MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT

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, 2004 through September 30, 2006

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

271-0405-07

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

Audit report information can be accessed at:
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Michigan

Office of the Auditor General
REPORT SUMMARY

Financial Audit
Including the Provisions of the Single Audit Act

Michigan Economic Development Corporation
(A Component Unit of the State of Michigan)

October 1, 2004 through September 30, 2006

Report Number:
271-0405-07

Released:
May 2007

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 report any findings related to internal control over financial reporting.

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Noncompliance and Other Matters Material to the Financial Statements

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

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Federal Awards:

Auditor's Reports Issued on Compliance

We audited one program as a major program and issued an unqualified opinion. The federal program audited as a major program is identified on the back of this summary.

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Internal Control Over Major Programs

We did not report any findings related to internal control over major programs.

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Required Reporting of Noncompliance

We did not identify any instances of noncompliance that are required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133.

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We audited the following program as a major program:

CFDA Number	Program Title	Compliance Opinion
11.611	Manufacturing Extension Partnership	Unqualified

A copy of the full report can be obtained by calling 517.334.8050 or by visiting our Web site at: http://audgen.michigan.gov

Michigan Office of the Auditor General
201 N. Washington Square
Lansing, Michigan 48913

Thomas H. McTavish, C.P.A.
Auditor General

Scott M. Strong, C.P.A., C.I.A.
Deputy Auditor General

STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

May 25, 2007

Mr. James C. Epolito, President and Chief Executive Officer
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Epolito:

This is our report on the financial audit, including the provisions of the Single Audit Act, of the Michigan Economic Development Corporation (MEDC), a component unit of the State of Michigan, for the period October 1, 2004 through September 30, 2006.

This report contains our report summary, independent auditor's report on the financial statements, the MEDC management's discussion and analysis, the MEDC financial statements, and the schedule of expenditures of federal awards. This report also contains our independent auditor's report on internal control over financial reporting and on compliance and other matters, our independent auditor's report 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.

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

AUDITOR GENERAL

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INDEPENDENT AUDITOR'S REPORT

STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

Independent Auditor's Report on the Financial Statements

Mr. James C. Epolito, President and Chief Executive Officer
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Epolito:

We have audited the accompanying 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, 2006 and September 30, 2005, 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 1, 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, 2006 and September 30, 2005 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, 2006 and September 30, 2005 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 15, 2007 on our consideration of the Michigan Economic Development Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis for the fiscal year ended September 30, 2006 (on pages 11 through 16) 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 required supplementary information. However, we did not audit the information and express no opinion on it. The management's discussion and analysis for the fiscal year ended September 30, 2005 was not presented because this information was presented with the Michigan Economic Development Corporation's prior year audited financial statements.

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

February 15, 2007

MANAGEMENT'S DISCUSSION AND ANALYSIS

This is a discussion and analysis of the financial performance of the Michigan Economic Development Corporation (MEDC) for the period October 1, 2005 through September 30, 2006. 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 State funds made available to MEDC.

The financial statements are interrelated and represent the financial status of MEDC. The statement of net assets presents assets and liabilities as of the end of the fiscal year. The statement of revenues, expenses, and changes in fund net assets presents the revenues earned and expenses incurred during the fiscal year. The statement of cash flows presents information related to cash in-flows and out-flows summarized by operating, noncapital, capital acquisition, and investing activities.

Major Changes

The significant changes in fiscal year 2005-06 were:

1. Effective November 21, 2005, Act 225, P.A. 2005, required MEDC to transfer assets ($68.7 million), including cash, loans, and investments, related to its Life Sciences and Technology Tri-Corridor programs to the Michigan Strategic Fund (MSF). A portion of the Life Sciences assets remained with MEDC because the assets were purchased with corporate funds. Act 225, P.A. 2005, also required MEDC to transfer assets and liabilities ($4.1 million each) related to the Capital Access Program to MSF.

2. The State of Michigan reduced its funding to MEDC by $2.2 million in fiscal year 2005-06. As a result, MEDC reduced its staff by 34 employees. These employees were transferred to the Michigan State Housing Development Authority.

Analysis of Financial Activities

The assets of MEDC exceeded its liabilities at September 30, 2006 by $87.6 million and by $164.9 million at September 30, 2005. As of September 30, 2006, $26.9 million of this amount was in equity in common cash of the State of Michigan.

MEDC's total net assets decreased by $77.3 million during the course of fiscal year 2005-06 operations. This decrease resulted from the transfer of $68.7 million in assets of the Life Sciences and Technology Tri-Corridor programs to MSF as well as use of assets to fund MEDC's operations.

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

	2006	2005
Current assets	$ 56,961,416	$ 117,083,470
Noncurrent assets:		
Loans receivable	27,497,212	40,899,235
Investments	5,342,821	14,999,333
Capital assets (net)	11,019,063	11,463,257
Other noncurrent assets		4,317,956
Total assets	$ 100,820,511	$ 188,763,251
Current liabilities	$ 11,631,659	$ 20,613,670
Long-term liabilities	1,585,369	3,267,964
Total liabilities	$ 13,217,028	$ 23,881,634
Net assets:		
Invested in capital assets	$ 11,019,063	$ 11,463,257
Unrestricted net assets	76,584,421	153,418,361
Total net assets	$ 87,603,484	$ 164,881,618

Current assets primarily consist of amounts in the State of Michigan's equity in common cash, cash and cash equivalents, short-term investments, short-term loans receivable, and receivables for gaming revenues. Interest earned on funds retained in the common cash pool is the income of the State and is not transferred to MEDC.

Current assets decreased by $60.1 million in fiscal year 2005-06 primarily because equity in common cash, current loans, and current investments related to the Life Sciences, Technology Tri-Corridor, and Capital Access programs were transferred to MSF as explained under the "Major Changes" discussion.

Loans receivable include the long-term portion of the outstanding loans, net of loan loss provisions. Long-term loans receivable decreased by $13.4 million in fiscal year 2005-06 primarily because of investments related to the Life Sciences and Technology Tri-Corridor programs were transferred to MSF as explained under the "Major Changes" discussion.

Investments include long-term securities and program investments. During fiscal year 2005-06, total noncurrent investments declined by $9.7 million primarily because investments related to the Life Sciences and Technology Tri-Corridor programs were transferred to MSF as explained under the "Major Changes" discussion. Also, MEDC liquidated some investments to cover the shortfall in tribal gaming revenues.

Capital assets (net) at September 30, 2006 include the cost of the MEDC headquarters building, furniture, and information technology equipment, net of depreciation. During fiscal year 2005-06, capital assets worth $68,511 were added.

Other noncurrent assets consisted of $4.3 million of Capital Access Program loan guarantee reserves in fiscal year 2004-05. The Program ended on September 30, 2002, and no new loans are enrolled. Act 225, P.A. 2005, provided for the transfer of the Program to MSF in fiscal year 2005-06.

Current liabilities primarily consist of accounts payable and the current portion of the compensated absences and Capital Access Program liabilities. The current liabilities decreased by $9.0 million during fiscal year 2005-06 because of the transfer of the Life Sciences, Technology Tri-Corridor, and Capital Access programs to MSF and the reduced compensated absences liabilities related to the reduced staffing.

Long-term liabilities primarily consist of $1.5 million in long-term compensated absences. The long-term liabilities in total decreased in fiscal year 2005-06 by $1.7 million mainly because of the transfer of the Capital Access Program liabilities to MSF.

Overall, **net assets** decreased by approximately $77.3 million during fiscal year 2005-06 as a result of the preceding activities.

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

	2006	2005
Operating revenues		
Operating grants and contributions	$ 37,350,677	$ 67,642,621
Interest and investment earnings	1,312,088	1,721,340
Other operating revenues	8,129,233	9,770,704
Total operating revenues	$ 46,791,998	$ 79,134,666
Operating expenses		
Salaries, wages, and other administrative expenses	$ 33,099,700	$ 37,066,953
Compensated Absences	63,426	1,002,725
Payment to MSF	3,945	52,637
Operating grants	22,230,462	42,759,192
Total operating expenses	$ 55,397,533	$ 80,881,508
Operating income (loss)	$ (8,605,535)	$ (1,746,842)
Nonoperating Revenues (Expenses)	(68,672,599)	
Change in net assets	$ (77,278,134)	$ (1,746,842)
Total net assets - Beginning	164,881,618	166,628,460
Total net assets - Ending	$ 87,603,484	$ 164,881,618

Operating grants and contributions include $2.5 million for two federal grants and $33.5 million received from State funding for the economic development programs and $1.3 million in miscellaneous fees received by MSF and transferred to MEDC. In fiscal year 2005-06, operating grants and contributions decreased by $30.3 million as a result of the Life Sciences program being transferred to MSF.

Interest and investment earnings for fiscal year 2005-06 decreased by $0.4 million because of a reduced investment portfolio (as explained under the "Investments" discussion).

Other operating revenues primarily consist of revenues reimbursed by the Michigan Department of Transportation for the Welcome Center operations and tribal gaming revenues received directly by MEDC. Tribal gaming revenue is received as a result of a consent judgment reached by the Keweenaw Bay Indian Community, the U.S. Department of the Interior, the U.S. Department of Justice, and the Governor during fiscal year 2000-01. MEDC receives a semiannual payment from the Keweenaw Bay Indian Community in an amount equal to 8% of the net win derived from all class III electronic games of chance. MEDC received tribal gaming revenue of $2.6 million in fiscal year 2005-06 and $2.5 million in fiscal year 2004-05.

Salaries, wages, and other administrative expenses for fiscal year 2005-06 were $4.0 million lower than fiscal year 2004-05 because of the transfer of employees to the Michigan State Housing Development Authority as well as general cost-cutting measures adopted by MEDC.

Compensated absences decreased by $0.9 million because of the transfer of employees to the Michigan State Housing Development Authority.

Operating grants for fiscal year 2005-06 primarily include grants for the Economic Development Job Training Program. Operating grants for fiscal year 2004-05 also included grants for the Life Sciences and Technology Tri-Corridor programs. There was a decrease of $20.5 million in grant requests and disbursements for these programs in fiscal year 2005-06 because of the transfer of the Life Sciences and Technology Tri-Corridor programs to MSF as explained under the "Major Changes" discussion.

Nonoperating Expenses consist of $68.7 million in assets and liabilities transferred from MEDC to MSF as explained under the "Major Changes" discussion.

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

	2006	2005
Cash provided (used) by:		
Operating activities	$ (13,945,751)	$ (11,833,485)
Noncapital financing activities	(49,644,419)	
Capital and related financing activities	(68,511)	(93,992)
Investing activities	7,404,104	14,574,025
Net increase (decrease) in cash	$ (56,254,577)	$ 2,646,548
Cash and cash equivalents at beginning of year	87,141,452	84,494,904
Cash and cash equivalents at end of year	$ 30,886,876	$ 87,141,452

Cash and cash equivalents at the end of fiscal year 2005-06 ($30.9 million) included $26.9 million equity in the State of Michigan common cash. The balance of the cash on hand ($3.9 million) represented investments in instruments with maturity dates of less than 12 months. The noncapital financing activities related to the transfer of assets and liabilities to MSF in fiscal year 2005-06.

FINANCIAL STATEMENTS

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

	2006	2005
ASSETS		
Current assets:		
Cash (Note 2)	$ 833,995	$ 189,787
Equity in common cash (Note 2)	26,938,615	75,300,747
Capital Access Program - Cash		474,351
Money market mutual funds (Note 2)	3,114,266	6,858,610
Tribal gaming revenue receivable (Note 8)	1,431,523	1,823,793
Amounts due from MSF	154,161	
Amounts due from federal agencies	610,419	621,555
Loans receivable (Note 4)	1,791,033	5,285,229
Investments (Note 2)	20,487,769	25,740,118
Other current assets:		
Interest receivable	422,446	211,629
Miscellaneous	1,177,189	577,651
Total current assets	$ 56,961,416	$ 117,083,470
Noncurrent assets:		
Capital Access Program - Reserve	$	$ 4,317,956
Loans receivable (Note 4)	27,497,212	40,899,235
Investments (Note 2)	5,342,821	14,999,333
Capital assets (net) (Note 5)	11,019,063	11,463,257
Total noncurrent assets	$ 43,859,095	$ 71,679,781
Total assets	$ 100,820,511	$ 188,763,251
LIABILITIES		
Current liabilities:		
Accounts payable and other liabilities	$ 10,255,186	$ 15,712,800
Compensated absences (Notes 6 and 7)	1,178,787	2,437,253
Amounts due to primary government	160,598	178,669
Capital Access Program (Note 6)		2,000,000
Deferred revenues	37,089	284,947
Total current liabilities	$ 11,631,659	$ 20,613,670
Long-term liabilities:		
Capital Access Program (Note 6)	$	$ 2,317,956
Compensated absences (Notes 6 and 7)	1,543,567	783,104
Other long-term liabilities	41,801	166,904
Total long-term liabilities	$ 1,585,369	$ 3,267,964
Total liabilities	$ 13,217,028	$ 23,881,634
NET ASSETS		
Invested in capital assets	$ 11,019,063	$ 11,463,257
Unrestricted net assets	76,584,421	153,418,361
Total net assets (Note 9)	$ 87,603,484	$ 164,881,618

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

	2006	2005
OPERATING REVENUES		
Operating grants and contributions		
Federal revenue	$ 2,530,080	$ 2,483,000
Payments from MSF - State appropriations (Note 3)	33,513,501	64,281,460
Payments from MSF - Tribal gaming revenue and fees (Note 3)	1,307,097	878,162
Total operating grants and contributions	$ 37,350,677	$ 67,642,621
Interest and investment earnings		
Investment earnings	$ 1,703,547	$ (7,306,020)
Net increase (decrease) in fair value of investments	(772,715)	8,586,425
Interest income on loans	356,897	401,820
Interest income	24,357	39,115
Total interest and investment earnings	$ 1,312,088	$ 1,721,340
Other operating revenues		
Tribal gaming revenue (Note 8)	$ 2,575,484	$ 2,499,306
Other operating revenues	5,553,749	7,271,399
Total other operating revenues	$ 8,129,233	$ 9,770,704
Total operating revenues	$ 46,791,998	$ 79,134,666
OPERATING EXPENSES		
Salaries, wages, and other administrative expenses	$ 33,099,700	$ 37,066,953
Compensated absences (Note 7)	63,426	1,002,725
Payment to MSF	3,945	52,637
Operating grants	22,230,462	42,759,192
Total operating expenses	$ 55,397,533	$ 80,881,508
Operating income (loss)	$ (8,605,535)	$ (1,746,842)
Nonoperating revenues (expenses)		
Revenue from Capital Access Program liabilities transferred to MSF	$ 4,060,788	$
Expenses for Capital Access Program assets transferred to MSF	(4,060,788)	
Expenses for Life Sciences and Technology Tri-Corridor assets transferred to MSF	(68,672,599)	
Total nonoperating revenues (expenses)	$ (68,672,599)	$ 0
Change in net assets	$ (77,278,134)	$ (1,746,842)
Total net assets - Beginning	164,881,618	166,628,460
Total net assets - Ending	$ 87,603,484	$ 164,881,618

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

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Payments to employees	$ (19,152,718)	$ (21,764,918)
Payments to suppliers	(14,138,880)	(16,767,184)
Tribal gaming revenue	2,967,753	2,025,341
Other operating revenue	5,311,109	7,296,472
Grants received from federal government	2,541,216	2,236,574
Operating grants	(26,136,722)	(49,966,755)
Payment to MSF	(3,945)	(52,637)
Payments from MSF	34,666,436	65,159,622
Net cash provided (used) by operating activities	$ (13,945,751)	$ (11,833,485)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Nonoperating expenses	$ (49,644,419)	$
Net cash provided (used) by noncapital financing activities	$ (49,644,419)	$ 0
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets (Note 5)	$ (68,511)	$ (93,992)
Net cash provided (used) by capital and related financing activities	$ (68,511)	$ (93,992)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale and maturities of investment securities (Note 2)	$ 5,887,017	$ 21,883,350
Interest and dividends on investments	1,517,088	(7,309,325)
Net cash provided (used) by investing activities	$ 7,404,104	$ 14,574,025
Net cash provided (used) - all activities	$ (56,254,577)	$ 2,646,548
Cash and cash equivalents at beginning of year	87,141,452	84,494,904
Cash and cash equivalents at end of year	$ 30,886,876	$ 87,141,452
RECONCILIATION OF CASH AND CASH EQUIVALENTS		
Per statement of net assets classifications:		
Cash	$ 833,995	$ 189,787
Equity in common cash	26,938,615	75,300,747
Capital Access Program		4,792,308
Money market mutual funds	3,114,266	6,858,610
Cash and cash equivalents at end of year	$ 30,886,876	$ 87,141,452
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:		
Operating income (loss)	$ (8,605,535)	$ (1,746,842)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Interest (nonprogram) and investment income	(1,517,088)	7,309,325
Depreciation	512,705	571,944
Net increase (decrease) in fair value of investments	772,715	(8,586,425)
Changes in assets and liabilities:		
Amounts due from MSF and tribal gaming revenue receivable	238,108	(473,964)
Mortgages and loans receivable (program loans)	1,799,213	(9,283,374)
Amounts due from federal agencies	11,136	(246,426)
Other assets	(810,355)	(419,168)
Accounts payable and other liabilities	(6,346,650)	1,041,444
Net cash provided (used) by operating activities	$ (13,945,751)	$ (11,833,485)
SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES		
Loans transferred to MSF	$ (15,097,006)	$
Investment transferred to MSF	(8,249,130)	
Loans converted to grants	203,960	727,822
Increase/(decrease) in fair market value of investments	(772,715)	8,586,425
Net noncash provided (used) by investing, capital, and financing activities	$ (23,914,890)	$ 9,314,247

The accompanying notes are an integral part of 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 in April 1999 by a 10-year contract (interlocal agreement, as amended) 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 20 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. Financial Statement Presentation

The basic financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by GASB.

MEDC follows the business type activities reporting requirements of GASB Statement No. 34, which provides for a statement of net assets; a statement of revenues, expenses, and changes in fund net assets; and a statement of cash flows.

MEDC's operations 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. Accordingly, they do not purport to, and do not, present fairly the financial position and the changes in financial position and cash flows of the State of Michigan or its component units in conformity with generally accepted accounting principles.

c. Measurement Focus and Basis of Accounting

The financial statements contained in this report are presented using the economic resources measurement focus and the full accrual basis of accounting as provided by generally accepted accounting principles applicable to governments. Under the full accrual basis of accounting, revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows.

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.

Effective November 21, 2005, Act 225, P.A. 2005, required MEDC to transfer assets ($68.7 million), including cash, loans, and investments, related to MEDC's Life Sciences and Technology Tri-Corridor programs to MSF. Act 225, P.A. 2005, also reestablished the Capital Access Program within MSF and required the transfer of the assets and liabilities related to the Program from MEDC to MSF.

MEDC financial statements primarily present the following:

(1) Cash and Cash Equivalents: The amount reported as "Cash and cash equivalents at end of year" on the statement of cash flows is equal to the total of the amounts reported on the statement of net assets for the line items entitled "Cash," "Equity in common cash," "Capital Access Program - Cash," "Money market mutual funds," and "Capital Access Program - Reserve."

(2) Investments: MEDC reports marketable investments at fair value and other nonmarketable investments at cost.

(3) Loans Receivable: Loans receivable are reported net of allowance for losses.

(4) Capital Assets: Capital assets, which mainly include a building, furniture, and equipment, are reported at historical cost, net of depreciation.

(5) Operating Revenues: Operating revenues include revenues from federal grants, other restricted sources, amounts available to MEDC from State appropriations, tribal gaming revenue (see Notes 3 and 8), and investment earnings. Also included in operating revenues are IDRB issuance fees and Michigan Economic Growth Authority (MEGA) and Brownfield fees collected by MSF and transferred to MEDC during the fiscal year.

(6) Operating Expenses: Operating expenses include 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 Community Development Block Grant 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, 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

	As of September 30	
	2006	2005
Equity in State of Michigan common cash	$ 26,938,615	$ 75,300,747
Checking	113,995	189,787
Money market account	720,000	
Capital Access Program - Cash		474,351
Total deposits	$ 27,772,610	$ 75,964,885

Custodial Credit Risk: Governmental accounting standards require disclosures related to custodial credit risks for deposits. Custodial credit risk for deposits is the risk that, in the event of a bank failure, MEDC's deposits may not be returned to it. Deposits are exposed to custodial credit risk if they are not covered by depository insurance and are uncollateralized, collateralized with securities held by the pledging financial institution, or collateralized with securities held by the pledging financial institution's trust department or agent but not in MEDC's name.

Deposits included in MEDC's bank accounts (without recognition of outstanding checks or deposits in transit) were $633,480 at September 30, 2006 ($7,498,894 at September 30, 2005). Of that amount, $523,645 ($5,254,272 at September 30, 2005) was uninsured and uncollateralized at September 30, 2006. There were no deposits collateralized with securities held by the pledging financial institution or by the pledging financial institution's trust department or agent but not in MEDC's name. MEDC has no policy for controlling custodial credit risk.

MEDC's deposits included in the State of Michigan's equity in common cash are managed by the State Treasurer. Custodial credit risk disclosures and policies for controlling the risks regarding these deposits are described in Note 5 of the *SOMCAFR* for the fiscal year ended September 30, 2006.

c. Investments

All marketable investments are reported at fair value. Equity investments in business and industrial development corporations (BIDCOs) are reported using cost-based measures, which MEDC has determined approximates fair value.

MEDC makes grant commitments as a part of its economic development mission. These commitments are paid from the proceeds of the investments held in short-term and long-term securities. The timing of cash required for program commitments is dependent upon the completion of projects, and MEDC attempts to match investment maturities with its cash flow needs to meet grant commitments. For this reason, investments have frequent turnover. Therefore, the proceeds from sales and maturities of all investments are shown as a net balance on the statement of cash flows.

Governmental accounting standards require disclosures for investments for interest rate risk, custodial credit risk, credit risk, foreign currency risk, and concentration of credit risk:

The following table shows the fair value of investments at September 30, 2006 by investment type and in total:

		Investment Maturities			
	Fair Value	Less Than 1 Year	1 to 5 Years	6 to 10 Years	More Than 10 Years
Investment Type					
Commercial paper	$7,603,066	$ 7,603,066	$	$	$
Money market mutual funds	3,114,266	3,114,266			
Government securities	13,301,409	12,884,703			416,706
Equities	1,592,154		1,592,154		
Venture capital	3,333,962			3,333,962	
Total investments	$28,944,857	$23,602,035	$1,592,154	$3,333,962	$ 416,706

The following table shows the fair value of investments at September 30, 2005 by investment type and in total:

		Investment Maturities			
	Fair Value	Less Than 1 Year	1 to 5 Years	6 to 10 Years	More Than 10 Years
Investment Type					
Commercial paper	$25,150,180	$25,150,180	$	$	$
Money market mutual funds	6,858,610	6,858,610			
Government securities	776,174				776,174
Corporate bonds and notes	638,295	589,938			48,357
Equities	2,470,260		2,470,260		
Venture capital	11,704,543			11,704,543	
Total investments	$47,598,062	$32,598,728	$2,470,260	$11,704,543	$ 824,531

(1) Interest Rate Risk: Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of those investments. MEDC does not have a policy regarding interest rate risk. As of September 30, 2006, investments in commercial paper, money market mutual funds, and government securities with a market value of $24.0 million were exposed to interest rate risk. As of September 30, 2005, investments in commercial paper, money market mutual funds, government securities, and corporate bonds and notes with a market value of $33.4 million were exposed to interest rate risk.

(2) Custodial Credit Risk: Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, MEDC will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of MEDC, and are held by either the counterparty or the counterparty's trust department or agent but not in MEDC's name.

As of September 30, 2006, investments in commercial paper, government securities, and equities with a market value of $22.5 million were exposed to custodial credit risk. As of September 30, 2005, investments in commercial paper, government securities, corporate bonds and notes, and equities with a market value of $29.0 million were exposed to custodial credit risk. These securities were uninsured, not registered in MEDC's name, and held by the counterparty. MEDC does not have a policy for limiting custodial credit risk.

(3) Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Generally accepted accounting principles require disclosures of the credit quality ratings of investments in debt securities. MEDC had the following policy for controlling credit risk of debt securities in fiscal years 2005-06 and 2004-05. Short-term investments (less than one year) shall have a credit rating of not less than A-1/P-1. Long-term investments shall have a credit rating equal to BBB or better. The average quality rating of the fixed income portfolio shall have a credit rating of BBB or better.

The following table shows the credit quality ratings of investments in debt securities as of September 30, 2006:

		Credit Quality Rating	
Investment Type	Fair Value	Standard & Poor's	Moody's Investors Service
Commercial paper	$ 6,238,319	A-1+	P-1
Commercial paper	1,364,747	A-1	P-1
Government securities - U.S. agencies	13,301,409	AAA	Aaa
Money market mutual funds	3,114,266	AAA	Aaa
Total investments	$24,018,741		

The following table shows the credit quality ratings of investments in debt securities as of September 30, 2005:

Investment Type	Fair Value	Standard & Poor's	Moody's Investors Service
Commercial paper	$19,547,759	A-1+	P-1
Commercial paper	5,602,421	A-1	P-1
Government securities - U.S. agencies	776,174	AAA	Aaa
Corporate bonds and notes	289,140	AAA	Aaa
Corporate bonds and notes	349,155	Not rated	Not rated
Money market mutual funds	6,858,610	AAA	Aaa
Total investments	$33,423,259		

(4) Foreign Currency Risk: Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of investments or deposits. As of September 30, 2006 and September 30, 2005, MEDC did not have any investments in foreign securities.

(5) Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributable to the magnitude of MEDC's investments with a single issuer. MEDC does not have a policy limiting the dollar value of investments with a single issuer. At September 30, 2006, MEDC had investments in the following issuers for more than 5% of MEDC's total investments:

Name of Issuer	Amount	Percent of Investments
Federal Home Loan Bank	$2,397,744	8.28%
Federal Home Loan Mortgage corporation	$2,418,016	8.35%
Federal National Mortgage Association	$8,185,650	28.28%

At September 30, 2005, MEDC did not have any investments in any single issuer totaling more than 5% of MEDC's investments.

Note 3 Revenues From MSF

Revenues from MSF consisted of the following:

	Fiscal Year	
	2005-06	2004-05
Tribal gaming revenue and fees	$ 1,307,097	$ 878,162
Federal revenue - Employment Service		440,976
State's General Fund programs	32,651,928	53,339,734
Other State restricted programs	861,572	500,750
State's tobacco revenue funding		10,000,000
Total revenues from MSF	$ 34,820,598	$ 65,159,622

Tribal gaming revenue received from MSF decreased significantly during fiscal years 2005-06, 2004-05, and 2003-04 because the two tribes remitting funds to MSF under the 1998 compact agreement with the State placed these revenues into a separate account rather than submitting them to MSF. The tribes contend that the Club Keno game, introduced by the Bureau of State Lottery, violates the terms of the compact agreement. Based on information provided by the tribes, MSF estimated that the tribes placed a total of approximately $36.8 million into a separate account relating to these fiscal years.

Note 4 Loans Receivable

Loans receivable consisted of the following:

	As of September 30	
	2006	2005
Urban Land Assembly Fund loans	$ 6,263,022	$ 5,976,557
Seed capital loan	3,400,000	3,400,000
BIDCO loans	2,151,932	2,266,366
Life Sciences Program	4,693,374	19,093,513
Michigan Core Community Fund Program	12,890,688	13,246,474
Other loans	9,289,230	11,601,554
Total	$ 38,688,245	$55,584,464
Less: Allowance for uncollectible loans	(9,400,000)	(9,400,000)
Total loans receivable	$ 29,288,245	$46,184,464

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

MEDC provided no additional allowance for losses during the fiscal year ended September 30, 2006 for loans receivable that may be converted to grants or uncollectible in future years. Allowances for loan losses are reduced for the amounts recovered, BIDCO credits, and write-offs for the nonperforming loans. These loans generally provide for no principal or interest payments during the term of the loans. Some of 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, 2006 were as follows:

Capital Assets	Beginning Balance	Increases	Decreases	Ending Balance
Building and improvement	$ 13,086,970	$	$	$13,086,970
Furniture	2,497,430	68,511		2,565,941
Non-EDP equipment	78,265			78,265
EDP equipment	852,890			852,890
Capital assets (cost)	$ 16,515,555	$ 68,511	$ 0	$16,584,067
Less accumulated depreciation for:				
Building and improvement	$ (1,771,550)	$ (436,608)	$	$ (2,208,158)
Furniture	(2,459,311)	(22,153)		(2,481,464)
Non-EDP equipment	(78,265)			(78,265)
EDP equipment	(743,172)	(53,945)		(797,117)
Total accumulated depreciation	$ (5,052,299)	$ (512,705)	$ 0	$ (5,565,004)
Capital assets (net)	$ 11,463,257	$ (444,194)	$ 0	$11,019,063

Capital asset activities for the fiscal year ended September 30, 2005 were as follows:

Capital Assets	Beginning Balance	Increases	Decreases	Ending Balance
Building and improvement	$ 13,086,970	$	$	$ 13,086,970
Furniture	2,482,763	14,667		2,497,430
Non-EDP equipment	78,265			78,265
EDP equipment	773,565	79,325		852,890
Capital assets (cost)	$ 16,421,564	$ 93,992	$ 0	$ 16,515,555
Less accumulated depreciation for:				
Building and improvement	$ (1,334,942)	$ (436,608)	$	$ (1,771,550)
Furniture	(2,415,347)	(43,964)		(2,459,311)
Non-EDP equipment	(78,265)			(78,265)
EDP equipment	(651,800)	(91,372)		(743,172)
Total accumulated depreciation	$ (4,480,355)	$ (571,944)	$ 0	$ (5,052,299)
Capital assets (net)	$ 11,941,209	$ (477,952)	$ 0	$ 11,463,257

Note 6 Long-Term Liabilities

Long-term liabilities are accrued when incurred. The following table summarizes the Capital Access Program and compensated absences liabilities of MEDC for the fiscal year ended September 30, 2006:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Capital Access Program	$4,317,956		$4,317,956		
Compensated absences	$3,220,357	$621,805	$1,119,808	$2,722,354	$1,178,787

The following table summarizes the Capital Access Program and compensated absences liabilities of MEDC for the fiscal year ended September 30, 2005:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Capital Access Program	$5,614,856	$ 431,734	$1,728,634	$4,317,956	$2,000,000
Compensated absences	$2,217,632	$2,460,053	$1,457,328	$3,220,357	$2,437,253

Note 7 Pension Plans

State classified employees detailed to MEDC are covered by the plans offered by the State of Michigan. Specific information 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, Department of Management and Budget.

MEDC offers a defined contribution plan (under 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, 2006 and September 30, 2005, 27 and 41 employees, respectively, were eligible to receive contributions. The employer contributions to the plan were current. MEDC also offers a 457 deferred compensation plan to these employees. As of September 30, 2006 and September 30, 2005, 23 and 24 employees, respectively, participated in this plan. The employer 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 Tribal Gaming Revenue

Under a consent judgment reached between the Keweenaw Bay Indian Community, the U.S. Department of the Interior, the U.S. Department of Justice, and the Governor, MEDC receives a semiannual payment from the Keweenaw Bay Indian Community in an amount equal to 8% of the net win derived from all class III electronic games of chance. MEDC recorded tribal gaming revenue of $2.6 million in fiscal year 2005-06 and $2.5 million in 2004-05.

Note 9 Commitments

Of the total net assets ($87,603,484 and $164,881,618, respectively), a portion is committed for the following economic development projects as of September 30, 2006 and September 30, 2005:

	2006	2005
Access Technology - North Coast	$ 150,000	$ 250,000
Automotive Technological Accelerator	239,950	807,250
Core Communities II	634,597	1,046,375
Detroit Downtown Development Authority		2,050,858
Economic Development Job Training Program	13,569,002	12,829,876
Emerging Technology Fund	35,000	359,375
Life Sciences Program	2,035,677	48,051,371
Marketing	238,980	619,120
Michigan Core Community Fund Program	2,434,139	2,966,501
Michigan Growth Fund	5,000	56,358
Minority Investments	1,959,624	2,003,564
SmartZone Initiatives		312,400
University Matching Research	339,861	300,000
Urban Land Development	2,379,290	2,587,036
Total	$ 24,021,120	$ 74,240,083

Note 10 Related Party Transactions

When MEDC was created, it assumed ownership of an investment in a venture capital firm from MSF. One of the members on the MEDC Executive Committee is also a general partner of that venture capital firm. The investment was made through the ordinary course of business prior to that member's appointment to the MEDC Executive Committee. As of September 30, 2006 and September 30, 2005, the investment was recorded on the statement of net assets as a noncurrent asset in the amount of $23,678 and $24,202, respectively. There have been no related party transactions with this firm during fiscal years 2005-06 and 2004-05.

SUPPLEMENTAL
FINANCIAL SCHEDULE

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Schedule of Expenditures of Federal Awards (1)
For the Period October 1, 2004 Through September 30, 2006

Federal Agency/Program	*CFDA* (2) Number	Pass-Through Identification Number	For the Fiscal Year Ended September 30, 2005: Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
U.S. Department of Commerce					
Direct Program:					
Manufacturing Extension Partnership	11.611		$	$ 2,093,625	$ 2,093,625
Total U.S. Department of Commerce			**$ 0**	**$ 2,093,625**	**$ 2,093,625**
U.S. Department of Labor					
Pass-Through Program:					
Michigan Strategic Fund					
Employment Service/Wagner-Peyser Funded Activities	17.207	205-Y04	$ 440,976	$	$ 440,976
Total U.S. Department of Labor			**$ 440,976**	**$ 0**	**$ 440,976**
Total Expenditures of Federal Awards			$ 440,976	$ 2,093,625	$ 2,534,601

(1) Basis of Presentation: This schedule presents the federal grant activity of the Michigan Economic Development Corporation on the full accrual basis of accounting and in accordance with the requirements of U.S. Office of Management and Budget (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*.

For the Fiscal Year Ended September 30, 2006			
Directly Expended	Distributed to Subrecipients	Total Expended and Distributed	Total Expended and Distributed for the Two-Year Period
$	$ 2,297,782	$ 2,297,782	$ 4,391,407
$ 0	**$ 2,297,782**	**$ 2,297,782**	**$ 4,391,407**
$	$	$ 0	$ 440,976
$ 0	**$ 0**	**$ 0**	**$ 440,976**
$ 0	$ 2,297,782	$ 2,297,782	$ 4,832,383

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INDEPENDENT AUDITOR'S REPORTS ON INTERNAL CONTROL AND COMPLIANCE

STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
(517) 334-8050
FAX (517) 334-8079

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

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

Mr. James C. Epolito, President and Chief Executive Officer
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Epolito:

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, 2006 and September 30, 2005, as identified in the table of contents, and have issued our report thereon dated February 15, 2007. 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.

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 an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control 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 the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

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 grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Michigan Economic Development Corporation's management, 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

February 15, 2007

STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
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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

Mr. James C. Epolito, President and Chief Executive Officer
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Epolito:

Compliance

We have audited the compliance of the Michigan Economic Development Corporation 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, 2006. The Michigan Economic Development Corporation's major federal program is 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 first paragraph that are applicable to each major federal program for the two-year period ended September 30, 2006.

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 the internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control 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 noncompliance with the applicable requirements of laws, regulations, contracts, and grants caused by error or fraud 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. We noted no matters involving the internal control over compliance 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 management, 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

February 15, 2007

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 or other matters material to financial statements?	No

Federal Awards

Internal control over major programs:	
Material weaknesses identified?	No
Reportable conditions identified that are not considered to be material weaknesses?	None reported
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)?	No

Identification of major programs:

CFDA Number	Name of Federal Program
11.611	Manufacturing Extension Partnership

Dollar threshold used to distinguish between type A and type B programs:	$300,000
Auditee qualified as a low-risk auditee*?	No

* *See glossary at end of report for definition.*

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

We did not report any findings related to federal awards.

* *See glossary at end of report for definition.*

OTHER SCHEDULES

Summary Schedule of Prior Audit Findings
As of February 15, 2007

PRIOR AUDIT FINDINGS RELATED TO THE FINANCIAL STATEMENTS

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

PRIOR AUDIT FINDINGS RELATED TO FEDERAL AWARDS

There were no findings related to federal awards in the prior Single Audit.

* *See glossary at end of report for definition.*

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Corrective Action Plan
As of May 9, 2007

FINDINGS RELATED TO THE FINANCIAL STATEMENTS

There were no findings related to the financial statements for fiscal years 2004-05 and 2005-06.

FINDINGS RELATED TO FEDERAL AWARDS

There were no findings related to federal awards for the two-year period ended September 30, 2006.

GLOSSARY

BIDCO	business and industrial development corporation.
CFDA	*Catalog of Federal Domestic Assistance.*
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.
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 changes in financial position or cash flows in conformity with the disclosed basis of accounting.
material noncompliance	Violations of laws and regulations that could have a direct and material effect on major federal programs or on financial schedule and/or financial statement amounts.

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.
MSF	Michigan Strategic Fund.
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) initiate, record, process, and report financial data consistent with the assertions of management in the financial schedule and/or financial statements or (2) administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Violations of State laws, regulations, contracts, and

grant agreements that should be communicated to management but are not material to the financial schedules and/or financial statements may also be reported.

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.

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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 and/or financial statements 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 and/or financial statements 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.

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STATE OF MICHIGAN

OFFICE of the AUDITOR GENERAL