

Michigan Education Savings Program
(a fiduciary fund of the State of Michigan)

Audited Financial Statements

*Year Ended September 30, 2015
with Report of Independent Auditors*

Michigan Education Savings Program

Audited Financial Statements

Year Ended September 30, 2015

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Report of Independent Auditors

Mr. Nick Khouri, Trustee, Michigan Education Savings Program, Michigan Department of Treasury
Mr. Doug A. Ringler, CPA, CIA, Auditor General, State of Michigan
Lansing, Michigan

Report on the Financial Statements

We have audited the accompanying financial statements of the Michigan Education Savings Program, a fiduciary fund of the State of Michigan, as of and for the year ended September 30, 2015, and the related notes to the financial statements, which collectively comprise the Michigan Education Savings Program's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express opinions 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net position of the Michigan Education Savings Program, a fiduciary fund of the State of Michigan, as of September 30, 2015, and the change in fiduciary net position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Michigan Education Savings Program, a fiduciary fund of the State of Michigan, and do not purport to, and do not present fairly the financial position of the State of Michigan in its entirety as of September 30, 2015, and the changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 5 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 4, 2015, on our consideration of the Michigan Education Savings Program'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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Michigan Education Savings Program's internal control over financial reporting and compliance.

Andrews Hooper Pavlik PLC

Okemos, Michigan
December 4, 2015

Michigan Education Savings Program

Management's Discussion and Analysis

September 30, 2015

This section of the Michigan Education Savings Program's (MESP or Program) financial statements presents a discussion and analysis of the Program's financial performance during the year ended September 30, 2015. MESP consists of two components, a Direct-Sold Plan managed by TIAA-CREF Tuition Financing, Inc. (TFI) and the MI 529 Advisor Plan managed by TFI for which Allianz Global Investors Distributors, LLC is the plan administrator and distributor. MESP is a fiduciary fund of the State of Michigan. Readers should consider the information presented in this section in conjunction with the Program's financial statements and notes to financial statements.

Financial Highlights

The Program received approximately \$184.4 million in net contributions from account owners for the year ended September 30, 2015.

The Program earned approximately \$93.4 million from investment operations and paid out approximately \$7.4 million for operating expenses during the year ended September 30, 2015.

Overview of the Financial Statements

The Program's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

This report consists of two parts, management's discussion and analysis (this section) and the basic financial statements. The basic financial statements are composed of a statement of fiduciary net position, a statement of changes in fiduciary net position, and notes to financial statements that explain some of the information in the financial statements and provide more detailed information.

The statement of fiduciary net position presents information on the Program's assets and liabilities, with the difference between the two reported as net position as of September 30, 2015. This statement, along with all of the Program's financial statements, is prepared using the accrual basis of accounting. Contributions are recognized when enrollment in the Program is finalized; subsequent contributions and redemptions are recognized on the trade date; expenses and liabilities are recognized when services are provided, regardless of when cash is disbursed.

The statement of changes in fiduciary net position presents information showing how the Program's assets changed during the most recent fiscal period. Changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenue and expenses are reported in this statement for some items that will result in cash flows in future fiscal years.

The notes to financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

Michigan Education Savings Program

Management's Discussion and Analysis

September 30, 2015

This report presents the operating results and financial status of the Program, which the State of Michigan reports as a fiduciary fund. Fiduciary fund reporting is used to account for resources held for the benefit of parties outside the governmental entity.

Financial Analysis

Net Position

The following is a condensed statement of fiduciary net position as of September 30, 2015 and 2014:

	<u>2015</u>	<u>2014</u>
Assets		
Investments	\$ 4,379,524,362	\$ 4,234,190,281
Cash	105,657	509,037
Receivables	4,814,875	4,951,596
Total assets	4,384,444,894	4,239,650,914
Liabilities – payables	5,484,772	5,958,136
Net position	<u>\$ 4,378,960,122</u>	<u>\$ 4,233,692,778</u>

Net position represents total contributions from account owners, plus the net increase from operations, less withdrawals and expenses.

Net position increased by 3.4 percent and 13.7 percent or \$145,267,344 and \$510,322,083 for the years ended September 30, 2015 and 2014, respectively. This increase is primarily due to participant contributions to the Direct-Sold Plan and the MI 529 Advisor Plan, as well as positive economic conditions in the marketplace during the year ended September 30, 2014.

Investments in MESP are approximately 100 percent of total net position, and consist of investments in the Direct-Sold Plan and investments in the MI 529 Advisor Plan. Investments in the Direct-Sold Plan include 33 investment portfolios, including 27 age-based portfolios (9 age-based portfolios for each of 3 risk strategies – conservative, moderate, and aggressive) and 6 other investment portfolios. Each portfolio invests in varying percentages in multiple TIAA-CREF funds, or the funding agreements issued by TIAA-CREF Life Insurance Company to the Program. Investments in the MI 529 Advisor Plan include 18 portfolios, including 6 age-based portfolios and 12 other portfolios. Each portfolio invests in various mutual funds.

Other assets consist of cash and receivables for securities sold, contributions, and accrued income. Liabilities consist mainly of payables for securities purchased, withdrawals, and accrued expenses.

Michigan Education Savings Program

Management's Discussion and Analysis

September 30, 2015

Changes in Net Position

The following is a condensed statement of changes in fiduciary net position for the years ended September 30, 2015 and 2014:

	<u>2015</u>	<u>2014</u>
Additions		
Subscriptions	\$ 502,805,405	\$ 475,134,926
Interest and dividends	93,443,757	78,593,159
Net increase (decrease) in fair value of investments	(125,109,990)	245,059,188
Total additions – net	<u>471,139,172</u>	<u>798,787,273</u>
Deductions		
Redemptions	318,444,856	281,700,930
Operating expenses	7,426,972	6,764,260
Total deductions	<u>325,871,828</u>	<u>288,465,190</u>
Change in net position	145,267,344	510,322,083
Net position – beginning of year	<u>4,233,692,778</u>	<u>3,723,370,695</u>
Net position – end of year	<u>\$ 4,378,960,122</u>	<u>\$ 4,233,692,778</u>

Total additions decreased by \$327.7 million, from \$798.8 million to \$471.1 million. This decrease is due to market depreciation, offset by an increase in subscriptions as a result of an increase in the number of account holders and an increase in income and gains from the underlying investments.

Total deductions increased \$37.4 million, from \$288.5 million to \$325.9 million due to an increase in redemptions, which can be attributed to an increase in the number of account holders. Total deductions also increased due to an increase in operating expenses. Nearly all of the operating expenses increased because they are based on percentages of net position and net position increased from the prior year.

Michigan Education Savings Program

Statement of Fiduciary Net Position

September 30, 2015

	The Direct-Sold Plan	MI 529 Advisor Plan	Total
Assets			
Cash	\$ 18,253	\$ 87,404	\$ 105,657
Investments – at fair market value (Note 4)	4,012,334,502	367,189,860	4,379,524,362
Dividends and interest receivable	2,820,583	105,560	2,926,143
Receivable for securities transactions	238,508	47,730	286,238
Receivable for Program units sold	1,225,940	376,417	1,602,357
Receivable from Program Administrator	-	137	137
Total assets	4,016,637,786	367,807,108	4,384,444,894
 Liabilities			
Accrued Program management fee	319,306	151,261	470,567
Payable for securities transactions	3,537,470	216,538	3,754,008
Payable for Program units redeemed	753,837	120,921	874,758
Other liabilities	232,193	153,246	385,439
Total liabilities	4,842,806	641,966	5,484,772
Net Position – Held in trust for participant education savings program	\$ 4,011,794,980	\$ 367,165,142	\$ 4,378,960,122

The notes to the financial statements are an integral part of this statement.

Michigan Education Savings Program

Statement of Changes in Fiduciary Net Position

Year Ended September 30, 2015

	The Direct-Sold Plan	MI 529 Advisor Plan	Total
Additions			
Subscriptions	\$ 419,488,803	\$ 83,316,602	\$ 502,805,405
Investment Income:			
Interest and dividends	81,610,497	11,833,260	93,443,757
Net decrease in fair value of investments	(97,967,023)	(27,142,967)	(125,109,990)
Total investment loss	(16,356,526)	(15,309,707)	(31,666,233)
 Total additions	 403,132,277	 68,006,895	 471,139,172
Deductions			
Redemptions	295,642,642	22,802,214	318,444,856
Operating expenses	3,796,143	3,630,829	7,426,972
Total deductions	299,438,785	26,433,043	325,871,828
 Change in net position	 103,693,492	 41,573,852	 145,267,344
Net position – beginning of year	3,908,101,488	325,591,290	4,233,692,778
Net position – end of year	\$ 4,011,794,980	\$ 367,165,142	\$ 4,378,960,122

The notes to the financial statements are an integral part of this statement.

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

1. Organization

The Michigan Education Savings Program (Program), a fiduciary fund of the State of Michigan, is designed to help people save for the costs of higher education. The Program was established by the Michigan Department of Treasury and is administered by the State Treasurer of Michigan (Treasurer), who acts as trustee of the Program. The Program constitutes a qualified tuition program under Section 529 of the Internal Revenue Code and was established pursuant to Section 529 and the Michigan Compiled Laws 390.1471 et seq. The Program consists of two components, the Direct-Sold Plan and the MI 529 Advisor Plan. Investment portfolios and allocations, as approved by the Treasurer, are described in the current disclosure booklet for each respective component. The Treasurer has the authority to enter into contracts for program management services, appoint a program manager, adopt policies and operating procedures to implement and administer the Program, and establish investment policies for the Program.

TIAA-CREF Tuition Financing, Inc. (TFI), a wholly-owned, indirect subsidiary of Teachers Insurance and Annuity Association of America (TIAA), manages the Direct-Sold Plan under the direction of the Treasurer pursuant to a contract that it has entered into with the State of Michigan. The assets in the Principal Plus Interest Option and certain other investment portfolios are allocated to funding agreements issued by TIAA-CREF Life Insurance Company (TIAA-CREF Life), an affiliate of TFI. The funding agreements guarantee to the Michigan Department of Treasury a minimum rate of interest and provide the opportunity for additional interest as declared periodically by TIAA-CREF Life. Teachers Advisors, Inc. (Advisors), an affiliate of TFI, is registered with the Securities and Exchange Commission as an investment advisor and provides investment advisory services to the TIAA-CREF funds.

The MI 529 Advisor Plan component of the Michigan Education Savings Program was established under Public Act (PA) No. 161 of 2000 of the State of Michigan, which was amended by PA No. 153 of 2007. TFI acts as the program manager for the MI 529 Advisor Plan. TFI, per the State's approval, has delegated the responsibilities of being the administrator and distributor to Allianz Global Investors Distributors, LLC (AGID). AGID provides services to the MI 529 Advisor Plan including administration, distribution, and investment management services. AGID has delegated the investment-related functions for the MI 529 Advisor Plan to Allianz Global Investors U.S. LLC (AGI U.S.), an affiliate of AGID, including making recommendations to the Treasurer as to the formulation of the investment portfolios and the selection of the underlying funds and asset allocations among such funds.

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

2. Significant Accounting Policies

The accompanying financial statements were prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB), which may require the use of estimates made by management. Actual results may differ from those estimates. The following is a summary of the significant accounting policies consistently followed by the Program.

Valuation of Investments

The market value of the investments in the underlying mutual funds is based on the net asset values of the respective classes of the mutual funds on the close of business on the valuation date. The value of the TIAA-CREF Life funding agreements (within the Direct-Sold Plan), to which the Principal Plus Interest Option and certain other investment portfolios allocate assets, is stated at cost, which approximates fair value. The TIAA-CREF Life funding agreements have a floating rate of interest that resets annually based on a projected rate of return.

Units

The beneficial interest for each account owner in the investment portfolios is represented by Program units. Subscriptions and redemptions are recorded upon receipt of the account owner's instructions in good order, based on the next determined daily net asset value per unit (Unit Value). Unit Values for each investment portfolio are determined at the close of business of the New York Stock Exchange.

Investment Transactions

Portfolio transactions, normally in shares of the underlying funds, are accounted for as of the trade date. Realized gains and losses are determined on the identified cost basis.

Withdrawals

The earnings portions of nonqualified and penalty-free withdrawals are taxable to the account owner or the beneficiary. Earnings portions of nonqualified withdrawals also may be subject to a federal penalty tax.

Distributions

All net investment income and net realized gains of the portfolios will be reinvested in the portfolios; distributions will not be declared.

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

2. Significant Accounting Policies (continued)

Investment Income

Dividend income and capital gain distributions from the underlying funds, if any, are recorded on the ex-dividend date. Capital gain distributions, if any, from underlying funds are a component of net increase (decrease) in fair value investments. Interest income is recorded as earned.

Income Taxes

The Program is exempt from federal income tax under Section 529 of the Internal Revenue Code of 1986 and does not expect to have any unrelated business income subject to tax. Accordingly, no provision for federal income taxes has been made.

3. Management Agreements

A separate management agreement exists for the Direct-Sold Plan and the MI 529 Advisor Plan.

Direct-Sold Plan

During the fiscal year, for its services as program manager of the Direct-Sold Plan, with respect to all investment portfolios (other than the Principal Plus Interest Option), TFI is paid an annual program management fee of 0.05% of the average daily net position of the Direct-Sold Plan invested in such portfolios (0.06% through November 18, 2014, when total assets in the Direct-Sold Plan were less than \$4.0 billion). In addition, Advisors is paid investment management fees on the underlying investments in the TIAA-CREF funds.

For its services related to administering the Direct-Sold Plan, each investment portfolio (with the exception of the Principal Plus Interest Option) pays to the Michigan Department of Treasury an administrative fee at an annual rate of 0.02% of the average daily net position held by that portfolio. Prior to September 1, 2015, this fee was at an annual rate of 0.05% of the average daily net position held by the portfolio.

The Principal Plus Interest Option does not pay a fee to the program manager or to the Michigan Department of Treasury. TIAA-CREF Life, the issuer of the funding agreements in which this portfolio invests and an affiliate of TFI, makes payments to TFI. TIAA-CREF Life also pays the Michigan Department of Treasury a fee equal to 0.02% of the average daily net position held by the Principal Plus Interest Option. Prior to September 1, 2015, this fee was at an annual rate of 0.05% of the average daily net position held by the Principal Plus Interest Option.

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

3. Management Agreements (continued)

MI 529 Advisor Plan

The State of Michigan has entered into a program management agreement with TFI, which has subcontracted with AGID to provide administrative, recordkeeping, marketing, and investment management services to the MI 529 Advisor Plan. Account owners bear expenses at the investment portfolio level and also indirectly bear the expenses in the underlying funds.

The MI 529 Advisor Plan compensates AGID for services provided and expenses incurred in connection with sales of units and services rendered to unit-holders and for maintenance of unit-holder accounts of A and C units. The Program paid AGID distribution and servicing and administration fees at an effective annual rate as set forth below (calculated as a percentage of each portfolio's average daily net position attributable to each class):

	<u>Class A Units</u>	<u>Class C Units</u>
Program management fee ¹	0.50%	0.50%
Servicing and administrative fee:		
PIMCO Short Asset Investment Portfolio	0.10%	0.10%
Other portfolios	0.25%	0.08%, 0.15% ³
Distribution fee:		
PIMCO Short Asset Investment Portfolio	None	None
Other portfolios	None	0.25%, 0.50% ²
State administration fee ⁴	0.10%	0.10%

¹ A portion of the program management fee is paid by AGID to the program manager monthly.

² The Age-Based and Static Investment Portfolios are assessed a distribution fee of 0.50 percent. The individual Investment Portfolios are assessed a distribution fee of 0.25 percent.

³ The Age-Based and Static Investment Portfolios are assessed a servicing and administrative fee of 0.15 percent. The individual Investment Portfolios are assessed a servicing and administrative fee of 0.08 percent.

⁴ Paid directly to the State of Michigan to administer and maintain the State of Michigan's qualified tuition programs.

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

3. Management Agreements (continued)

MI 529 Advisor Plan (continued)

AGID also receives the proceeds of the initial sales charge paid by the unit-holders upon the purchase of A units and the contingent deferred sales charges (CDSC) paid by unit-holders upon certain redemptions of C units as described in detail in the prevailing plan disclosure statement. Units of PIMCO Short Asset Investment Portfolio are not subject to initial sales charges or CDSC.

For the year ended September 30, 2015, AGID received approximately \$242,000 in initial sales charges and \$11,000 in CDSC. All or a substantial portion of the sales charges paid by the investor may be paid to the selling financial intermediary through which the account owners make their investments.

4. Investments

Investments in the Direct-Sold Plan include 33 investment portfolios, including 27 age-based portfolios (9 age-based portfolios for each of 3 risk strategies – conservative, moderate, and aggressive) and 6 other investment portfolios. Each portfolio invests in varying percentages in multiple TIAA-CREF funds, or the funding agreements issued by TIAA-CREF Life Insurance Company to the Program. Investments in the MI 529 Advisor Plan include 18 portfolios, including 6 age-based portfolios and 12 other portfolios. Each portfolio invests in various mutual funds.

Cash Deposits

Cash deposits were reflected in the accounts of the bank (without recognition of checks written, but not yet cleared, or of deposits in transit). As of September 30, 2015, the Program's bank balance was \$105,657 with an insured amount of \$105,657.

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

4. Investments (continued)

As of September 30, 2015 the Program's investments consisted of the following:

	<u>Cost</u>	<u>Market Value</u>
The Direct-Sold Plan:		
TIAA-CREF Funds (Institutional Class):		
Bond Index Fund	\$ 993,876,913	\$ 993,649,625
Emerging Markets Equity Index Fund	89,556,629	74,651,627
Equity Index Fund	986,627,714	1,338,626,713
Inflation-Linked Bond Fund	295,326,757	280,786,646
International Equity Index Fund	446,815,321	477,080,984
High-Yield Fund	137,002,569	128,232,209
TIAA-CREF Life Insurance Company:		
Funding agreements	579,548,246	579,548,246
Vanguard REIT Index Fund	140,243,386	139,758,452
Subtotal	3,668,997,535	4,012,334,502
MI 529 Advisor Plan:		
AllianzGI Best Styles Global Equity Fund	88,382,439	87,670,103
AllianzGI Best Styles International Equity Fund	8,061,437	8,015,149
AllianzGI Best Styles U.S. Equity Fund	6,923,743	6,875,504
AllianzGI Income & Growth Fund	10,110,818	9,146,124
AllianzGI Global Allocation Fund	92,284,496	91,881,380
AllianzGI Global Small-Cap Fund	6,385,043	6,218,077
AllianzGI Short Duration High Income Fund	8,950,667	8,659,365
PIMCO CommodityRealReturn Strategy Fund	10,630,042	10,674,423
PIMCO Income Fund	14,867,213	14,605,916
PIMCO RealEstateRealReturn Strategy Fund	9,690,328	8,199,001
PIMCO Real Return Fund	27,649,748	26,867,944
PIMCO Short Asset Investment Fund	33,837,398	33,803,634
PIMCO Total Return Fund	10,420,501	9,848,750
TIAA-CREF Bond Index Fund	16,895,588	16,942,347
TIAA-CREF Small-Cap Blend Index Fund	6,881,381	6,901,130
TIAA-CREF S&P 500 Index Fund	20,002,020	20,881,013
Subtotal	371,972,862	367,189,860
Total	<u>\$ 4,040,970,397</u>	<u>\$ 4,379,524,362</u>

All of the investments above, except the Vanguard REIT Index Fund, are related party transactions.

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

4. Investments (continued)

An account owner has an investment in an investment portfolio and not a direct investment in any underlying mutual fund or other investment vehicle to which funds in that investment portfolio may be allocated.

Certain investments are subject to a variety of investment risks based on the amount of risk in the underlying funds. GASB requires that entities disclose certain essential risk information about deposits and investments. All of the Program's investment portfolios are uninsured and unregistered and are held by a custodian in the Program's name.

The mutual funds in which the portfolios invest are comprised of various investment securities, which include corporate debt and equity securities, obligations of the United States government and government agencies, and international equity securities. Certain underlying funds may invest in certain specified derivative securities, including interest rate and credit default swaps; caps and floors for hedging purposes; exchange-traded options; and over-the-counter options executed with primary dealers, including long calls and puts and covered calls and financial futures and options. Certain underlying funds may invest in restricted securities including: instruments issued by trusts, partnerships, or other issuers, including pass-through certificates representing participations in, or debt instruments backed by, the securities owned by such issuers. These underlying funds also may engage in securities lending, reverse repurchase agreements, and dollar roll transactions. In addition, certain underlying funds may invest in mortgage-backed securities, structured investment vehicles, below-investment grade debt, debt obligations of foreign issuers and stocks of foreign corporations, securities in foreign investment funds or trusts, foreign derivative securities including futures contracts, options, interest rate and currency swap transactions, and various other investment vehicles, each with inherent risks, including market, credit, interest rate, foreign currency leverage, and liquidity risks. Due to the level of risk associated with these investment securities, it is at least reasonably possible that changes in their fair values may occur in the near term and that such changes could materially affect account owner balances and the amounts reported in the Program's financial statements.

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a failure, the Program's deposits and investments may not be returned. The Program does not have formal custodial credit risk policies for investments. An account owner has an investment in an investment portfolio and not a direct investment in any underlying mutual fund or other investment vehicle to which funds in that investment portfolio may be allocated. Because of this ownership structure, the custodial credit risk is significantly mitigated.

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

4. Investments (continued)

Credit Risk

The underlying funds investing primarily in fixed-income securities are subject to credit risk. Credit risk is the potential of failure of the other party to pay interest and principal when due as a result of adverse market or economic conditions. The Program does not have formal investment policies for managing credit risk. The underlying mutual funds do not carry a formal credit quality rating. The underlying funding agreements, to which the Principal Plus Interest Option and certain other portfolios of the Direct-Sold Plan allocate assets, are guaranteed insurance products issued by TIAA-CREF Life. TIAA-CREF Life has a Standard & Poor's credit rating of AA+ as of September 30, 2015.

Interest Rate Risk

Interest rate risk is the risk that the value of investments will decrease as a result of a rise in interest rates. The Program does not have a formal investment policy that limits maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. As of September 30, 2015, the average maturities for the underlying fixed-income mutual funds are as follows:

	<u>Market Value</u>	<u>Average Maturity</u>
The Direct-Sold Plan:		
TIAA-CREF Funds (Institutional Class):		
Bond Index Fund	\$ 993,649,625	7.41 years
High-Yield Fund	128,232,209	6.63 years
Inflation-Linked Bond Fund	280,786,646	8.58 years
MI 529 Advisor Plan:		
AllianzGI Short Duration High Income Fund	8,659,365	3.55 years
PIMCO CommodityRealReturn Strategy Fund	10,674,423	3.47 years
PIMCO Income Fund	14,605,916	5.39 years
PIMCO Short Asset Investment Fund	33,803,634	0.09 years
PIMCO RealEstateRealReturn Strategy Fund	8,199,001	4.01 years
PIMCO Real Return Fund	26,867,944	8.42 years
PIMCO Total Return Fund	9,848,750	7.80 years
TIAA-CREF Bond Index Fund	16,942,347	7.41 years

Michigan Education Savings Program

Notes to Financial Statements

September 30, 2015

4. Investments (continued)

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of investments in foreign securities. The Program does not have formal foreign currency risk policies for investments. Certain investment portfolios allocate assets to underlying mutual funds that are exposed to foreign currency risk. The Program does not have any direct investment in foreign fixed-income securities. As of September 30, 2015, the values of investments in underlying mutual funds that primarily invest in foreign securities are as follows:

Investment	Market Value
The Direct-Sold Plan:	
TIAA-CREF Funds (Institutional Class):	
Emerging Markets Equity Index Fund	\$ 74,651,627
International Equity Index Fund	477,080,984
MI 529 Advisor Plan:	
AllianzGI Best Styles International Equity Fund	8,015,149
AllianzGI Best Styles Global Equity Fund	87,670,103
AllianzGI Global Small-Cap Fund	6,218,077
AllianzGI Global Allocation Fund	91,881,380

5. Subsequent Event

On October 1, 2015, the State administration fee for the MI 529 Advisor Plan was reduced by 0.05%, from 0.10% to 0.05%.

Independent Auditors' Report on Internal Control Over Financial Reporting and on
Compliance and Other Matters Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards*

Independent Auditors' Report on Internal Control Over Financial Reporting and on
Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance with *Government Auditing Standards*

Mr. Nick Khouri, Trustee, Michigan Education Savings Program, Michigan Department of Treasury
Mr. Doug A. Ringler, CPA, CIA, Auditor General, State of Michigan
Lansing, Michigan

We have audited, 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, the financial statements of the Michigan Education Savings Program (Program), a fiduciary fund of the State of Michigan, as of and for the year ended September 30, 2015, and the related notes to the financial statements, which collectively comprise the Program's basic financial statements, and have issued our report thereon dated December 4, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Program's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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 Program's internal control. Accordingly, we do not express an opinion on the effectiveness of the Program's internal control.

A deficiency in internal control 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 and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit, we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Michigan Education Savings Program'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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of our testing, and not to provide an opinion on the effectiveness of the Program's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Program's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Andrews Hooper Pavlik PLC

Okemos, Michigan
December 4, 2015