



MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT



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

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

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Michigan
Office of the Auditor General
REPORT SUMMARY

Financial Audit

Including the Provisions of the Single Audit Act

Michigan Early Childhood Investment Corporation
(A Discretely Presented Component Unit of the State of Michigan)

October 1, 2005 through September 30, 2007

Report Number:
431-1100-08

Released:
December 2009

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 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 Early Childhood Investment Corporation's (ECIC's) financial statements.

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Internal Control Over Financial Reporting

We identified significant deficiencies in internal control over financial reporting (Finding 1). We consider Finding 1 to be a material weakness.

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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 federal program as a major program and issued an unqualified opinion. We identified known questioned costs of \$571,109 and known and likely questioned costs totaling \$576,781. ECIC expended a total of \$23.5 million in federal awards during the two-year period ended September 30, 2007. 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 identified significant deficiencies in internal control over federal program compliance (Finding 2). We do not consider these significant deficiencies to be material weaknesses.

~ ~ ~ ~ ~

Required Reporting of Noncompliance

We identified instances of noncompliance that are required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133 (Finding 2).

~ ~ ~ ~ ~

We audited the following program as a major program:

<u><i>CFDA Number</i></u>	<u><i>Program or Cluster Title</i></u>	<u><i>Compliance Opinion</i></u>
93.575	Child Care and Development Fund (CCDF) Cluster	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
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

December 2, 2009

Ms. Susan K. Broman, Chair
Michigan Early Childhood Investment Corporation Board
and
Ms. Judy Samelson, Chief Executive Officer
Michigan Early Childhood Investment Corporation
221 North Pine
Lansing, Michigan

Dear Ms. Broman and Ms. Samelson:

This is our report on the financial audit, including the provisions of the Single Audit Act, of the Michigan Early Childhood Investment Corporation (ECIC), a discretely presented component unit of the State of Michigan, for the period October 1, 2005 through September 30, 2007.

This report contains our report summary, our independent auditor's report on the financial statements, the ECIC management's discussion and analysis, the ECIC 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, this report contains ECIC's corrective action plan and a glossary of acronyms and terms.

Our findings and recommendations are contained in Section II and Section III of the schedule of findings and questioned costs. The agency preliminary responses are contained in the corrective action plan. The *Michigan Compiled Laws* and administrative procedures require that the audited agency 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

TABLE OF CONTENTS

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION

	<u>Page</u>
INTRODUCTION	
Report Summary	1
Report Letter	3
INDEPENDENT AUDITOR'S REPORT	
Independent Auditor's Report on the Financial Statements	8
MANAGEMENT'S DISCUSSION AND ANALYSIS	
Management's Discussion and Analysis	11
FINANCIAL STATEMENTS	
Entity-Wide Financial Statements	
Statement of Net Assets	18
Statement of Activities	19
Governmental Fund Financial Statements	
Governmental Fund Balance Sheet	20
Governmental Fund Statement of Revenues, Expenditures, and Changes in Fund Balance	21
Reconciliation of the Governmental Fund Balance Sheet to the Statement of Net Assets	22

Reconciliation of the Governmental Fund Statement of Revenues, Expenditures, and Changes in Fund Balance to the Statement of Activities	23
Notes to the Financial Statements	24

SUPPLEMENTAL FINANCIAL SCHEDULE

Schedule of Expenditures of Federal Awards	34
--	----

INDEPENDENT AUDITOR'S REPORTS ON INTERNAL CONTROL AND COMPLIANCE

Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters	38
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	40

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section I: Summary of Auditor's Results	43
Section II: Findings Related to the Financial Statements	44
1. Internal Control	44
Section III: Findings and Questioned Costs Related to Federal Awards	46
2. Child Care and Development Fund (CCDF) Cluster, <i>CFDA</i> 93.575	46

OTHER SCHEDULE

Corrective Action Plan	53
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GLOSSARY

Glossary of Acronyms and Terms	62
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INDEPENDENT AUDITOR'S REPORT



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

Independent Auditor's Report on the Financial Statements

Ms. Susan K. Broman, Chair
Michigan Early Childhood Investment Corporation Board
and
Ms. Judy Samelson, Chief Executive Officer
Michigan Early Childhood Investment Corporation
221 North Pine
Lansing, Michigan

Dear Ms. Broman and Ms. Samelson:

We have audited the accompanying financial statements of the Michigan Early Childhood Investment Corporation, a discretely presented component unit of the State of Michigan, as of and for the fiscal years ended September 30, 2007 and September 30, 2006, as identified in the table of contents. These financial statements are the responsibility of the Michigan Early Childhood Investment 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 Early Childhood Investment 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, 2007 and September 30, 2006 and the changes in financial position 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 Early Childhood Investment Corporation as of September 30, 2007 and September 30, 2006 and the changes in financial position 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 October 14, 2009 on our consideration of the Michigan Early Childhood Investment 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 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 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 Early Childhood Investment 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

October 14, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis

This is a discussion and analysis of the financial performance of the Michigan Early Childhood Investment Corporation (ECIC) for the period October 1, 2005 through September 30, 2007. ECIC's management is responsible for the financial statements, the notes to the financial statements, and this discussion.

ECIC was established through an interlocal agreement pursuant to the Urban Cooperation Act of 1967 (Act 7, P.A. 1967 [Ex. Sess.], Sections 124.501 - 124.512 of the *Michigan Compiled Laws*) between the Department of Human Services (DHS), a principal department of the State of Michigan, and participating intermediate school districts (ISDs), bodies corporate established as authorized under Part 7 of the Revised School Code, Act 451, P.A. 1976, as amended. The purpose of the interlocal agreement was to create and empower ECIC to implement the powers, privileges, and authority of each of the parties with respect to the subject matter of the agreement, including, but not limited to, the performance of successful, effective, and efficient coordination and delivery of early childhood development and child care programs and functions throughout the State.

ECIC is a public body corporate and politic of the State of Michigan, separate and distinct from the State, exercising public and essential governmental functions and created by the State. ECIC is a discretely presented component unit of the State and is governed by the Corporation Board, including the Executive Committee. The governing body of each participating ISD is authorized to appoint 1 member to the Corporation Board to serve at the will of the ISD. For each ISD-appointed member, the Governor shall appoint up to 2 members to the Corporation Board that represent the State and serve at the will of the Governor. If there are fewer than 5 ISD participants, the Governor may appoint up to 12 additional members to the Corporation Board that represent the State and serve at the will of the Governor. The Executive Committee consists of 15 members. The members of the Executive Committee include the director of DHS or his or her designated representative from within DHS and 14 residents of Michigan appointed by the Governor. The members appointed by the Governor include at least 1 resident representing the participating ISDs. As of September 30, 2007, there were 21 participating ISDs.

On December 19, 2006, the Executive Committee of the Corporation approved an amendment to the bylaws to expand membership on the Executive Committee to

include one member appointed by the Senate Majority Leader, one member appointed by the Senate Minority Leader, one member appointed by the Speaker of the House of Representatives, and one member appointed by the Minority Leader of the House of Representatives. This bylaw change was in accordance with Section 32b.(1)(b), Act 342, P.A. 2006.

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 that component units provide financial statements prepared on both the accrual basis of accounting (entity-wide financial statements) and the modified accrual basis of accounting (fund level financial statements). The entity-wide financial statements include a statement of net assets and a statement of activities. The fund level financial statements include a fund balance sheet and a statement of revenues, expenditures, and changes in fund balance.

The following narrative and overview of the financial activities of ECIC is for the period October 1, 2005 through September 30, 2007. The basic financial statements provide information about the activities of ECIC as a whole and include all assets and liabilities. They also include notes to the financial statements, which explain some of the information in the basic financial statements in greater detail.

Financial Analysis of ECIC

The principal activities of ECIC in fiscal years 2006-07 and 2005-06 were twofold. One set of activities was focused on providing strategic planning, outcome measures, training, and parent and advocacy group coordination for early childhood services through the continued support of ISDs and Regional Educational Service Agencies by establishing Great Start Collaboratives. ECIC established 14 and 7 Great Start Collaboratives in fiscal years 2005-06 and 2006-07, respectively, for a total of 21 Collaboratives. ECIC is organized to provide ongoing and comprehensive technical assistance to the Great Start Collaboratives. The second set of activities was focused on improving the quality of child care in Michigan. For example, through contractual relationships, ECIC funded professional development for child care providers, a Statewide system of resources and referral for families with child care needs, and publications to improve the knowledge and skills of child care providers.

It is important to note that ECIC was not fully operational until May of fiscal year 2005-06. For example, major contracts that ECIC administers such as Professional Development, Research and Referral and Teacher Education and Compensation Helps (T.E.A.C.H.) were not in place until January 2006 and April 2006, respectively. In addition, in August 2006, ECIC moved from full in-kind support from DHS in the Grand Tower to its current suite of offices at 221 North Pine Street in Lansing. Consequently, because fiscal year 2006-07 was the first full year of operation for ECIC, results of a comparison between fiscal years 2006-07 and 2005-06 are generally not comparable.

Condensed Entity-Wide Financial Information
From the Statement of Net Assets and Statement of Activities
As of and for the Fiscal Years Ended September 30

	2007	2006
<u>Statement of Net Assets</u>		
Total assets	\$ 6,146,988	\$ 3,049,455
Total liabilities	3,879,898	2,771,932
Net assets		
Unrestricted	\$ 2,267,090	\$ 277,523
Total net assets*	\$ 2,267,090	\$ 277,523
<u>Statement of Activities</u>		
Expenses:		
Grants and operations	\$16,530,636	\$ 8,815,633
Total program expenses	\$16,530,636	\$ 8,815,633
Program Revenues:		
Operating grants	\$17,427,601	\$ 9,092,137
Contributions	5,543	1,019
Payments from the State of Michigan	1,000,000	
Total program revenues	\$18,433,144	\$ 9,093,156
Net program revenues	\$ 1,902,508	\$ 277,523
General Revenues:		
Interest earned	\$ 87,059	\$
Total general revenues	\$ 87,059	\$ 0
Increase in net assets	\$ 1,989,567	\$ 277,523
Net assets - Beginning of fiscal year	277,523	
Net assets - Ending of fiscal year	\$ 2,267,090	\$ 277,523

* All of ECIC's funding supports designated initiatives that are aligned with specific purposes defined by contracts with the State and public agencies. The designated initiatives are not narrower in scope than ECIC's primary purpose and functions. Consequently, ECIC's assets are not restricted.

Total assets primarily consist of cash and amounts due from DHS and the Department of Community Health. Total assets increased by \$3.1 million in fiscal year 2006-07 primarily because of a \$2.1 million grant received in fiscal year 2006-07 from the Kellogg Foundation, of which ECIC used only a small portion by fiscal year-end. Also, there was an increase in reimbursement requests for federal funds related to an increase in activity associated with the addition of seven Great Start Collaborative contracts at ECIC in fiscal year 2006-07.

Total liabilities primarily consist of accounts payable and other liabilities. Total liabilities increased by \$1.1 million in fiscal year 2006-07 primarily because of an increase in expenses associated with the addition of seven new Great Start Collaboratives in fiscal year 2006-07 and the increase in operations of seven other Great Start Collaboratives.

Overall, **net assets** increased by \$2.0 million during fiscal year 2006-07 as a result of the \$2.1 million grant received from the Kellogg Foundation.

Expenses increased by approximately \$7.7 million and primarily consist of federal awards expended (early childhood services grants) and State funds expended (Great Start Collaborative State support). Because ECIC's revenues result from the reimbursement of expenses, the fluctuations in ECIC expenses are directly related to the fluctuations in ECIC revenues. The reason the increase in expenses does not match the increase in revenues is because ECIC did not use the majority of the \$2.1 million received from the Kellogg Foundation.

Revenues primarily consist of grants from federal awards (early childhood services grants), foundations (family support services grants), and appropriations which the Great Start Collaboratives received directly from the State's School Aid Fund (Great Start Collaborative State support). Revenues increased by \$9.4 million in fiscal year 2006-07 primarily because 2006-07 was ECIC's first complete year of operation. The majority of ECIC's revenues result from the reimbursement of expenses. Other factors related to the increase include a \$2.1 million contribution from the Kellogg Foundation and \$1 million in funds received by the Great Start Collaboratives directly from the State's School Aid Fund.

Contacting ECIC

The financial report is designed to present users with a general overview of ECIC's finances and to demonstrate ECIC's accountability for the funds. The contact information for ECIC is:

Michigan Early Childhood Investment Corporation

221 North Pine

Lansing, MI 48933

Web site: www.ecic4kids.org

Judy Samelson, Chief Executive Officer

FINANCIAL STATEMENTS

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION
Statement of Net Assets
As of September 30

	<u>2007</u>	<u>2006</u>
ASSETS		
Current assets:		
Cash (Note 2)	\$ 2,049,685	\$ 207,891
Amounts due from State government	4,088,756	2,784,801
Other current assets	8,547	56,763
Total current assets	<u>\$ 6,146,988</u>	<u>\$ 3,049,455</u>
 Total assets	 <u>\$ 6,146,988</u>	 <u>\$ 3,049,455</u>
 LIABILITIES		
Current liabilities:		
Accounts payable and other liabilities	\$ 3,829,112	\$ 2,704,799
Compensated absences (Note 3)	20,388	20,433
Amounts due to State government	24,867	46,700
Total current liabilities	<u>\$ 3,874,367</u>	<u>\$ 2,771,932</u>
 Long-term liabilities:		
Compensated absences (Note 3)	\$ 5,531	\$
Total long-term liabilities	<u>\$ 5,531</u>	<u>\$ 0</u>
 Total liabilities	 <u>\$ 3,879,898</u>	 <u>\$ 2,771,932</u>
 NET ASSETS		
Unrestricted net assets (Note 4)	<u>\$ 2,267,090</u>	<u>\$ 277,523</u>
 Total net assets	 <u><u>\$ 2,267,090</u></u>	 <u><u>\$ 277,523</u></u>

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

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION
Statement of Activities
For the Fiscal Years Ended September 30

	<u>2007</u>	<u>2006</u>
EXPENSES		
Early childhood services grants (Note 1d)	\$ 15,187,580	\$ 8,797,272
Family support services grants (Note 1d)	327,754	18,361
Great Start Collaborative State support (Note 7)	1,000,000	
Miscellaneous expenses	15,302	
Total program expenses	<u>\$ 16,530,636</u>	<u>\$ 8,815,633</u>
PROGRAM REVENUES		
Operating grants and contributions:		
Early childhood services grants (Note 1d)	\$ 15,207,601	\$ 8,809,137
Family support services grants (Note 1d)	2,220,000	283,000
Contributions	5,543	1,019
Payments from the State of Michigan:		
Great Start Collaborative State support (Note 7)	1,000,000	
Total program revenues	<u>\$ 18,433,144</u>	<u>\$ 9,093,156</u>
Net program revenues	<u>\$ 1,902,508</u>	<u>\$ 277,523</u>
GENERAL REVENUES		
Other		
Interest earnings	\$ 87,059	\$
Total general revenues	<u>\$ 87,059</u>	<u>\$ 0</u>
Increase in net assets	\$ 1,989,567	\$ 277,523
Net assets - Beginning	<u>277,523</u>	<u></u>
Net assets - Ending	<u>\$ 2,267,090</u>	<u>\$ 277,523</u>

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

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION
 Governmental Fund Balance Sheet
As of September 30

	2007	2006
ASSETS		
Current assets:		
Cash (Note 2)	\$ 2,049,685	\$ 207,891
Amounts due from State government	4,088,756	2,784,801
Other current assets	8,547	56,763
Total current assets	\$ 6,146,988	\$ 3,049,455
 Total assets	 \$ 6,146,988	 \$ 3,049,455
 LIABILITIES		
Current liabilities:		
Accounts payable and other liabilities	\$ 3,829,112	\$ 2,704,799
Amounts due to State government	24,867	46,700
Total current liabilities	\$ 3,853,979	\$ 2,751,499
 Total liabilities	 \$ 3,853,979	 \$ 2,751,499
 FUND BALANCE		
Fund balance:		
Unreserved	\$ 2,293,009	\$ 297,956
 Total liabilities and fund balance	 \$ 6,146,988	 \$ 3,049,455

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

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION
 Governmental Fund Statement of Revenues, Expenditures, and Changes in Fund Balance
For the Fiscal Years Ended September 30

	2007	2006
REVENUES		
Early childhood services grants (Note 1d)	\$ 15,207,601	\$ 8,809,137
Family support services grants (Note 1d)	2,220,000	283,000
Great Start Collaborative State support (Note 7)	1,000,000	
Interest earnings	87,059	
Contributions	5,543	1,019
Total revenues	\$ 18,520,203	\$ 9,093,156
EXPENDITURES		
Early childhood services grants (Note 1d)	\$ 15,182,094	\$ 8,780,070
Family support services grants (Note 1d)	327,754	15,130
Great Start Collaborative State support (Note 7)	1,000,000	
Miscellaneous expenditures	15,302	
Total expenditures	\$ 16,525,150	\$ 8,795,200
Excess of revenues over expenditures	\$ 1,995,053	\$ 297,956
Fund balance - Beginning	297,956	
Fund balance - Ending	\$ 2,293,009	\$ 297,956

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

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION
 Reconciliation of the Governmental Fund Balance Sheet
 to the Statement of Net Assets
As of September 30

	<u>2007</u>	<u>2006</u>
Total fund balance	\$ 2,293,009	\$ 297,956
Amounts reported for governmental activities in the statement of net assets are different because:		
Compensated absences liabilities are not due and payable in the current period and, therefore, are not reported in the governmental fund statement	<u>(25,919)</u>	<u>(20,433)</u>
Net assets of governmental activities	<u>\$ 2,267,090</u>	<u>\$ 277,523</u>

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION

Reconciliation of the Governmental Fund Statement of Revenues, Expenditures,
and Changes in Fund Balance to the Statement of Activities
For the Fiscal Years Ended September 30

	<u>2007</u>	<u>2006</u>
Net change in fund balance	\$ 1,995,053	\$ 297,956
Amounts reported for governmental activities in the statement of activities are different because:		
Expenses for compensated absences are not recorded as expenditures for purposes of net assets	<u>(5,486)</u>	<u>(20,433)</u>
Change in net assets of governmental activities	<u><u>\$ 1,989,567</u></u>	<u><u>\$ 277,523</u></u>

Notes to the Financial Statements

Note 1 Significant Accounting Policies

The accounting policies of the Michigan Early Childhood Investment Corporation (ECIC) 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

ECIC was established through an interlocal agreement on February 22, 2005, pursuant to the Urban Cooperation Act of 1967 (Act 7, P.A. 1967 [Ex. Sess.], Sections 124.501 - 124.512 of the *Michigan Compiled Laws*) between the Department of Human Services (DHS), a principal department of the State of Michigan, and participating intermediate school districts (ISDs), bodies corporate established as authorized under Part 7 of the Revised School Code, Act 451, P.A. 1976, as amended.

ECIC was developed as a separate legal entity and public body corporate to administer activities related to early childhood development and to implement the objectives and further the purposes set forth in the interlocal agreement. These objectives include ensuring that every young child in Michigan has a great start and arrives at the kindergarten door healthy and ready to succeed in school. Each party to the agreement is a public agency under the Urban Cooperation Act of 1967 with the power to carry out the activities described in the agreement.

ECIC is a discretely presented government type component unit of the State of Michigan and is governed by the Corporation Board, including the Executive Committee. The governing body of each participating ISD is authorized to appoint 1 member to the Corporation Board to serve at the will of the ISD. For each ISD-appointed member, the Governor shall appoint up to 2 members to the Corporation Board that represent the State and serve at the will of the Governor. If there are fewer than 5 ISD participants, the Governor may appoint up to 12 additional members to the Corporation Board that represent the State and serve at the will of the Governor until there are 5 or more participating ISDs. The Executive Committee consists of 15 members. The members of the Executive

Committee include the director of DHS or his or her designated representative from within DHS and 14 residents of Michigan appointed by the Governor, all of whom are also Corporation Board members. The members appointed by the Governor include at least one resident representing the participating ISDs.

On December 19, 2006, the Executive Committee of the Corporation approved an amendment to the bylaws to expand membership on the Executive Committee to include one member appointed by the Senate Majority Leader, one member appointed by the Senate Minority Leader, one member appointed by the Speaker of the House of Representatives, and one member appointed by the Minority Leader of the House of Representatives. This bylaw change was in accordance with Section 32b.(1)(b), Act 342, P.A. 2006.

b. Financial Statement Presentation

ECIC is a discretely presented component unit of the State of Michigan. Under 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. ECIC's operations are accounted for in a separate set of self-balancing accounts that comprise its assets, liabilities, fund balances, revenues, and expenditures. Government resources are allocated to and accounted for in separate funding source accounts, based upon the purposes for which they are to be spent and the means by which spending activities are controlled.

ECIC is a governmental fund. The accompanying financial statements present only ECIC. Accordingly, they do not purport to, and do not, present fairly the financial position and the changes in financial position of the State of Michigan or its component units in conformity with accounting principles generally accepted in the United States of America.

c. Measurement Focus and Basis of Accounting

The fund level financial statements contained in this report are presented using the current financial resources measurement focus and the modified accrual basis of accounting as provided by accounting principles generally accepted in the United States of America. Under the modified accrual basis of accounting, revenues are recognized as they become susceptible

to accrual, generally when they are both measurable and available. Revenues are considered to be available when they are collected within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when a liability is incurred; however, certain expenditures related to long-term obligations are recorded only when payment is due and payable.

Governmental Accounting Standards Board (GASB) Statement No. 34 requires ECIC to provide financial statements prepared on both the modified accrual basis of accounting (fund level presentation) and the full accrual basis of accounting (entity-wide level presentation).

d. Financial Data

ECIC's financial statements primarily present the following:

- (1) Revenues consist of early childhood services grants, family support services grants, Great Start Collaborative State support, interest earnings, and contributions.
 - (a) Early childhood services grants are revenues from federal agencies provided to ECIC by DHS and the Department of Community Health as pass-through grants which consist of the Child Care and Development Block Grant and the Maternal and Child Health Federal Consolidated Program. Also included are revenues from DHS for Head Start State Collaboration Office activities and in-kind support for DHS employee salaries and benefits.
 - (b) Family support services grants are revenues and in-kind support received directly from foundations which include the Kellogg Foundation, Council of Michigan Foundations, Build Initiative, and National Smart Start Technical Assistance Center (in-kind support).
 - (c) Great Start Collaborative State support is the funding provided by the Michigan Department of Education directly to the Great Start Collaboratives pursuant to Section 32b.(1), Act 342,

P.A. 2006, to support ECIC's purpose in providing early childhood services throughout Michigan.

(d) Interest earnings are amounts earned from funds held in ECIC's money market account.

(e) Contributions are amounts received from non-federal and non-foundation sources and include private donations.

(2) Expenditures consist of early childhood services grants, family support services grants, Great Start Collaborative State support, and miscellaneous expenditures funded primarily with DHS and Department of Community Health pass-through grants, foundation grants, and earned interest.

(a) Early childhood services grant expenditures are primarily for services in the following areas:

- Child care resource/referral and training for providers.
- Public education materials for consumers.
- A portion of administrative costs.
- Technical assistance for ISDs and Regional Educational Service Agencies (RESAs).
- Parent engagement in early childhood.
- Public engagement in early childhood.

(b) Family support service grant expenditures are primarily for services in the following areas:

- Costs associated with launching a new organization, particularly technical assistance, consulting, and organizational infrastructure that use funds received directly from foundations.
- Development of a sustainable funding plan for both ECIC and Great Start Collaboratives.
- Funding Great Start Collaboratives and increasing their numbers.

- Communication activities focused on building public awareness.
- Building stronger State/local connections to support early learning systems.

Note 2 Deposits and Investments

a. Deposits

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of a depository financial institution's failure, ECIC's deposits may not be returned to it.

Deposits reflected in ECIC's bank accounts (without recognition of outstanding checks or deposits in transit) as of September 30, 2007 and September 30, 2006 were \$2,075,336 and \$225,616, of which \$1,875,336 and \$125,616, respectively, were not covered by federal depository insurance and were uncollateralized and, hence, were exposed to custodial credit risk. ECIC does not have a policy for limiting custodial credit risk.

b. Investments

No investment activities occurred during the fiscal years 2006-07 and 2005-06.

Note 3 Long-Term Liabilities

Long-term liabilities are accrued when incurred. The following table summarizes the compensated absences liabilities of ECIC for the fiscal years ended September 30, 2007 and September 30, 2006, respectively:

		Fiscal Year 2006-07					
		Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year	Amounts Due Thereafter
Compensated Absences		\$20,433	\$46,307	\$40,821	\$25,919	\$20,388	\$5,531

		Fiscal Year 2005-06					
		Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year	Amounts Due Thereafter
Compensated Absences		\$0	\$23,750	\$3,317	\$20,433	\$20,433	\$0

Note 4 Unrestricted Net Assets

Unrestricted net assets consist of net assets that do not have constraints, that is, they are not narrower in scope than an entity's primary purpose, placed on their use either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation. Unrestricted net assets often are designated for specific purposes that can be modified. All of ECIC's funding supports designated initiatives that are aligned with specific purposes defined by contracts with the State and public agencies. The designated initiatives are not narrower in scope than ECIC's primary purpose and functions.

Note 5 Postemployment Benefits

ECIC does not participate in the State of Michigan defined benefit or defined contribution plans. ECIC's management established a 457(b) defined contribution plan in August 2006, which the Executive Committee formally approved on January 9, 2008, to provide benefits at retirement to its employees. Upon establishment, employer contributions to the 457(b) plan were retroactive to the employees' hire date. During fiscal years 2006-07 and 2005-06, the plan required ECIC to contribute 4% and match any voluntary employee contributions up to 3% of an employee's salary to the 457(b) plan. ECIC contributions to the 457(b) plan for fiscal year 2006-07 and 2005-06

totaled \$43,132 and \$19,923, respectively. Employee contributions to the 457(b) plan for fiscal years 2006-07 and 2005-06 totaled \$57,450 and \$8,254, respectively. John Hancock Financial Services administered the 457(b) plan.

Subsequent to the fiscal year ended September 30, 2007, ECIC's management established a 401(a) defined contribution plan in November of 2007, which the Executive Committee approved on November 19, 2007. The 401(a) plan requires ECIC to make employer contributions of 4% and match any employee contributions up to 3% to the 401(a) plan. Any voluntary employee contributions are placed in the 457(b) plan. In March 2008, ECIC transferred employer contributions from the 457(b) plan that were contributed from January 1, 2007, through September 30, 2007, to the 401(a) plan. The 401(a) plan is also administered by John Hancock Financial Services.

ECIC does not provide retired employees with health, dental, and vision benefits or life insurance coverage.

Note 6 Differences in Reporting From the SOMCAFR

ECIC's financial statements were adjusted for the fiscal years ended September 30, 2007 and September 30, 2006 from the amounts reported in the fiscal years 2006-07 and 2005-06 *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)* as a result of this audit and the prior financial audit for the fiscal year ended September 30, 2006. Current assets, total liabilities, expenses, revenues, and total net assets increased by approximately \$1.6 million, \$15,000, \$1.5 million, \$3.1 million, and \$1.6 million, respectively, from the amounts reported in the fiscal year 2006-07 *SOMCAFR*. Current assets, restricted assets, total liabilities, and expenses decreased by approximately \$304,000, \$203,000, \$521,000, and \$14,000, respectively, and total net assets increased by approximately \$15,000 from the amounts reported in the fiscal year 2005-06 *SOMCAFR*. The Office of Financial Management, Department of Management and Budget, issued a waiver for fiscal years 2006-07 and 2005-06 which allows for this different presentation from that reported in the two *SOMCAFRs*.

Note 7 Revenues From School Aid Fund

Section 32b.(1), Act 342, P.A. 2006, required that the School Aid Fund would allocate an amount not to exceed \$1.0 million for fiscal year 2006-07 for competitive grants to ISDs, Regional Educational Service Districts (RESDs),

and RESAs for the creation of great start communities or other community purposes as identified by ECIC. Through an electronic funds transfer on January 20, 2007, MDE advanced \$1.0 million in School Aid Funds to the Great Start Collaboratives, composed of 21 ISDs, RESDs, and RESAs, based on an allocation determined by ECIC. When an ISD, RESD, and RESA submitted its statement of expenditures for reimbursement, ECIC reduced the amount of the reimbursement request by the portion of the advance still outstanding.

Note 8 Subsequent Events

- a. On October 1, 2007, the Kresge Foundation notified ECIC that the trustees of that Foundation approved a grant of \$1,280,000 toward the first of two year's support of early childhood collaboratives in Wayne, Oakland, and Macomb Counties, and capacity-building for ECIC. The notification also stated that the Foundation trustees had approved their intention to make a grant of \$1,455,000 for the second of two year's support for the same purpose. The total Kresge Foundation Grant is \$2,735,000.

- b. Section 32b.(1), Act 137, P.A. 2007, increased the amount of State support to be provided to Great Start Collaboratives from \$1,000,000 for fiscal year 2006-07 to \$1,750,000 for fiscal year 2007-08. This will enable ECIC to establish contracts with 11 additional ISDs and RESDs from April 1, 2008 through September 30, 2008. Those collaboratives are Bay-Arenac ISD, Berrien County ISD, Clare-Gladwin RESD, Copper Country ISD, Delta-Schoolcraft ISD, Lenawee ISD, Midland County Educational Service Agency, Macomb ISD, Montcalm Area ISD, Traverse Bay Area ISD, and Washtenaw ISD.

SUPPLEMENTAL
FINANCIAL SCHEDULE

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION
Schedule of Expenditures of Federal Awards (Note 1)
For the Period October 1, 2005 through September 30, 2007

Federal Agency/Program or Cluster	CFDA (Note 2) Number	Pass-Through Identification Number	For the Fiscal Year Ended September 30, 2006		
			Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
U.S. Department of Health and Human Services					
CCDF Cluster:					
Pass-Through Program:					
Michigan Department of Human Services					
Child Care and Development Block Grant (Notes 3 and 4)	93.575		\$ 2,296,205	\$ 6,065,730	\$ 8,361,935
Total CCDF Cluster			<u>\$ 2,296,205</u>	<u>\$ 6,065,730</u>	<u>\$ 8,361,935</u>
Pass-Through Programs:					
Michigan Department of Community Health					
Maternal and Child Health Federal Consolidated Program	93.110	H25MC00252	\$ 82,878		\$ 82,878
Total U.S. Department of Health and Human Services			<u>\$ 2,379,083</u>	<u>\$ 6,065,730</u>	<u>\$ 8,444,813</u>
Total Expenditures of Federal Awards			<u>\$ 2,379,083</u>	<u>\$ 6,065,730</u>	<u>\$ 8,444,813</u>

(1) Basis of Presentation: This schedule presents the federal grant activity of the Michigan Early Childhood Investment Corporation (ECIC) on the modified 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 basic financial statements. As a result, the amounts reported as expended on this schedule do not agree with the amounts reported as federal revenue (Early Childhood Services Grants) in the statement of activities and governmental fund statement of revenues, expenditures, and changes in fund balance. ECIC received federal revenue of \$177,062 and \$82,468 for fiscal years 2006-07 and 2005-06, respectively, for providing services to the Head Start State Collaboration Office with the Michigan Department of Human Services (DHS). Because ECIC has a vendor relationship with DHS, these amounts are not federal assistance so they are not included on this schedule. Also, ECIC reported actual amounts paid and provided from its vendors and subrecipients subsequent to the fiscal year-end for its payables on the schedule of expenditures of federal awards instead of estimated payables and correlating amounts due from State government on its statement of net assets and governmental fund balance sheet. This resulted in a difference of approximately \$251,000 for fiscal year 2005-06.

(2) CFDA is defined as *Catalog of Federal Domestic Assistance*.

(3) In-Kind Assistance: As part of the Child Care and Development Block Grant, DHS provided in-kind assistance to ECIC in the form of personnel and equipment for the administration of the program in the amount of \$142,074 and \$206,714 for fiscal years 2005-06 and 2006-07, respectively.

(4) There is no pass-through identification number associated with the Child Care and Development Block Grant.

For the Fiscal Year Ended September 30, 2007

Directly Expended	Distributed to Subrecipients	Total Expended and Distributed	Total Expended and Distributed for the Two-Year Period
\$ 6,608,828	\$ 8,274,236	\$ 14,883,064	\$ 23,244,999
<u>\$ 6,608,828</u>	<u>\$ 8,274,236</u>	<u>\$ 14,883,064</u>	<u>\$ 23,244,999</u>
\$ 140,000	\$	\$ 140,000	\$ 222,878
<u>\$ 6,748,828</u>	<u>\$ 8,274,236</u>	<u>\$ 15,023,064</u>	<u>\$ 23,467,877</u>
<u>\$ 6,748,828</u>	<u>\$ 8,274,236</u>	<u>\$ 15,023,064</u>	<u>\$ 23,467,877</u>

INDEPENDENT AUDITOR'S REPORTS ON INTERNAL CONTROL AND COMPLIANCE



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

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

Ms. Susan K. Broman, Chair
Michigan Early Childhood Investment Corporation Board
and
Ms. Judy Samelson, Chief Executive Officer
Michigan Early Childhood Investment Corporation
221 North Pine
Lansing, Michigan

Dear Ms. Broman and Ms. Samelson:

We have audited the financial statements of the Michigan Early Childhood Investment Corporation, a discretely presented component unit of the State of Michigan, as of and for the fiscal years ended September 30, 2007 and September 30, 2006, as identified in the table of contents, and have issued our report thereon dated October 14, 2009. 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 Early Childhood Investment Corporation's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Michigan Early Childhood Investment Corporation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Michigan Early Childhood Investment Corporation's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed in the next paragraph, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in

Finding 1 in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we consider the significant deficiencies identified in the third paragraph of this section to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Michigan Early Childhood Investment 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*.

The Michigan Early Childhood Investment Corporation's responses to the findings identified in our audit are described in the accompanying corrective action plan. We did not audit the Corporation's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Governor, the Legislature, the Michigan Early Childhood Investment Corporation Board, management, others within the entity, 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

October 14, 2009



STATE OF MICHIGAN
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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

Ms. Susan K. Broman, Chair
Michigan Early Childhood Investment Corporation Board
and
Ms. Judy Samelson, Chief Executive Officer
Michigan Early Childhood Investment Corporation
221 North Pine
Lansing, Michigan

Dear Ms. Broman and Ms. Samelson:

Compliance

We have audited the compliance of the Michigan Early Childhood Investment 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 its major federal program for the two-year period ended September 30, 2007. The Michigan Early Childhood Investment 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 Early Childhood Investment Corporation's management. Our responsibility is to express an opinion on the Michigan Early Childhood Investment 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 preceding 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 Early Childhood Investment 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 Early Childhood Investment Corporation's compliance with those requirements.

In our opinion, the Michigan Early Childhood Investment Corporation complied, in all material respects, with the requirements referred to in the first paragraph that are applicable to its major federal program for the two-year period ended September 30, 2007. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as Finding 2.

Internal Control Over Compliance

The management of the Michigan Early Childhood Investment 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 Early Childhood Investment 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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Michigan Early Childhood Investment Corporation's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the Michigan Early Childhood Investment Corporation's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as Finding 2 to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. We did not consider any of the deficiencies described in the preceding paragraph to be material weaknesses.

The Michigan Early Childhood Investment Corporation's responses to the findings identified in our audit are described in the accompanying corrective action plan. We did not audit the Michigan Early Childhood Investment Corporation's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Governor, the Legislature, the Michigan Early Childhood Investment Corporation Board, management, others within the entity, 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

October 14, 2009

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?	Yes
Significant deficiencies* identified that are not considered to be material weaknesses?	No
Noncompliance or other matters material to the financial statements noted?	No

Federal Awards

Internal control over major programs:	
Material weaknesses identified?	No
Significant deficiencies identified that are not considered to be material weaknesses?	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

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
93.575	Child Care and Development Fund (CCDF) Cluster

Dollar threshold used to distinguish between type A and type B programs:	\$704,036
Auditee qualified as a low-risk auditee*?	No

* See glossary at end of report for definition.

Section II: Findings Related to the Financial Statements

FINDING 4310801

1. Internal Control

The Michigan Early Childhood Investment Corporation (ECIC) had not established comprehensive internal control. As a result, ECIC was at an increased risk for fraud, accounting and financial reporting errors, and noncompliance with both federal and private grant agreements.

ECIC is responsible for the establishment of internal control that is designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness* and efficiency* of operations, and compliance with applicable laws and regulations. An entity's internal control generally has five components: the control environment, the entity's risk assessment process, information and communication systems, control activities, and monitoring.

As required by generally accepted auditing standards, we obtained an understanding of ECIC's internal control in order to plan our audit. In obtaining our understanding, we identified significant deficiencies and, in some cases, material weaknesses in ECIC's internal control:

- a. In obtaining our understanding of ECIC's control environment, we noted that ECIC staff did not have a sound understanding of governmental financial accounting and reporting requirements and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, requirements. This created difficulties for ECIC in identifying what financial statements and schedules needed to be prepared and in preparing them in accordance with generally accepted accounting principles. The financial statements prepared by ECIC for inclusion in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)* were materially misstated. For ECIC's own reporting purposes, ECIC requested and received a waiver from the Department of Management and Budget to correct the misstatements and issue financial statements different from those issued as a part of the *SOMCAFR*. We consider this to be a material weakness in internal control.

* See glossary at end of report for definition.

- b. In obtaining our understanding of ECIC's information and communication systems, we noted that ECIC did not maintain accounts payable and accounts receivable subsidiary ledgers. These subsidiary records, when maintained, would help minimize errors in ECIC's statement of net assets. They would also provide the necessary supporting documentation for the amounts reported on the statement.

- c. In obtaining our understanding of ECIC's control activities, we noted that ECIC had not established control activities that ensured the proper segregation of duties, the accuracy of financial statement presentations, or the maintenance of adequate supporting documentation. For example:
 - (1) ECIC allowed one individual to make deposits, record and modify transactions, generate checks, and perform the bank reconciliation. Also, while ECIC may occasionally receive miscellaneous donations through the mail, ECIC had assigned only one employee to open the mail at any point in time.

 - (2) ECIC did not have a process to reconcile its financial statements to supporting records to ensure the accuracy of the financial statement presentations.

 - (3) ECIC did not maintain documentation to support adjusting entries.

 - (4) ECIC did not maintain documentation to support employer and employee retirement contributions.

- d. In our review of ECIC's monitoring activities, we noted exceptions that indicated that ECIC's monitoring efforts were limited:
 - (1) ECIC's expenditures were not always properly approved. ECIC's procedure for expenditures over \$100,000 requires a secondary approval by a member of the Executive Committee of ECIC's Corporation Board. However, as noted in Finding 2, we identified 5 expenditures totaling \$1.2 million that did not have the required Executive Committee member's approval prior to the release of the check. One check of \$406,000 was not approved by the Executive Committee member until after the payment cleared the bank.

- (2) ECIC did not detect that it had overcontributed approximately \$1,800 and \$1,400 to two different employees' defined contribution plans.
- (3) ECIC did not detect that it had paid an employee twice for the same pay period. As of September 30, 2007, the duplicate wages had not been recovered.

We reported a similar condition in our prior financial audit of ECIC (431-1100-07) in March 2008. ECIC informed us that it agreed and that it had begun corrective action in fiscal year 2007-08.

RECOMMENDATION

We recommend that ECIC establish comprehensive internal control to prevent and detect fraud, to ensure accurate accounting and financial reporting, and to ensure federal program compliance.

Section III: Findings and Questioned Costs* Related to Federal Awards

FINDING 4310802

2. Child Care and Development Fund (CCDF) Cluster, CFDA 93.575

U.S. Department of Health and Human Services	CCDF Cluster: CFDA 93.575: Child Care and Development Block Grant
Award Numbers: G 07 01 MI CCDF G 07 01 MI CCDF	Award Periods: 10/01/2005 - 09/30/2006 10/01/2006 - 09/30/2007
Pass-Through Entity: Michigan Department of Human Services	Known Questioned Costs: \$571,109

ECIC's internal control over the CCDF Cluster did not ensure its compliance with federal laws and regulations regarding allowable costs/cost principles, procurement and suspension and debarment, and subrecipient* monitoring. Our review disclosed significant deficiencies in internal control over compliance requirements related to allowable costs/cost principles, procurement and suspension and

* See glossary at end of report for definition.

debarment, and subrecipient monitoring. As a result, we identified known questioned costs of \$571,109 and known and likely questioned costs of \$576,781.

Internal control that does not ensure compliance with State and federal laws and regulations could result in sanctions, disallowances, and/or future reductions in CCDF Cluster awards.

Federal expenditures for the CCDF Cluster totaled \$23,244,999 for the two-year period ended September 30, 2007. ECIC expended federal financial assistance under only the Child Care and Development Block Grant (CFDA 93.575), 1 of the 2 programs included in the cluster.

Our exceptions, by compliance area, are as follows:

a. Allowable Costs/Cost Principles

ECIC's internal control did not ensure that expenditures were in compliance with federal laws and regulations regarding allowable costs/cost principles. As a result, we questioned costs in the amount of \$24,001. Our tests disclosed:

- (1) ECIC did not return federal funds that were received through reimbursement, after an audit adjustment subsequently reduced the expenditures that supported the amount reimbursed. Appendix A, section C.4. of OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments* (Title 2, Part 225 of the *Code of Federal Regulations* [CFR]), requires that a reduction of expenditure-type transactions allocated to federal awards as a direct cost shall be credited to the Federal award either as a cost reduction or cash refund. ECIC requested and received reimbursement for expenditures incurred in fiscal year 2005-06 related to the CCDF Cluster. Subsequent to this reimbursement, ECIC reduced a portion of these expenditures as a result of a financial audit but did not return the federal funds after the adjustment. As a result, we questioned costs totaling \$17,202.
- (2) ECIC did not calculate retirement contributions in accordance with the requirements established within its 457(b) retirement plan for ECIC employees and ECIC's employee handbook. Appendix B, section 8.d.(5) of OMB Circular A-87 (federal regulation 2 CFR 225) states that pension

costs are allowable provided such costs are granted under established policies. As a result, we questioned costs totaling \$5,919.

- (3) ECIC did not have an effective process to identify original documentation used to support contract expenditures previously submitted for reimbursement. Consequently, ECIC sought federal reimbursement for a fiscal year 2006-07 contract expenditure twice. If ECIC had a process to cancel invoices upon payment, it would reduce the risk of requesting duplicate reimbursement for the same expenditure. Appendix A, section C.1.j. of federal regulation 2 *CFR* 225 requires that costs charged to federal awards be adequately documented. We questioned costs in the amount of \$750 for fiscal year 2006-07.
- (4) ECIC did not obtain adequate documentation to support the amount paid for 1 (1%) of 82 nonpayroll related expenditures. ECIC paid one vendor \$65 more than the amount supported by the original billing detail. Appendix A, section C.1.j. of OMB Circular A-87 (federal regulation 2 *CFR* 225) requires that costs charged to federal awards be adequately documented. As a result, we questioned costs totaling \$65.
- (5) ECIC did not meet the requirements set forth in its contracts and grant agreements related to the CCDF Cluster. OMB Circular A-133, Section 300(c), requires ECIC to comply with the provisions of contracts and grant agreements related to federal programs. Our review disclosed:
 - (a) ECIC inappropriately included travel expenditures incurred in August and September 2006 on its October 2006 monthly statement of expenditures for 1 (5%) of 22 expenditures reviewed. ECIC's Establishment Grant Agreement with the Department of Human Services (DHS) for fiscal year 2006-07 required that the monthly statement of expenditures must reflect total actual program expenditures incurred in that month. Also, because ECIC's grant agreements with DHS are only for a period of one year (October 1 through September 30), ECIC cannot receive reimbursement for an expenditure incurred during a prior grant agreement period. As a result, we questioned costs in the amount of \$65.

- (b) ECIC inappropriately paid \$585 more to one of its subrecipients than required in the contract. Federal regulation 45 *CFR* 98.60(f) also requires contract advances to be limited to the minimum amount needed. Advance contract payments in excess of the amount stipulated in a contract represent more than the minimum amount needed. These costs were not questioned because they were eventually recouped from the subrecipient.
- (6) As discussed in the procurement and suspension and debarment section (part b. of this finding), ECIC did not document the significant histories of all contracts it procured. We questioned costs of \$547,108 in the procurement and suspension and debarment section (part b. of this finding).
- (7) Controls established by ECIC to ensure that expenditures charged to federal grants are allowable include a requirement that all checks will be subject to a second review and approval before they are issued. In our audit of the process, we identified 4 (6%) of 65 expenditures that did not have the proper authorization. ECIC paid for 2 expenditures that did not have a date associated with the approval signature and 2 expenditures that had check request approvals dated after the checks were written. Without proper approval, there is an increased risk that ECIC could issue payment for expenditures not allowed by federal laws and regulations. However, because we determined that the expenditures were approved by the appropriate individual subsequent to the payment being issued, we did not question the costs of these expenditures.
- (8) As a control to limit the risk of the significant misappropriation of assets, ECIC procedures require that an Executive Committee member approve check requests for payment before checks are issued for amounts greater than \$100,000. In our audit, we identified 5 expenditures greater than \$100,000 that did not have the required Executive Committee member's approval, including one which was not approved by the Corporation Board until after the check was cashed.
- (9) ECIC did not have a process to obtain semiannual payroll certifications for employees that charged 100% of their time to the CCDF Cluster. Subsequent to the audit period, ECIC obtained a payroll certification for

the entire audit period for each applicable employee after being informed of the requirement by the auditors.

Appendix B, section 8.h.(3) of OMB Circular A-87 (federal regulation 2 *CFR* 225) requires employees who are expected to work solely on a single federal award to periodically certify that the employees did work solely on that program for the period covered by the certifications. The certifications must be prepared at least semiannually and must be signed by the employee or supervisory official having firsthand knowledge of the work performed by the employee.

b. Procurement and Suspension and Debarment

ECIC's internal control did not ensure that all expenditures requiring contracts were awarded in accordance with federal laws and regulations. As a result, we questioned costs in the amount of \$547,108. Our tests disclosed:

- (1) ECIC did not maintain any documentation to detail the significant histories for 40 (56%) of 71 contracts it procured, as required by federal regulation 45 *CFR* 92.36(b)(9).

Federal regulation 45 *CFR* 92.36(b)(9) requires that grantees and subgrantees maintain records sufficient to detail the significant history of a procurement, including the rationale for the method of procurement, selection of contract type, contractor selection or rejection, and basis for contract price.

- (2) ECIC's procurement policies and procedures did not ensure that all contracts entered into during the audit period were through a request-for-proposal process as required by federal regulations and State laws.

Federal regulation 45 *CFR* 92.36(b)(1) requires grantees and subgrantees to use their own procurement procedures, which reflect applicable State laws. Section 678(2), Act 345, P.A. 2006, and Section 678, Act 147, P.A. 2005, require that ECIC bid out all contracts through a Statewide request-for-proposal process.

c. Subrecipient Monitoring

ECIC's internal control did not ensure that activities concerning subrecipients were in compliance with federal laws and regulations. Our tests disclosed that ECIC did not effectively monitor the activities of one of its subrecipients as necessary to ensure that the federal award expenditures were in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals were achieved, as required by OMB Circular A-133, Section 400(d)(3). ECIC allowed one subrecipient to submit 6 (86%) of 7 billings totaling \$628,718, which exceeded its 90-day contract requirement, at least 120 days after the end of a billing period for fiscal year 2005-06. As a result, ECIC could not review the subrecipient's billings in a timely manner, which limited ECIC's ability to ensure that the subrecipient's activities met federal and contract requirements throughout the fiscal year. Also, ECIC was not able to recoup the subrecipient's contract advance, paid back through monthly billings, in a timely manner. The subrecipient, in coordination with ECIC, improved its billing process and submitted timely billings throughout fiscal year 2006-07.

RECOMMENDATION

We recommend that ECIC improve its internal control over the CCDF Cluster to ensure its compliance with federal laws and regulations regarding allowable costs/cost principles, procurement and suspension and debarment, and subrecipient monitoring.

OTHER SCHEDULE

MICHIGAN EARLY CHILDHOOD INVESTMENT CORPORATION

Corrective Action Plan
As of October 13, 2009

FINDINGS RELATED TO THE FINANCIAL STATEMENTS

Finding Number: 4310801
Finding Title: Internal Control

Management Views: The Michigan Early Childhood Investment Corporation (ECIC) agrees that it will continue to implement effective internal control procedures in order to ensure the reliability of its financial reporting and compliance with State laws and grant agreements. ECIC management would like to take this opportunity to express concern that despite an audit process that began in January 2008 ECIC was not made aware of certain internal control findings until March 2009. ECIC is particularly concerned with the finding that there was a material misstatement in the financial statements published in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*. ECIC notes that the vast majority of this misstatement involving net assets was identified by ECIC management and the appropriate entries were posted to ECIC's accounting system prior to the beginning of the field audit. These entries were also reflected in the draft financial statements submitted by ECIC to the Office of the Auditor General (OAG) at the beginning of the audit. Any misstatements actually identified by the OAG should be considered immaterial both individually and in the aggregate.

Part a.: ECIC is a relatively new entity, and with that comes a learning curve. The first part of the learning curve is making sure one has the right staff members

in place to ensure that the job is being done properly. For the time period of this audit, ECIC was still in process of bringing all financial related aspects in house and no longer using an outside provider to do the monthly accounting and compile financial statements. Since this audit, ECIC has hired both a controller and an accounting clerk to ensure that both Governmental Accounting Standards Board (GASB) and U.S. Office of Management and Budget (OMB) Circular A-133 requirements are adhered to. ECIC was never notified that the statements were not in conformity with accounting principles generally accepted in the United States of America, except in regards to the preparation of the Statement of Federal Expenditures (SEFA). Furthermore, the only previous audit of ECIC's records related solely to the fiscal year 2005-06 financial statements. Since this current audit is the first audit related to the federal awards, ECIC management would have expected to receive a client assistance listing that detailed out all schedules and/or reports that the auditor needed. No such assistance list was provided. ECIC management was simply informed that the OAG would not be preparing the financial statements as it had in the previous year. ECIC management was told to prepare the same statement that the OAG had prepared in the previous year. In the prior audit period, ECIC management had not been required to prepare financial statements so management did not anticipate that ECIC would be required to prepare any A-133 schedules. When the OAG requested the preparation of a SEFA schedule, it was certainly not the expectation of management that a sincere attempt to comply in a timely manner would turn into a finding that management lacked knowledge of federal requirements. ECIC management understands that going forward the responsibility to prepare the SEFA

falls solely on management. The financial statements did include differences as compared to the *SOMCAFR*. ECIC management properly requested and received a waiver regarding the differences from the Office of Financial Management. Due to the nature of the ECIC, we do expect to have some differences as compared to *SOMCAFR*, but have put procedures in place to help keep these immaterial.

Part b.: ECIC believes that due to the nature and timing of the vendors and subcontractors we do business with, that there will always be some type of adjustments in receivables and payables relating to our subrecipients requests for reimbursements. We are striving to implement a reasonable way to estimate what the final payments to the subrecipients will be on an annual basis, as to minimize the adjustments needed. ECIC maintained subsidiary ledgers for fiscal year 2007-08 and will continue to do so.

Part c.(1): ECIC has brought in additional personnel in the accounting department to help with the segregation of duties. As for the one person opening mail, ECIC believes that the cost-benefit to hiring additional people to help perform this duty is lacking, and feels that having other individuals cover this duty as needed, is a sufficient control, as ECIC does not solicit donations, so very few, if any, donations come in during any given fiscal year, and they are in no way material to the financial statements taken as a whole.

Part c.(2): ECIC has established a monthly review process to verify that all requests agree with the detail listed in the general ledger, thus agreeing monthly will help to verify the total amounts requested/received on an annual basis.

Part c.(3): ECIC believes that with the additional personnel added to the accounting department, that we will be better suited to maintaining control over adjustments and the documents supporting them.

Part c.(4): ECIC has implemented procedures to ensure that the retirement contributions are calculated properly on both a pay period and an annual basis; ECIC believes that this will properly support all retirement contributions for subsequent periods.

Part d.(1): ECIC's policies and procedures are quite clear in regard to approvals required for check requests and checks. ECIC believes that in no instance was a check released without the appropriate approvals. In the future, ECIC will not only continue to follow its internal control procedures but also will take extra steps to ensure that all signatories have dated the check or the check requests correctly.

ECIC has brought in additional personnel to help the accounting department verify that this procedure is followed at all times.

Part d.(2): During the period under audit, ECIC did over-contribute to two employees' retirement plans. Steps have been put in place to correct this overage, in the following period, as well as, to monitor retirement contributions going forward.

Part d.(3): ECIC has put a wage recalculation into place to verify the wages paid out are correct. Also, the overpaid employee has worked out a plan to payback the excess wages.

Corrective Action:

ECIC has undertaken the following steps in order to improve its system of internal controls:

During fiscal year 2006-07, ECIC retained the services of Plante Moran to draft financial policies and procedures. The manual was expanded and updated during 2008 by an independent consultant retained by ECIC. The manual underwent a thorough review by the Department of Human Services (DHS) and is awaiting implementation and approval of the ECIC Board of Directors.

After the abrupt departure of ECIC's contractual accountant in early 2007, ECIC retained the services of Plante Moran to maintain the accounting records and produce monthly financial statements. Plante Moran began the process of transitioning ECIC's financial records to the Peachtree accounting software.

In April 2008, ECIC hired a Certified Public Accountant as an ECIC employee and began an orderly in-house transition of the accounting functions away from Plante Moran.

The new accountant focused her attention on internal controls and implemented compensating controls, improvements in the segregation of duties for opening mail and check processing, financial grant management oversight procedures, documentation of financial transactions, and the creation of subsidiary ledgers.

DHS has authorized the creation of an additional contract administrator to assist in the monitoring of Great Start Collaborative contracts. The position was filled in early 2009.

ECIC also added an additional position to the accounting function in early 2009.

Anticipated Completion Date: August 2009

Responsible Individuals: CEO, CAO, Controller, and contract administrators.

FINDINGS RELATED TO FEDERAL AWARDS

Finding Number: 4310802

Finding Title: Child Care and Development Fund (CCDF) Cluster,
CFDA 93.575

Management Views: ECIC agrees with most but not all of the findings in parts a., b., and c. Specific disagreements are detailed below. ECIC does not believe any of the costs in question should be disallowed since they were made pursuant to valid contracts and were allowable CCDF expenditures in line with ECIC's mission.

Corrective Action: Part a.(1): ECIC reimbursed DHS for the costs in question. The costs in question involved a year-end entry for compensated absences that should not have been reimbursed but rather should have only been recorded in the "Statement of Net Assets" and the "Statement of Activities" portions of the financial statements. The error was one-time and will not reoccur.

Part a.(2): The employee pension contributions have been corrected. ECIC will periodically review its pension contributions during the fiscal year to ensure compliance with established policies and procedures.

Part a.(3): ECIC will ensure that contract expenditures include the appropriate documentation.

Part a.(4): ECIC will ensure that all vendor payments are supported by adequate documentation.

Part a.(5)(a): ECIC has already taken steps to ensure that all staff including contract managers are familiar with accrual accounting procedures so that travel expenditures are recorded against the appropriate fiscal year.

Part a.(5)(b): ECIC recouped the \$585 contract advance.

Part a.(6): See response to parts b.(1) and b.(2).

Part a.(7): ECIC's policies and procedures are quite clear in regard to approvals required for check requests and checks. ECIC believes that in no instance was a check released without the appropriate approvals. In the future, ECIC will not only continue to follow its internal control procedures but also will take extra steps to ensure that all signatories have dated the check or the check requests correctly.

Part a.(8): ECIC's policies and procedures related to expenditure transactions over \$100,000 are quite clear and adequate. Once again, ECIC believes that in no instance was a check released without the appropriate approvals. In the future, ECIC will not only continue to follow its internal control procedures but also will take extra steps to ensure that all signatories have dated the check or check requests correctly.

Part a.(9): ECIC will obtain certifications from employees charged to federal awards at least semiannually.

Part b.(1): ECIC will comply with federal procurement requirements on an ongoing basis. ECIC has updated its Financial Policies and Procedures Manual to comply with federal regulations. In addition, the Establishment Agreement with DHS has been modified to include language that spells out ECIC's small purchase procedure requirements pursuant to federal regulation 45 *CFR* 92.36(d)(4)(i).

Part b.(2): ECIC should be in compliance with State laws going forward now that the boilerplate requirement in the DHS budget bill was modified for fiscal year 2008-09 to reflect the original understanding that the large child care contracts must be bid and not every single purchase no matter how small.

Part c.(1): ECIC will ensure that subrecipient billings are submitted pursuant to contract requirements.

Anticipated Completion Date: August 2009

Responsible Individuals: CEO, CAO, Controller, and contract administrators.

GLOSSARY

Glossary of Acronyms and Terms

CCDF	Child Care and Development Fund.
<i>CFDA</i>	<i>Catalog of Federal Domestic Assistance.</i>
<i>CFR</i>	<i>Code of Federal Regulations.</i>
control deficiency in internal control over federal program compliance	The design or operation of a control that does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect on a timely basis noncompliance with a type of compliance requirement of a federal program.
control deficiency in internal control over financial reporting	The design or operation of a control that does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis.
DHS	Department of Human Services.
ECIC	Michigan Early Childhood Investment Corporation.
effectiveness	Program success in achieving mission and goals.
efficiency	Achieving the most outputs and outcomes practical with the minimum amount of resources.
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 presented fairly in all material respects in conformity with the disclosed basis of accounting.
GAAP	accounting principles generally accepted in the United States of America.

internal control	A process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
ISD	intermediate school district.
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, regulations, contracts, and grants that could have a direct and material effect on major federal programs or on financial schedule and/or financial statement amounts.
material weakness in internal control over federal program compliance	A significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected.
material weakness in internal control over financial reporting	A significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial schedules and/or financial statements will not be prevented or detected.

OAG	Office of the Auditor General.
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.
RESA	Regional Educational Service Agencies.
RESA	Regional Educational Service Agencies.
RESA	Regional Educational Service Agencies.
SEFA	schedule of expenditures of federal awards.
significant deficiency in internal control over federal program compliance	A control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected.
significant deficiency in internal control over financial reporting	A control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial schedules and/or financial statements that is more than inconsequential will not be prevented or detected.

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 <i>Government Auditing Standards</i> 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.
<i>SOMCAFR</i>	<i>State of Michigan Comprehensive Annual Financial Report.</i>
subrecipient	A nonfederal entity that expends federal awards received from another nonfederal entity to carry out a federal program.
unqualified opinion	<p>An auditor's opinion in which the auditor states that:</p> <ol style="list-style-type: none"> <li data-bbox="565 1136 1446 1304">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 <li data-bbox="565 1356 1446 1806">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.

