in tax revenues is explained by the expiration of the statutory automatic taxpayer refund program.

General Fund expenditures decreased $166.6 million, or 1.4% from FY 2013. Distributions to pension funds relating to the automatic taxpayer refund program were not required in FY 2014 as they were in FY 2013, resulting in a $360.6 million reduction in general government expenditures. Offsetting these decreases was an increase in education expenditures for state schools for tuition support and full day kindergarten of $118.4 million and General Fund appropriations for state colleges and universities of $88.5 million.

General Fund transfers in decreased $264.0 million or 15.7% from FY 2013. Transfers out were $3.4 billion in FY 2014 as compared to $3.2 billion in FY 2013. 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 increased $134.8 million.

Public Welfare-Medicaid Assistance Fund

Medicaid is an insurance program for low-income individuals. It is jointly funded by the Federal government and the State. The Medicaid Assistance Fund received $6.0 billion in Federal revenue as compared to $5.7 billion in FY 2013. State funding comes through transfers from the General Fund. Transfers in were $2.0 billion in FY 2014 as compared to $2.2 billion in FY 2013. Transfers out were $500.5 million compared with $565.3 million in FY 2013. The Fund distributed $8.5 billion in Medicaid assistance during the year, which is an increase of $250.5 million over FY 2013. The change in fund balance increased $14.8 million from FY 2013 to FY 2014.

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 $305.4 million to the State Highway Fund. $200.0 million was transferred into the fund from the Major Moves 2020 Trust Fund, which is part of the General Fund. The fund also received $9.2 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 2013 to FY 2014 was a decline of $137.3 million.

General Fund Budgetary Highlights

Actual State General Fund revenue collections decreased by $59.8 million, or 0.4%, in FY 2014. This is the result of both tax cuts enacted in FY 2014 as well as a weaker than projected economy. Actual expenditure growth was 2.15% in FY 2014 compared with growth of nearly 5.9% between FY 1996 and FY 2004. The goal of Governor Pence's administration is to limit year-over-year growth to 2.5%, which is roughly the 5-year inflationary CAGR. At year-end, the State had $2.0 billion in reserves, with $1.0 billion residing in the general fund, $445.0 million in the Medicaid Reserve Fund, $150.0 million in the Tuition Reserve Fund, and $373.9 million residing in the Rainy Day Fund. These changing funding balances are both the result of legislative requirements as well as FY 2014 close out transactions. A transfer of $150.0 million from the General Fund to the Tuition Reserve Fund was required in the 2013 budget bill. In addition, a transfer of $250.0 million was made to the Medicaid Reserve Fund. At close out, an additional $50.0 million was transferred to the Medicaid Reserve Fund increasing the balance to $445.0 million.

Capital Asset and Debt Administration

Capital Assets

Capital assets were $15.0 billion, which was 55.2% of total assets for the primary government. Related debt was $1.1 billion. Net investment in capital assets for the primary government was $13.9 billion. Related debt was 7.3% of capital assets. Total capital assets increased $526.0 million or 3.6% and is attributable to increases in the Indiana Department of Transportation's land and infrastructure. The net increase in capital assets is comprised of increases for INDOT's capital assets of $590.9 million, $2.0 million in internal service funds' capital assets and $1.6 million in DOA Public Works CIP with decreases of $64.2 million in capital assets of the primary government, and software in development of $3.4 million. INDOT's $590.9 million increase is comprised of increases in land, $95.2 million, and infrastructure consisting of interstate roads, non-interstate roads, and bridges, $563.4 million, and a decrease in CIP consisting of right of way and work in progress, $67.7 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 2013 to fiscal year 2014.

State of Indiana
Capital Assets
(in millions of dollars)

	Governmental Activities		Business-type Activities		Total Primary Government		Total % Change
	2014	2013	2014	2013	2014	2013	
Land	$ 1,960.9	$ 1,859.3	$ -	$ -	$ 1,960.9	$ 1,859.3	5.5%
Infrastructure	9,854.3	9,291.5	-	-	9,854.3	9,291.5	6.1%
Construction in Progress	2,015.5	2,085.0	-	-	2,015.5	2,085.0	-3.3%
Property, plant and equipment	2,689.8	2,709.8	1.1	1.1	2,690.9	2,710.9	-0.7%
Computer software	60.7	52.8	-	-	60.7	52.8	15.0%
Less accumulated depreciation	(1,598.8)	(1,542.1)	(0.6)	(0.4)	(1,599.4)	(1,542.5)	3.7%
Total	**$ 14,982.4**	**$ 14,456.3**	**$ 0.5**	**$ 0.7**	**$ 14,982.9**	**$ 14,457.0**	**3.6%**

Long-term Obligations

Major long-term obligations items are included in the following table. These items comprised 100% of total long-term liabilities and 36.1% of total liabilities.

The following table shows the percentage change from fiscal year 2013 to fiscal year 2014.

State of Indiana
Long-term Liabilities
(in millions of dollars)

	Governmental Activities		Business-type Activities		Total Primary Government		Total % Change
	2014	**2013**	**2014**	**2013**	**2014**	**2013**	
Accrued liability for compensated absences	$ 146.3	$ 148.6	$ 0.6	$ 0.5	$ 146.9	$ 149.1	-1.5%
Intergovernmental payable	10.0	20.0	-	-	10.0	20.0	-50.0%
Capital lease payable	1,112.6	1,156.9	-	-	1,112.6	1,156.9	-3.8%
Claims payable	-	-	28.4	28.6	28.4	28.6	-0.7%
Net pension obligations	1,201.3	1,166.8	-	-	1,201.3	1,166.8	3.0%
Other postemployment benefits	133.7	134.1	-	-	- 133.7	134.1	-0.3%
Pollution remediation	45.9	44.7	-	-	45.9	44.7	2.7%
Total	**$ 2,649.8**	**$ 2,671.1**	**$ 29.0**	**$ 29.1**	**$ 2,678.8**	**$ 2,700.2**	**-0.8%**

Total long-term liabilities decreased by 0.8% or $21.3 million. The largest decrease was in capital lease payable of $44.3 million. Other long-term liabilities to decrease were intergovernmental payables by $10.0 million and liabilities for compensated absences by $2.3 million.

The decrease in capital lease payable is due to the repayment of principal by the State Highway Fund for the highway revenue bonds held by the Indiana Finance Authority.

A significant increase in long-term liabilities was for net pension obligations which increased by $34.5 million. This increase in NPO liability is primarily due to increases in the liabilities of the Teachers' Retirement Fund (pre-1996 Account).

Claims payable for business activities decreased by $0.2 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.

Infrastructure

As required by GASB Statement No. 34, the State has capitalized its infrastructure. This amounts to $9.8 billion in roads and bridges using the modified approach, $1.7 billion in right of way classified as land, and $23.0 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.
- 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 expenses 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 based on the right wheel path (IRI RWP) of no more than 101 for Interstate Roads, NHS Non-Interstate and Non-NHS Roads (a good rating is in the range of 80–114). The most recent condition assessment, completed for FY 2014, indicated that the average IRI RWP for roads was in an acceptable range.

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 2014, indicated that the average sufficiency rating for bridges exceeded the minimum acceptable standard.

Total actual maintenance and preservation costs for roads were lower than planned during fiscal 2014. Various factors contributed to these costs being less than planned including bids under estimates, the deferral of projects as priorities changed, and "shrinkage" which results when the scope of work to be done is refined during the final bidding process. The average IRI RWP for all road categories were either in the good or excellent condition rating range.

Total actual maintenance and preservation costs for bridges were lower than planned including on the interstate, NHS, and non-NHS road classes. Various factors contributed to these costs being less than planned including bids under estimates, the deferral of projects as priorities changed, and shrinkage. Bridge sufficiency ratings were within the State's policy for the maintenance of bridges in all road classes.

Economic Factors

The economic and revenue forecasts upon which the FY 2013 – FY 2014 State budget was based were presented to the State Budget Committee on April 16, 2013. At that time, Indiana's real Gross Domestic Product (real GDP) was forecast to increase by 2.2% in FY 2014. Personal income was forecasted to increase by 4.6%. The Indiana unemployment rate was forecast to average 7.7% for FY 2014.

With a 2013 Gross Domestic Product of $294.2 billion, Indiana's economy ranked 16th largest in the U.S. in terms of the value of goods and services. Indiana's largest contributor to GDP growth was the manufacturing sector, which accounted for 30.0% of Indiana's GDP in 2013. The nondurable goods subset of the manufacturing sector was the biggest cause of Indiana's GDP growth in 2013.

In 2013, the manufacturing sector accounted for nearly 16.7% 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 12.7% in 2013. Per capita personal income was $38,622 and the State's unemployment rate averaged 7.5% in 2013.

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.