

FINANCIAL AUDIT
INCLUDING THE PROVISIONS OF THE SINGLE AUDIT ACT
OF THE

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
(A Component Unit of the State of Michigan)

October 1, 2000 through September 30, 2002



Michigan
Office of the Auditor General
REPORT SUMMARY

Financial Audit

*Including the Provisions of the Single Audit Act
 October 1, 2000 through September 30, 2002*

Report Number:
 07-402-03

Michigan Economic Development Corporation

Released:
 May 2003

A Single Audit is designed to meet the needs of all financial report users, including an entity's federal grantor agencies. The audit determines if the financial schedules and/or financial statements are fairly presented; considers internal control over financial reporting and internal control over federal program compliance; determines compliance with State compliance requirements material to the financial schedules and/or financial statements; and assesses compliance with direct and material requirements of the major federal programs.

Financial Statements:

Auditor's Report Issued

We issued an unqualified opinion on the Michigan Economic Development Corporation's (MEDC's) financial statements.

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Internal Control Over Financial Reporting

We did not identify any material weaknesses in internal control over financial reporting.

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**Noncompliance Material to
 the Financial Statements**

We did not identify any instances of noncompliance applicable to the financial statements that are required to be reported under *Government Auditing Standards*.

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Federal Awards:

Auditor's Report Issued on Compliance

We audited 2 programs as major programs and issued 2 unqualified opinions. The federal programs audited as major programs are identified on the back of this summary.

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Internal Control Over Major Programs

We did not identify any material weaknesses in internal control over major programs.

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Required Reporting of Noncompliance

We identified an instance of noncompliance that is required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133 (Finding 1).

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We audited the following programs as major programs:

<u><i>CFDA Number</i></u>	<u><i>Program Title</i></u>	<u><i>Compliance Opinion</i></u>
11.611	Manufacturing Extension Partnership	Unqualified
17.207	Employment Service	Unqualified

A copy of the full report can be
obtained by calling 517.334.8050
or by visiting our Web site at:
www.state.mi.us/audgen/



Michigan Office of the Auditor General
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

May 22, 2003

Ms. Sabrina Keeley, Chief Operating Officer
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Ms. Keeley:

This is our report on the financial audit of the Michigan Economic Development Corporation for the fiscal years ended September 30, 2002 and September 30, 2001 and the audit of the provisions of the Single Audit Act for the Michigan Economic Development Corporation (MEDC) for the period October 1, 2000 through September 30, 2002.

This report contains our report summary; our independent auditor's report on the financial statements; the MEDC management's discussion and analysis; and the MEDC financial statements, notes to the financial statements, and schedule of expenditures of federal awards. This report also contains our independent auditor's reports on compliance and on internal control over financial reporting and on compliance with requirements applicable to each major program and on internal control over compliance in accordance with U.S. Office of Management and Budget Circular A-133 and our schedule of findings and questioned costs. In addition, the report contains MEDC's summary schedule of prior audit findings, its corrective action plan, and a glossary of acronyms and terms.

Our finding and recommendation are contained in Section III of the schedule of findings and questioned costs. The entity preliminary response is contained in the corrective action plan. The *Michigan Compiled Laws* and administrative procedures require that the audited entity develop a formal response within 60 days after release of the audit report.

We appreciate the courtesy and cooperation extended to us during this audit.

AUDITOR GENERAL

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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

Independent Auditor's Report on the Financial Statements

December 27, 2002

Mr. Doug Rothwell, President and Chief Executive Officer
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Rothwell:

We have audited the financial statements of the Michigan Economic Development Corporation, a component unit of the State of Michigan, as of September 30, 2002 and September 30, 2001, as identified in the table of contents. These financial statements are the responsibility of the Michigan Economic Development Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1b, the financial statements present only the Michigan Economic Development Corporation and do not purport to, and do not, present fairly the financial position of the State of Michigan or its component units as of September 30, 2002 and September 30, 2001 and the changes in financial position and cash flows thereof for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Michigan Economic Development Corporation as of September 30, 2002 and September 30, 2001 and the changes in financial position and cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1c, the Michigan Economic Development Corporation adopted Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*; Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*; and Statement No. 38, *Certain Financial Statement Note Disclosures*.

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

In accordance with *Government Auditing Standards*, we have also issued a report dated December 27, 2002 on our tests of the Michigan Economic Development Corporation's compliance with certain provisions of laws, regulations, contracts, and grants and on our consideration of its internal control over financial reporting. 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 audit.

The schedule of expenditures of federal awards, required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is presented for purposes of additional analysis and is not a required part of the Michigan Economic Development Corporation's financial statements referred to in the first paragraph. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

AUDITOR GENERAL

Management's Discussion and Analysis

This is a discussion and analysis of the financial performance of the Michigan Economic Development Corporation (MEDC) for the fiscal year ended September 30, 2002. MEDC is a public body corporate and a component unit of the financial reporting entity of the State of Michigan. MEDC's management is responsible for the financial statements, notes to the financial statements, and this discussion.

Using the Financial Report

This financial report is prepared in accordance with Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*.

The reporting standards require a statement of net assets; a statement of revenues, expenses, and changes in fund net assets; and a statement of cash flows (direct method).

This financial report includes the reports of independent auditors, management's discussion and analysis, the basic financial statements, and the notes to the financial statements.

Amounts reported in the financial statements include both the MEDC corporate funds as well as the portion of the State appropriations made available to MEDC.

The financial statements are interrelated and represent the financial status of MEDC. The balance sheet is now referred to as the statement of net assets, which includes assets and liabilities.

The statement of revenues, expenses, and changes in fund net assets presents the revenues earned and expenses incurred during the year.

The statement of cash flows presents information related to cash in-flows and out-flows summarized by operating, capital acquisition, and investing activities.

Analysis of Financial Activities

The MEDC Executive Committee approves an annual budget and the investment policy. The President and Chief Executive Officer and Chief Operating Officer are responsible for implementing the programs approved by the Executive Committee.

Condensed Financial Information From the Statement of Net Assets As of September 30

	2002	2001
Current assets	\$ 194,884,652	\$ 243,040,169
Noncurrent assets:		
Investments	50,695,027	77,407,896
Loans receivable	27,129,212	18,124,711
Capital assets	14,652,484	15,407,411
Other noncurrent assets	11,693,622	13,888,239
Total Assets	<u>\$ 299,054,997</u>	<u>\$ 367,868,426</u>
Current liabilities	\$ 26,829,438	\$ 52,184,525
Long-term liabilities	7,868,642	9,571,724
Total Liabilities	<u>\$ 34,698,081</u>	<u>\$ 61,756,249</u>
Net Assets		
Capital assets	\$ 14,652,484	\$ 15,407,411
Unrestricted net assets	249,704,432	290,704,766
Total Net Assets	<u>\$ 264,356,916</u>	<u>\$ 306,112,177</u>

Current assets primarily consist of amounts retained by the State of Michigan in its equity in Common Cash for the unspent appropriations (details are provided at the end of this discussion and analysis), cash and cash equivalents, amounts due from the Michigan Strategic Fund (MSF), short-term investments, and loans receivable. Interest earned on funds retained in the Common Cash pool is the income for the State and does not get transferred to MEDC.

Current assets declined significantly primarily because of a change in the amount retained by the State of Michigan in its equity in Common Cash from \$200.2 million at September 30, 2001 to \$145.7 million at September 30, 2002. The decline was due to

amounts payable or committed in fiscal year 2000-01 for the Life Science and Michigan Core Community Fund Programs but not disbursed until fiscal year 2001-02.

Investments include long-term securities and program investments. During fiscal year 2001-02, total investments (short-term and long-term) declined by \$16.3 million compared with fiscal year 2000-01 because of the liquidation of investments necessary to pay for program grant commitments made in earlier years by MSF. This also resulted in reduced investment income during the year.

Loans receivable include only the long-term portion of the outstanding loans net of loan loss provisions. Total loans receivable (short-term and long-term) increased by \$1.5 million in fiscal year 2001-02 when compared with fiscal year 2000-01 because of new loans made from State funds for Life Science (\$2.8 million) and Michigan Core Community Fund (\$4.7 million) Programs netted against repayments of business and industrial development corporation (BIDCO) loans (\$1.3 million) and conversion of a loan to investment (\$4.2 million).

Capital assets at September 30, 2002 include the cost of a new building, new furniture, and information technology equipment net of depreciation. During the year, \$664,544 was added to the capital assets.

Other noncurrent assets consist of Capital Access Program reserves.

Current liabilities primarily consist of accounts payable. Current liabilities declined by \$25.4 million in fiscal year 2001-02 when compared with fiscal year 2000-01. Accounts payable at fiscal year 2000-01 year-end were substantially higher primarily because of liabilities for Life Science grants (for awards made from fiscal year 2000-01 and fiscal year 1999-2000 State appropriations) due but not disbursed until after fiscal year 2000-01 year-end.

Long-term liabilities primarily consist of Capital Access Program loan guarantee reserves.

Overall, **net assets** were reduced by approximately \$41.8 million during fiscal year 2001-02.

Condensed Financial Information
From the Statement of Revenues, Expenses, and Changes in Fund Net Assets
For the Fiscal Years Ended September 30

	2002	2001
Operating Revenues		
Operating grants and contributions	\$ 117,268,457	\$ 129,964,516
Interest and investment earnings	(1,237,647)	3,991,128
Other operating revenues	3,167,496	6,691,104
Total Operating Revenues	<u>\$ 119,198,306</u>	<u>\$ 140,646,749</u>
Operating Expenses		
Salaries, wages, and other administrative	\$ 43,578,143	\$ 49,246,713
Payment to MSF	2,937,913	
Operating grants	114,437,511	110,932,188
Total Operating Expenses	<u>\$ 160,953,567</u>	<u>\$ 160,178,901</u>
Change in net assets	\$ (41,755,261)	\$ (19,532,152)
Total net assets - Beginning	306,112,177	325,644,329
Total net assets - Ending	<u><u>\$ 264,356,916</u></u>	<u><u>\$ 306,112,177</u></u>

Operating grants and contributions include the amount received from State appropriations for the economic development functions; grants received from the National Institute of Standards and Technology (NIST), a federally funded program; and gaming revenues, fees, etc., received by MSF and transferred to MEDC.

Interest and investment earnings declined significantly because of (1) overall bear stock and bond market conditions and lower yields during fiscal year 2001-02, (2) a reduction in the total amount available for investments, and (3) the recognition of the difference between cost and market value of the investments as of September 30, 2002 compared with October 1, 2001. As of September 30, 2002, the market value of MEDC investments was \$11.6 million lower than the cost. As of September 30, 2001, the market value of MEDC investments was \$2.7 million lower than the cost. As a result, \$9.0 million was recorded as expenses to reflect the market value of MEDC investments on September 30, 2002.

Other operating revenues primarily consisted of gaming revenues. As a result of a consent judgment reached between the Keweenaw Bay Indian Community (KBIC), the U.S. Department of the Interior, the U.S. Department of Justice, and the Governor during fiscal year 2000-01, MEDC receives a semi-annual payment from KBIC in an amount equal to 8% of the net win derived from all class III electronic games of chance. During fiscal year 2001-02, MEDC received \$2.3 million for the period October 2001 through September 2002 compared to \$5.1 million received in fiscal year 2000-01. Payments received during fiscal year 2000-01 covered the period from June 1999 through September 2001.

Salaries, wages, and other administrative expenses decreased because of budget cuts, staffing reduction, and early retirements. Also, in fiscal year 2000-01, these expenses included a one-time charge of \$3.6 million to write off the amounts receivable from MSF that were not collectible.

Operating grants primarily include grants for Economic Development Job Training, Life Science, and Michigan Core Community Fund Programs and technical training programs.

The payment to MSF consisted of unspent amounts returned to the State General Fund. These funds were originally transferred to MEDC for Michigan Core Community Fund Program in fiscal year 1999-2000.

Condensed Financial Information
From the Statement of Cash Flows
For the Fiscal Years Ended September 30

	2002	2001
Cash provided (used) by:		
Operating activities	\$ (66,395,611)	\$ (4,598,029)
Capital and related financing activities	(664,544)	(9,754,530)
Investing activities	15,076,924	29,995,594
Net increase (decrease) in cash	\$ (51,983,230)	\$ 15,643,034
Cash and cash equivalents at beginning of year	237,794,439	222,151,405
Cash and cash equivalents at end of year	<u>\$185,811,208</u>	<u>\$237,794,439</u>

The **net cash** decreased from \$15.6 million in fiscal year 2000-01 to a negative \$52.0 million in fiscal year 2001-02 primarily because of the reduction of \$10.9 million in revenue from MSF, a decrease in interest and investment earnings, and operating grant expenses incurred during the fiscal year but earmarked from prior year funds.

The cash on hand at year-end included \$145.7 million equity in State of Michigan Common Cash. It is earmarked for the following obligations of MEDC:

<u>Program</u>	<u>Amount</u>
Life Science	\$ 67,661,122
Michigan Core Community Fund	23,048,075
Technology Centers (M-TECS)	4,022,106
Economic Development Job Training	25,352,513
Michigan Growth Fund	4,002,054
Michigan Promotion Program	413,090
Miscellaneous	2,954,170
Accounts payable*	18,276,087
Total Equity in State of Michigan Common Cash	<u><u>\$145,729,217</u></u>

* This amount represents payments made after September 30, 2002 against the obligations of fiscal year 2001-02.

The balance of the cash on hand represented investments in instruments with maturity dates of less than 12 months.

Other Pertinent Information

Contingent upon the opening of the remaining casinos approved under a 1998 compact, MEDC may receive additional revenues from MSF in fiscal years 2002-03 and 2003-04. The opening dates of these casinos and the amounts to be received are not certain.

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Net Assets
As of September 30

	2002	2001
ASSETS		
Current Assets:		
Cash	\$ 146,367,223	\$ 200,994,666
Capital Access Program - Cash	351,394	599,927
Short-term notes (Note 2)	27,398,970	22,311,606
Gaming revenues receivable	1,200,000	1,245,744
Amounts due from MSF	4,600,000	5,298,031
Amounts due from federal agencies		61,944
Investments (Note 2)	14,052,297	3,654,000
Other Current Assets:		
Loans receivable (Note 4)	475,289	7,963,378
Interest receivable	219,812	356,910
Miscellaneous	219,668	553,963
Total Current Assets	\$ 194,884,652	\$ 243,040,169
Noncurrent Assets:		
Capital Access Program - Cash Reserve	\$ 11,693,622	\$ 13,888,239
Loans receivable (Note 4)	27,129,212	18,124,711
Investments (Note 2)	50,695,027	77,407,896
Capital assets (net) (Note 5)	14,652,484	15,407,411
Total Noncurrent Assets	\$ 104,170,345	\$ 124,828,257
Total Assets	\$ 299,054,997	\$ 367,868,426
LIABILITIES		
Current Liabilities:		
Accounts payable and other liabilities	\$ 20,642,278	\$ 45,563,266
Compensated absences (Notes 6 and 7)	1,114,062	1,167,615
Amounts due to primary government	66,779	
Capital Access Program	5,000,000	5,402,762
Deferred revenues	6,319	50,882
Total Current Liabilities	\$ 26,829,438	\$ 52,184,525
Long-Term Liabilities:		
Capital Access Program	\$ 6,703,134	\$ 8,494,990
Compensated absences (Notes 6 and 7)	1,137,609	1,076,734
Other long-term liabilities	27,899	
Total Long-Term Liabilities	\$ 7,868,642	\$ 9,571,724
Total Liabilities	\$ 34,698,081	\$ 61,756,249
NET ASSETS		
Invested in capital assets	\$ 14,652,484	\$ 15,407,411
Unrestricted net assets (Note 9)	249,704,432	290,704,766
Total Net Assets	\$ 264,356,916	\$ 306,112,177

The accompanying notes are an integral part of the financial statements.

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Revenues, Expenses, and Changes in Fund Net Assets
For the Fiscal Years Ended September 30

	2002	2001
OPERATING REVENUES		
<u>Operating Grants and Contributions</u>		
Federal revenue - NIST	\$ 1,576,568	\$ 3,084,498
Payments from MSF - State appropriations	105,232,185	116,203,382
Payments from MSF - Gaming revenues, fees, etc.	10,459,705	10,676,636
Total Operating Grants and Contributions	\$ 117,268,457	\$ 129,964,516
<u>Interest and Investment Earnings</u>		
Investment earnings	\$ 7,346,040	\$ 8,875,142
Net increase (decrease) in fair value of investments	(8,982,985)	(5,902,457)
Interest income on loans	258,452	745,374
Interest income	140,846	273,069
Total Interest and Investment Earnings	\$ (1,237,647)	\$ 3,991,128
<u>Other Operating Revenues</u>		
Gaming revenues	\$ 2,349,131	\$ 5,052,001
Other operating revenue	818,365	1,639,103
Total Other Operating Revenues	\$ 3,167,496	\$ 6,691,104
Total Operating Revenues	\$ 119,198,306	\$ 140,646,749
 OPERATING EXPENSES		
Salaries, wages, and other administrative	\$ 43,570,821	\$ 49,067,530
Compensated absences (Note 7)	7,322	179,183
Payment to MSF	2,937,913	
Operating grants	114,437,511	110,932,188
Total Operating Expenses	\$ 160,953,567	\$ 160,178,901
 Operating Income (Loss)	\$ (41,755,261)	\$ (19,532,152)
 Change in net assets	\$ (41,755,261)	\$ (19,532,152)
 Total net assets - Beginning	306,112,177	325,644,329
 Total net assets - Ending	\$ 264,356,916	\$ 306,112,177

The accompanying notes are an integral part of the financial statements.

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Cash Flows
For the Fiscal Years Ended September 30

	2002	2001
CASH FLOWS FROM OPERATING ACTIVITIES		
Payments to employees	\$ (22,226,752)	\$ (18,130,554)
Payments to suppliers	(23,967,007)	(26,786,755)
Gaming revenues	2,394,875	3,806,257
Other operating revenue	818,365	1,639,103
Grants received from federal government	1,944,133	2,716,932
Operating grants	(138,811,233)	(94,136,148)
Payments to component unit (MSF)	(2,937,913)	
Payments from component unit (MSF)	116,389,921	126,293,135
Net cash provided (used) by operating activities	\$ (66,395,611)	\$ (4,598,029)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Net cash provided (used) by noncapital financing activities	\$ 0	\$ 0
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets	\$ (664,544)	\$ (9,754,530)
Net cash provided (used) by capital and related financing activities	\$ (664,544)	\$ (9,754,530)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale and maturities of investment securities	\$ 16,314,571	\$ 26,004,465
Interest and dividends on investments	(1,237,647)	3,991,128
Net cash provided (used) by investing activities	\$ 15,076,924	\$ 29,995,594
Net cash provided (used) - all activities	\$ (51,983,230)	\$ 15,643,034
Cash and cash equivalents at beginning of year	237,794,439	222,151,405
Cash and cash equivalents at end of year	\$ 185,811,208	\$ 237,794,439
RECONCILIATION OF CASH AND CASH EQUIVALENTS		
Per statement of net assets classifications:		
Cash	\$ 638,006	\$ 744,453
Equity in Common Cash	145,729,217	200,250,213
Capital Access Program	12,045,016	14,488,166
Short-term Notes	27,398,970	22,311,606
Cash and cash equivalents at end of year	\$ 185,811,208	\$ 237,794,439
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:		
Operating income (loss)	\$ (41,755,261)	\$ (19,532,152)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Interest (nonprogram) and investment income	1,237,647	(3,991,128)
Depreciation	1,419,471	155,926
Changes in assets and liabilities:		
Amounts due from component unit (MSF)	698,031	3,021,244
Mortgages and loans receivable (program loans)	(1,516,412)	(5,149,992)
Amounts due from federal agencies	61,944	
Other assets	517,137	(936,841)
Accounts payable and other liabilities	(27,058,169)	21,834,915
Net cash provided (used) by operating activities	\$ (66,395,611)	\$ (4,598,029)
SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES	\$ 0	\$ 0

The accompanying notes are an integral part of the financial statements.

Notes to the Financial Statements

Note 1 Significant Accounting Policies

The accounting policies of the Michigan Economic Development Corporation (MEDC) conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The following is a summary of the more significant policies:

a. Reporting Entity

Article VII, Section 28 of the State Constitution and Act 7, P.A. 1967, provided for the creation of MEDC as a public body corporate. MEDC was created by a 10-year contract (interlocal agreement) between a participating local economic development corporation formed under Act 338, P.A. 1974, as amended, and the Michigan Strategic Fund (MSF). MEDC is a separate legal entity created to promote smart economic growth by developing strategies and providing services to create and retain good jobs and a high quality of life for Michigan residents. Under the terms of the agreement, the governance of MEDC resides in an executive committee of 17 members appointed to eight-year, staggered terms by the Governor.

MEDC is a component unit of the financial reporting entity of the State of Michigan. The decision to include a potential component unit in the reporting entity is made by applying the criteria set forth in Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*. The basic criteria include the appointment of a voting majority of the governing board of MEDC; the legal separation of the State and MEDC; the fiscal independence of MEDC; whether exclusion of the unit would make the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)* misleading; and whether there is a potential for MEDC to provide specific financial benefits to, or impose specific financial burdens on, the State.

b. Basis of Presentation

(1) Fund Accounting: The accounts of the component units of the State of Michigan are organized on the basis of funds, each of which is

considered a separate accounting entity. MEDC's operations are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, net assets, revenues, and expenses. Government resources are allocated to and accounted for in separate funds, based upon the purposes for which they are to be spent and the means by which spending activities are controlled.

- (2) Proprietary Funds: MEDC is a proprietary fund. Proprietary funds are accounted for using a flow of economic resources measurement focus and the accrual basis of accounting. The accounting objectives are a determination of net income, financial position, and cash flow. All assets and liabilities associated with proprietary fund activities are included on the statement of net assets.

Proprietary funds are used to account for operations that are financed and operated in a manner similar to private business enterprises, i.e., where the intent of the governing body is that the costs (expenses) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

The accompanying financial statements present only MEDC and are not intended to present fairly the financial position and results of operations and cash flows of the State of Michigan or its component units.

c. Basis of Accounting

Proprietary fund types use the accrual basis of accounting. The accrual basis emphasizes the measurement of "net income" (i.e., "economic resource" focus). Using this basis, revenues are recognized when "earned" and expenses are recognized when "incurred." Operating revenues and expenses generally result from providing services to the public and to State and local units of government. All financial resources and obligations of a fund, whether current or noncurrent, are recorded in the fund. MEDC follows all GASB pronouncements and those Financial Accounting Standards Board Statements, Interpretations, Opinions, and

Research Bulletins that were issued on or before November 30, 1989, except those that conflict with a GASB pronouncement.

New accounting standards were adopted in fiscal year 2000-01. MEDC adopted GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and modified by Statement No. 38, *Certain Financial Statement Note Disclosures*. Statement No. 34, as amended and modified, commonly referred to as the new reporting model, retained much of the old reporting and disclosure requirements under the prior reporting model, with certain modifications and newly added information. The most significant effect on MEDC's financial statements was the reclassification of operating transfers to operating revenues and the addition of the management's discussion and analysis as required supplementary information.

d. Financial Data

The MSF Board of Directors entered into an interlocal agreement with a local unit of government to create MEDC. MEDC came into existence on April 5, 1999. In accordance with the terms of the agreement, substantial assets, liabilities, and fund balances of MSF were transferred to MEDC on May 1, 1999. All revenues received from tribal gaming, industrial development revenue bond (IDRB) issuance fees, and other sources are transferred to MEDC on a monthly basis. This interlocal agreement also detailed all of MSF's State classified employees to MEDC. State appropriations available to MSF for this purpose are also made available to MEDC, as needed. MEDC financial statements include transactions recorded using all appropriated funds, except the Community Development Block Grants (CDBG) Program transactions as required by the federal granting agency. Revenues from the U.S. Department of Labor for the Employment Service grant are received by MSF and transferred to MEDC to fund program expenditures.

MEDC financial statements primarily present the following:

- (1) Operating Revenues: Revenues from federal grants, other restricted sources, amounts available to MEDC from State appropriations, gaming revenues (see Note 8), and investment earnings. Also included in operating revenues are tribal gaming revenues, IDRB issuance fees, and Michigan Economic Growth Authority (MEGA) and Brownfield fees collected by MSF and transferred to MEDC during the year.
- (2) Operating Expenses: Expenses related to program grants funded by State appropriations and MEDC nonappropriated funds. Also included in operating expenses are administrative expenses (including payables) incurred out of appropriated funds, except for the CDBG Program.

Note 2 Deposits and Investments

a. General Information

MEDC's investment policy allows investments in the following investment types:

- (1) Securities issued or guaranteed by the U.S. government or its agencies.
- (2) Bonds or other obligations of any U.S. state or any local unit of government of any such state.
- (3) Preferred stock issued by U.S. corporations.
- (4) Repurchase agreements fully collateralized by U.S. government securities.
- (5) Corporate and bank debt including, but not limited to, commercial paper, certificates of deposit, banker's acceptances, and other short-term obligations.
- (6) Corporate notes and bonds.

- (7) Taxable bond funds.
- (8) Money market mutual fund shares that offer daily purchase and redemption and maintain a constant share price.
- (9) Common stock of U.S. corporations.
- (10) Stock mutual funds with portfolios highly concentrated in securities of U.S. corporations.

b. Deposits

GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, requires certain disclosures regarding policies and practices with respect to deposits and investments and the custodial credit risk associated with them.

In accordance with GASB Statement No. 3, deposits are classified into three categories of credit risk as follows:

- Category 1: Insured or collateralized with securities held by the entity or by its agent in the entity's name.
- Category 2: Collateralized with securities held by the pledging financial institution's trust department or agent in the entity's name.
- Category 3: Uncollateralized, including bank balances that are collateralized with securities held by the pledging financial institution or by its trust department or agent but not in the entity's name.

MEDC's deposits and investments at September 30, 2002 were:

	<u>Deposits</u>	<u>Investments</u>
Current Deposits and Investments:		
Equity in State of Michigan Common Cash	\$ 145,729,217	\$
Checking	638,006	
Capital Access Program - Cash	351,394	
Capital Access Program - Cash Reserve	11,693,622	
Short-term notes		27,398,970
Marketable securities		13,929,341
Nonmarketable securities		122,956
Total Current Deposits and Investments	<u>\$ 158,412,239</u>	<u>\$ 41,451,266</u>
Long-term securities		50,695,027
Total Deposits and Investments	<u><u>\$ 158,412,239</u></u>	<u><u>\$92,146,293</u></u>

Deposits included in MEDC's bank accounts (without recognition of outstanding checks or deposits in transit) were \$12,869,698 at September 30, 2002 (\$15,232,620 at September 30, 2001). Of that amount, \$3,859,918 (\$4,098,490 at September 30, 2001) was covered by federal depository insurance and was classified in GASB credit risk category 1. The remaining \$9,009,780 (\$11,134,130 at September 30, 2001) was uninsured and uncollateralized at September 30, 2002 and was classified in GASB credit risk category 3.

The equity in Common Cash, which is managed by the State Treasurer, represents State appropriated funds (General Fund and tobacco revenues for the Life Science Program) that were committed for several grant programs but not spent (disbursed) at the end of the fiscal year.

As of September 30, 2001, MEDC's total deposits and investments were \$215,482,832 and \$103,373,502, respectively.

c. Investments

All marketable investments are carried at fair value.

Equity investments in business and industrial development corporations (BIDCOs) are carried at the lower of aggregate cost or fair value. MEDC has determined that cost will be used to approximate fair value.

In accordance with GASB Statement No. 3, investments are also classified into three categories of credit risk as follows:

Category 1: Investments that are insured or registered or for which the securities are held by the entity or its agent in the entity's name.

Category 2: Uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the entity's name.

Category 3: Uninsured and unregistered investments for which the securities are held by the counterparty or by its trust department or agent but not in the entity's name.

The following table shows the fair value of investments at September 30, 2002 by investment type and in total and does not include the checking account balances:

Investment Type	GASB Credit Risk Category			Not Categorized	Fair Value
	1	2	3		
Corporate securities	\$	\$	\$ 43,499,429	\$	\$ 43,499,429
Government securities			16,831,020		16,831,020
Equity	1,052,827				1,052,827
Mutual funds				12,278,125	12,278,125
Other nonmarketable investments				18,484,892	18,484,892
Total Investments	<u>\$ 1,052,827</u>	<u>\$ 0</u>	<u>\$ 60,330,449</u>	<u>\$ 30,763,017</u>	<u>\$ 92,146,293</u>

The fair value of investments at September 30, 2001 was \$103,373,502, of which \$6,604,414 and \$68,298,064 were recorded in GASB credit risk

category 1 and category 3, respectively. The balance of \$28,471,024 was not categorized in any risk category.

Note 3 Revenues From MSF

Revenues from MSF consisted of the following:

	Fiscal Year	
	2001-02	2000-01
Tribal gaming revenue, IDRB fees, etc.	\$ 10,459,705	\$ 10,676,636
State's General Fund appropriation	59,173,859	64,890,718
State's restricted appropriation	1,058,326	1,312,664
State's tobacco revenue appropriation	45,000,000	50,000,000
Total Revenues From MSF	<u>\$ 115,691,890</u>	<u>\$ 126,880,018</u>

Note 4 Loans Receivable

Loans receivable consisted of the following:

	As of September 30	
	2002	2001
Urban Land Assembly Fund loans	\$ 4,309,306	\$ 4,381,945
Seed capital loans	3,400,000	7,800,000
BIDCO	2,722,854	4,015,354
Life Science Program	5,469,903	2,687,672
Michigan Core Community Fund	8,561,240	3,828,036
Other loans	15,091,198	26,485,000
Total	<u>\$ 39,554,500</u>	<u>\$ 49,198,007</u>
Less: Allowance for uncollectible loans	<u>(11,950,000)</u>	<u>(23,109,918)</u>
Total Loans Receivable	<u>\$ 27,604,500</u>	<u>\$ 26,088,089</u>

Seed capital loans are uncollateralized, 10-year term loans (which can be extended) bearing interest at 9% per annum with a balloon payback required at the end of the loan period.

BIDCO and other loans are collateralized loans bearing varying rates of interest and repayment terms.

Loans included in the "Other loans" category are collateralized, for qualifying projects, on the basis of participating up to 50% with other public or private lenders. The loans are due under varying repayment terms, including interest at predominantly 9.5% per annum.

The current portion of loans receivable includes those payments expected to be received during the next fiscal year.

MEDC provided no additional allowance during the fiscal year ended September 30, 2002 for loans receivable that MEDC expected to be converted to grants or uncollectible. Loan provisions are reduced for the amounts recovered, BIDCO credits, and write-offs for the nonperforming loans. The loans generally provide for no principal or interest payments during the term of the loans. These loans are expected to be converted to grants at the end of their term provided that certain conditions are met by the borrowers. The conditions generally require the borrowers to continue to conduct their principal business activities in the State of Michigan and submit specified reports to MEDC.

Note 5 Capital Assets

MEDC recorded its capital assets at cost and depreciates them over their useful lives using the straight-line depreciation method.

Capital asset activities for the fiscal year ended September 30, 2002 were as follows:

Capital Assets	Beginning Balance	Increases	Decreases	Ending Balance
Building and improvement	\$12,589,351	\$ 464,442	\$	\$ 13,053,793
Furniture	2,285,438	145,533		2,430,971
Non-EDP equipment	78,265	0		78,265
EDP equipment	610,283	54,568		664,851
Capital assets (cost)	<u>\$15,563,337</u>	<u>\$ 664,544</u>	<u>\$ 0</u>	<u>\$ 16,227,881</u>
Less accumulated depreciation for:				
Building and improvement	\$ (34,970)	\$ (427,386)	\$	\$ (462,356)
Furniture	(63,484)	(786,068)		(849,552)
Non-EDP equipment	(2,174)	(26,088)		(28,262)
EDP equipment	(55,297)	(179,929)		(235,226)
Total Accumulated Depreciation	<u>\$ (155,926)</u>	<u>\$ (1,419,471)</u>	<u>\$ 0</u>	<u>\$ (1,575,397)</u>
Capital assets (net)	<u>\$15,407,411</u>	<u>\$ (754,928)</u>	<u>\$ 0</u>	<u>\$14,652,484</u>

Note 6 Long-Term Liabilities

Long-term liabilities are accrued when incurred in proprietary funds (using the accrual basis of accounting). The following table summarizes Capital Access Program and compensated absences liabilities of MEDC for the fiscal year ended September 30, 2002:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Capital Access Program	\$13,897,752	\$3,550,959	\$5,745,577	\$11,703,134	\$5,000,000
Compensated absences	\$ 2,244,350	\$1,264,765	\$1,257,443	\$ 2,251,672	\$1,114,062

Note 7 Pension Plans

State classified employees detailed to MEDC are covered by the plans offered by the State of Michigan. Detail and data regarding the plan descriptions, accounting policies, vesting and eligibility requirements, actuarial cost methods and assumptions, funding status and requirements, and 10-year historical trend information are provided in the *SOMCAFR* and the plans' detailed financial reports, issued by the Office of Retirement Services.

MEDC offers a defined contribution plan (under the Internal Revenue Service Code Section 401(A)) for the non-detailed employees. MEDC contributes 8% of the gross wages to the accounts of eligible employees. As of September 30, 2002, 35 employees were eligible to receive contributions. MEDC's contributions to the plan were current. MEDC also offers a 457 deferred compensation plan to these employees. As of September 30, 2002, 37 employees participated in this plan. MEDC does not make any contributions to the 457 plan. Both plans are administered by a third party administrator and the employees manage their own investments.

Note 8 Gaming Revenues

Under a consent judgment reached between the Keweenaw Bay Indian Community (KBIC), the U.S. Department of the Interior, the U.S. Department of Justice, and the Governor, MEDC receives a semi-annual payment from KBIC in an amount equal to 8% of the net win derived from all class III electronic games of chance. During fiscal year 2001-02, MEDC received \$2.3 million in such revenue (\$5.1 million in fiscal year 2000-01 covering the period from June 1999 through September 2001).

Note 9 Commitments

Of the total net assets (\$264,356,916), a portion is committed for the following economic development projects:

Access Technology - North Coast	\$ 500,000
Center for Career Training	2,751,680
Center for Michigan's Renaissance	1,390,998
Center for Virtual Learning	197,863
Covisint	3,500,000
Detroit Downtown Development Authority	2,996,564
Economic Development Job Training	25,352,513
Emerging Technology Fund	1,906,684
Life Science Program	67,661,122
Marketing	5,000,000
Michigan Core Community Fund	23,048,075
Michigan Growth Fund	4,002,107
Minority Investments	3,718,422
NextEnergy Initiative	52,500,000
SmartZones Initiatives	4,250,000
Technology Centers (M-TECS)	4,022,106
Technology Transfer Program	500,000
Urban Land Development	4,153,735
Total	<u>\$ 207,451,869</u>

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SUPPLEMENTAL
FINANCIAL SCHEDULE

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Schedule of Expenditures of Federal Awards (1)
For the Period October 1, 2000 Through September 30, 2002

For the Fiscal Year Ended September 30, 2001

<u>Federal Agency/Program</u>	<u>CFDA (2)</u> <u>Number</u>	<u>Pass-Through</u> <u>Identification</u> <u>Number</u>	<u>Directly</u> <u>Expended</u>	<u>Distributed to</u> <u>Subrecipients</u>	<u>Total Expended</u> <u>and Distributed</u>
<u>U.S. Department of Commerce</u>					
Direct Program:					
Manufacturing Extension Partnership (3)	11.611		\$	\$ 3,084,498	\$ 3,084,498
Total U.S. Department of Commerce			\$ 0	\$ 3,084,498	\$ 3,084,498
<u>U.S. Department of Labor</u>					
Pass-Through Program:					
Michigan Strategic Fund Employment Service (4)	17.207	205-Y01	\$ 770,000	\$	\$ 770,000
Total U.S. Department of Labor			\$ 770,000	\$ 0	\$ 770,000
Total Expenditures of Federal Awards			<u>\$ 770,000</u>	<u>\$ 3,084,498</u>	<u>\$ 3,854,498</u>

- (1) Basis of Presentation: This schedule includes the federal grant activity of the Michigan Economic Development Corporation and is presented on the modified accrual basis of accounting. This information is presented in accordance with the requirements of *OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts may differ from amounts presented in, or used in the preparation of, the financial statements.
- (2) *CFDA* is defined as *Catalog of Federal Domestic Assistance*.
- (3) *CFDA* 11.611 was transferred from the Michigan Strategic Fund on May 1, 1999.
- (4) These amounts are not shown on the financial statements as federal revenue. The amounts are appropriated to the Michigan Strategic Fund and are shown on the Michigan Strategic Fund financial statements as federal revenue. These funds are transferred to the Michigan Economic Development Corporation and included in the Payments from MSF-State Appropriations line in the financial statements.

For the Fiscal Year Ended September 30, 2002

<u>Directly Expended</u>	<u>Distributed to Subrecipients</u>	<u>Total Expended and Distributed</u>	<u>Total Expended and Distributed for the Two-Year Period</u>
\$	\$ 1,576,568	\$ 1,576,568	\$ 4,661,065
\$ 0	\$ 1,576,568	\$ 1,576,568	\$ 4,661,065
\$ 764,519	\$	\$ 764,519	\$ 1,534,519
\$ 764,519	\$ 0	\$ 764,519	\$ 1,534,519
<u>\$ 764,519</u>	<u>\$ 1,576,568</u>	<u>\$ 2,341,087</u>	<u>\$ 6,195,584</u>



STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
(517) 334-8050
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

Independent Auditor's Report on Compliance and on Internal Control Over Financial Reporting

December 27, 2002

Mr. Doug Rothwell, President and Chief Executive Officer
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Rothwell:

We have audited the financial statements of the Michigan Economic Development Corporation, a component unit of the State of Michigan, as of and for the fiscal years ended September 30, 2002 and September 30, 2001, as identified in the table of contents, and have issued our report thereon dated December 27, 2002. 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 *Government Auditing Standards* issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Michigan Economic Development Corporation'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 the Michigan Economic Development Corporation'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 internal control over financial reporting. Our consideration of internal control over financial reporting would not necessarily disclose all matters in internal control over financial reporting that might be material weaknesses. A material weakness is a reportable 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 caused by error or fraud 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 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 Michigan Economic Development Corporation's Executive Committee and management, the Michigan Strategic Fund, the Legislature, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL



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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

Independent Auditor's Report on Compliance With
Requirements Applicable to Each Major Program
and on Internal Control Over Compliance in
Accordance With OMB Circular A-133

December 27, 2002

Mr. Doug Rothwell, President and Chief Executive Officer
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Rothwell:

Compliance

We have audited the compliance of the Michigan Economic Development Corporation, a component unit of the State of Michigan, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each major federal program for the two-year period ended September 30, 2002. The Michigan Economic Development Corporation's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each major federal program is the responsibility of the Michigan Economic Development Corporation's management. Our responsibility is to express an opinion on the Michigan Economic Development Corporation's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to in the previous paragraph that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Michigan Economic Development Corporation's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that

our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Michigan Economic Development Corporation's compliance with those requirements.

In our opinion, the Michigan Economic Development Corporation complied, in all material respects, with the requirements referred to in the second previous paragraph that are applicable to each major federal program for the two-year period ended September 30, 2002.

Internal Control Over Compliance

The management of the Michigan Economic Development Corporation is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Michigan Economic Development Corporation's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted a certain matter involving internal control over compliance and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over compliance that, in our judgment, could adversely affect the Michigan Economic Development Corporation's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. The reportable condition is described in the accompanying schedule of findings and questioned costs as Finding 1.

A material weakness is a reportable 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 noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control over compliance would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition identified in the previous paragraph is not a material weakness.

This report is intended solely for the information and use of the Michigan Economic Development Corporation's Executive Committee and management, the Michigan Strategic Fund, the Legislature, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS*

Section I: Summary of Auditor's Results

Financial Statements

Type of auditor's report issued:	Unqualified*
Internal control* over financial reporting:	
Material weaknesses* identified?	No
Reportable conditions* identified that are not considered to be material weaknesses?	None reported
Noncompliance material to the financial statements?	No

Federal Awards

Internal control over major programs:	
Material weaknesses identified?	No
Reportable condition identified that is not considered to be a material weakness?	Yes
Type of auditor's report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133, Section 510(a)?	Yes

* See glossary at end of report for definition.

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program</u>
11.611	Manufacturing Extension Partnership
17.207	Employment Service

Dollar threshold used to distinguish between type A and type B programs: \$300,000

Auditee qualified as a low-risk auditee*? No

Section II: Findings Related to the Financial Statements

We did not report any findings related to the financial statements.

Section III: Findings and Questioned Costs Related to Federal Awards

FINDING (07M0301)

1. Subrecipient Monitoring

U.S. Department of Commerce	CFDA: 11.611 Manufacturing Extension Partnership
Award Number: 70NANB5H0059	Award Period: 10/01/2000 - 09/30/2001 10/01/2001 - 09/30/2002
	Questioned Costs: \$0

The Michigan Economic Development Corporation (MEDC) had not established controls to ensure that grant agreements were developed and signed on a timely basis.

* See glossary at end of report for definition.

The Single Audit Act Amendments of 1996 and OMB Circular A-133 require MEDC to advise its subrecipient of federal and grant requirements. To ensure that the subrecipient is aware of program requirements and changes in program requirements, MEDC should develop and sign grant agreements on a timely basis.

Our review of MEDC's subrecipient monitoring process disclosed that MEDC did not obtain an agreement with the Michigan Manufacturing Technical Center for the Manufacturing Extension Partnership grant until October 28, 2002, for the grant year beginning April 15, 2002. In addition, the prior agreement covering the period April 15, 2001 through April 14, 2002 was not signed until February 18, 2002.

Not obtaining signed agreements in a timely manner could result in noncompliance with program requirements.

RECOMMENDATION

WE AGAIN RECOMMEND THAT MEDC ESTABLISH CONTROLS TO ENSURE THAT GRANT AGREEMENTS ARE DEVELOPED AND SIGNED ON A TIMELY BASIS.

The status of the finding related to federal awards that was reported in the prior Single Audit is disclosed in the summary schedule of prior audit findings.

OTHER SCHEDULES

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Summary Schedule of Prior Audit Findings
As of September 30, 2002

PRIOR AUDIT FINDINGS RELATED TO THE FINANCIAL STATEMENTS

There were no findings related the financial statements in the prior Single Audit.

PRIOR AUDIT FINDINGS RELATED TO FEDERAL AWARDS

Audit Findings Not Corrected or Partially Corrected

Audit Period: October 1, 1998 through September 30, 2000

Finding Number: 07M0101

Finding Title: Subrecipient Monitoring

Finding: The Michigan Economic Development Corporation (MEDC) had not established controls to ensure that grant agreements were developed and signed on a timely basis.

Status: This finding is repeated in the current report (07M0301).

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

Corrective Action Plan

As of May 1, 2003

FINDINGS RELATED TO THE FINANCIAL STATEMENTS

There were no findings related to the financial statements for fiscal years 2000-01 and 2001-02.

FINDINGS RELATED TO FEDERAL AWARDS

Finding Number: 07M0301

Finding Title: Subrecipient Monitoring

Management Views: We agree with the recommendation.

Corrective Action: The delay in signing the agreement for grant year 2002-03 was due to the organizational changes at the Michigan Manufacturing Technical Center (MMTC) and changes in responsibility monitoring of MMTC activities at MEDC. We have procedures in place to have this agreement in place for grant year 2003-04 as soon as possible after the grant is awarded by the National Institute of Standards and Technology. We will not release any payments until the agreement is signed.

Anticipated Completion Date: June 2003

Responsible Individual: Jeff Kaczmarek

Glossary of Acronyms and Terms

BIDCO	business and industrial development corporation.
CDBG	Community Development Block Grants.
CFDA	<i>Catalog of Federal Domestic Assistance.</i>
detailed employees	The temporary assignment of employees from a governmental entity to another business entity. Employees in this capacity continue to receive the same compensation and benefits of the original employer, but receive day-to-day direction (work assignments and supervision) from the entity they are detailed to.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules and/or financial statements of an audited entity are fairly presented in conformity with the disclosed basis of accounting.
GASB	Governmental Accounting Standards Board.
IDRB	industrial development revenue bond.
internal control	A process, effected by management, designed to provide reasonable assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
KBIC	Keweenaw Bay Indian Community.
low-risk auditee	As provided for in OMB Circular A-133, an auditee that may qualify for reduced federal audit coverage if it receives an annual Single Audit and it meets other criteria related to prior audit results. In accordance with State statute, this Single

Audit was conducted on a biennial basis; consequently, this auditee is not considered a low-risk auditee.

material misstatement A misstatement in the financial schedules and/or financial statements that causes the schedules and/or statements to not present fairly the financial position or the results of operations or cash flows in conformity with the disclosed basis of accounting.

material weakness A reportable condition related to the design or operation of internal control that does not reduce to a relatively low level the risk that either misstatements caused by error or fraud in amounts that would be material in relation to the financial schedules and/or financial statements or noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

MEDC Michigan Economic Development Corporation.

MMTC Michigan Manufacturing Technical Center.

MSF Michigan Strategic Fund.

NIST National Institute of Standards and Technology.

OMB U.S. Office of Management and Budget.

questioned cost A cost that is questioned by the auditor because of an audit finding: (1) which resulted from a violation or possible violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the use of federal funds, including funds used to match federal funds; (2) where the costs, at the time of the audit, are not supported by adequate documentation; or

(3) where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

reportable condition

A matter coming to the auditor's attention relating to a significant deficiency in the design or operation of internal control that, in the auditor's judgment, could adversely affect the entity's ability to (1) record, process, summarize, and report financial data consistent with the assertions of management in the financial schedules and/or financial statements or (2) administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants.

Single Audit

A financial audit, performed in accordance with the Single Audit Act Amendments of 1996, that is designed to meet the needs of all federal grantor agencies and other financial report users. In addition to performing the audit in accordance with the requirements of 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, a Single Audit requires the assessment of compliance with requirements that could have a direct and material effect on a major federal program and the consideration of internal control over compliance in accordance with OMB Circular A-133.

SOMCAFR

State of Michigan Comprehensive Annual Financial Report.

subrecipient

A nonfederal entity that expends federal awards received from another nonfederal entity to carry out a federal program.

unqualified opinion

An auditor's opinion in which the auditor states that:

- a. The financial schedules and/or financial statements presenting the basic financial information of the audited agency are fairly presented in conformity with the disclosed basis of accounting; or
- b. The financial schedules and/or financial statements presenting supplemental financial information are fairly stated in relation to the basic financial schedules and/or financial statements. In issuing an "in relation to" opinion, the auditor has applied auditing procedures to the supplemental financial schedules to the extent necessary to form an opinion on the basic financial schedules and/or financial statements, but did not apply auditing procedures to the extent that would be necessary to express an opinion on the supplemental financial schedules taken by themselves; or
- c. The audited agency complied, in all material respects, with the cited requirements that are applicable to each major federal program.