

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

DEPARTMENT OF STATE

October 1, 2000 through September 30, 2002



Michigan
Office of the Auditor General
REPORT SUMMARY

Financial Audit

Report Number:
 23-100-03

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

Department of State

Released:
 June 2003

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

Financial Schedules:

Auditor's Report Issued

We issued an unqualified opinion on the Department's financial schedules.

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Internal Control Over Financial Reporting

We did not identify any material weaknesses in internal control over financial reporting. However, we did identify a reportable condition (Finding 1).

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**Noncompliance Material to
 the Financial Schedules**

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

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Federal Awards:

Auditor's Reports Issued on Compliance

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

~ ~ ~ ~ ~

Internal Control Over Major Programs

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

~ ~ ~ ~ ~

Required Reporting of Noncompliance

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

~ ~ ~ ~ ~

Systems of Accounting and Internal Control:

We determined that the Department was in substantial compliance with Sections 18.1483 - 18.1487 of the *Michigan Compiled Laws*. However, we did identify a reportable condition (Finding 1).

~ ~ ~ ~ ~

We audited the following program as a major program:

<u><i>CFDA Number</i></u>	<u><i>Program Title</i></u>	<u><i>Compliance Opinion</i></u>
15.904	Historic Preservation Fund Grants-In-Aid	Unqualified

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



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

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

James S. Neubecker, C.P.A., C.I.A., D.P.A.
Executive Deputy Auditor General

Scott M. Strong, C.P.A., C.I.A.
Director of Audit Operations



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

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

June 18, 2003

The Honorable Terri Lynn Land
Secretary of State
Treasury Building
Lansing, Michigan

Dear Secretary Land:

This is our report on the financial audit, including the provisions of the Single Audit Act, of the Department of State for the period October 1, 2000 through September 30, 2002.

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

Our finding and recommendation are contained in Section II of the schedule of findings and questioned costs. The agency preliminary response is 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

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TABLE OF CONTENTS

DEPARTMENT OF STATE

	<u>Page</u>
INTRODUCTION	
Report Summary	1
Report Letter	3
INDEPENDENT AUDITOR'S REPORT AND FINANCIAL SCHEDULES	
Independent Auditor's Report on the Financial Schedules	7
Department of State Financial Schedules	
Schedule of Revenues and Transfers - General Fund, School Aid Fund, Other Special Revenue Funds, Private Purpose Trust Fund, and Permanent Fund	10
Schedule of Sources and Disposition of General Fund Authorizations	12
Notes to the Financial Schedules	13
SUPPLEMENTAL FINANCIAL SCHEDULES	
Schedule of Revenues - Other Special Revenue Funds	20
Schedule of Revenues - Private Purpose Trust Fund	22
Schedule of Revenues - Permanent Fund	23
Schedule of Certain General Fund Assets and Liabilities	24
Schedule of Expenditures of Federal Awards	26

INDEPENDENT AUDITOR'S REPORTS ON
COMPLIANCE AND INTERNAL CONTROL

Independent Auditor's Report on Compliance and on Internal Control Over Financial Reporting	28
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	30

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section I: Summary of Auditor's Results	32
Section II: Findings Related to the Financial Schedules	33
1. Internal Auditor Independence	33
Section III: Findings and Questioned Costs Related to Federal Awards	34

OTHER SCHEDULES

Summary Schedule of Prior Audit Findings	36
Corrective Action Plan	37

GLOSSARY

Glossary of Acronyms and Terms	38
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OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
(517) 334-8050
FAX (517) 334-8079

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

Independent Auditor's Report on the Financial Schedules

April 4, 2003

The Honorable Terri Lynn Land
Secretary of State
Treasury Building
Lansing, Michigan

Dear Secretary Land:

We have audited the financial schedules of the Department of State for the fiscal years ended September 30, 2002 and September 30, 2001, as identified in the table of contents. These financial schedules are the responsibility of the Department's management. Our responsibility is to express an opinion on these financial schedules 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 schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1b, the financial schedules include only the revenues and transfers for the Department's General Fund, the School Aid Fund, other special revenue fund, private purpose trust fund, and permanent fund accounts and the sources and disposition of authorizations for the Department's General Fund accounts, presented using the current financial resources measurement focus and the modified accrual basis of accounting. Accordingly, these financial schedules do not purport to, and do not, constitute a complete financial presentation of the Department or the State's General Fund, School Aid Fund, other special revenue funds, private purpose trust funds, or permanent funds in accordance with accounting principles generally accepted in the United States of America.

In our opinion, the financial schedules referred to in the first paragraph present fairly, in all material respects, the revenues and transfers and the sources and disposition of authorizations of the Department of State for the fiscal years ended September 30, 2002 and September 30, 2001, on the basis of accounting described in Note 1b.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 4, 2003 on our tests of the Department's compliance with certain provisions of laws, regulations, contracts, and grants and on our consideration of its internal control over financial reporting. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

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

AUDITOR GENERAL

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DEPARTMENT OF STATE
Schedule of Revenues and Transfers
General Fund, School Aid Fund, Other Special Revenue Funds, Private Purpose Trust Fund, and Permanent Fund
For the Fiscal Years Ended September 30
(In Thousands)

	General Fund		School Aid Fund		Other Special Revenue Funds	
	2002	2001	2002	2001	2002	2001
REVENUES (Note 2)						
Taxes:						
Sales taxes	\$ 293,511	\$ 250,127	\$ 807,018	\$ 687,731	\$	\$
Use taxes	101,881	98,309	50,933	49,147		
Resident motor vehicle taxes					766,999	734,084
Nonresident motor vehicle taxes					60,348	42,920
Total Taxes	<u>\$ 395,393</u>	<u>\$ 348,436</u>	<u>\$ 857,952</u>	<u>\$ 736,879</u>	<u>\$ 827,347</u>	<u>\$ 777,004</u>
From Federal Agencies	\$ 0	\$ 855	\$ 0	\$ 0	\$ 0	\$ 0
From Services:						
Commercial lookup fees	\$ 30,695	\$ 29,435	\$	\$	\$	\$
Other	48	12				
Total From Services	<u>\$ 30,742</u>	<u>\$ 29,447</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
From Licenses and Permits:						
Motor vehicle operator and chauffeur licenses	\$ 33,673	\$ 34,738	\$	\$	\$ 12,491	\$ 13,486
Automobile repair facility and mechanic licenses	4,253	4,310				
Motor vehicle annual license transfer fee					10,260	9,577
Motor vehicle title fees	2,943	3,686			36,445	34,648
Watercraft registrations					10,497	9,658
Fundraising plate donations					223	125
Fundraising plate service fees					794	641
Other	13,704	11,925			10,514	9,756
Total From Licenses and Permits	<u>\$ 54,573</u>	<u>\$ 54,658</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 81,223</u>	<u>\$ 77,891</u>
Miscellaneous	\$ 1,786	\$ 2,298	\$ 0	\$ 0	\$ 68,327	\$ 60,790
Total Revenues	<u>\$ 482,494</u>	<u>\$ 435,694</u>	<u>\$ 857,952</u>	<u>\$ 736,879</u>	<u>\$ 976,898</u>	<u>\$ 915,685</u>
TRANSFERS (Note 2)						
From Special Revenue Funds:						
Michigan Transportation Fund	\$ 87,860	\$ 49,196	\$	\$	\$	\$
Marine Safety Fund	1,036	1,012				
Assigned Claims Facility and Plan Fund	687	743				
Total From Special Revenue Funds	<u>\$ 89,583</u>	<u>\$ 50,951</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
From Private Purpose Trust Funds:						
Gifts, Bequests, and Deposits Investment Fund	\$	\$ 70	\$	\$	\$	\$
Total From Private Purpose Trust Funds	<u>\$ 0</u>	<u>\$ 70</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
Total Transfers	<u>\$ 89,583</u>	<u>\$ 51,020</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
Total Revenues and Transfers	<u>\$ 572,077</u>	<u>\$ 486,714</u>	<u>\$ 857,952</u>	<u>\$ 736,879</u>	<u>\$ 976,898</u>	<u>\$ 915,685</u>

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

Private Purpose Trust Fund		Permanent Fund		Totals (Memorandum Only)	
2002	2001	2002	2001	2002	2001
\$	\$	\$	\$	\$ 1,100,530	\$ 937,858
				152,815	147,457
				766,999	734,084
				60,348	42,920
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 2,080,692</u>	<u>\$ 1,862,319</u>
\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 855
\$	\$	\$	\$	\$ 30,695	\$ 29,435
				48	12
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 30,742</u>	<u>\$ 29,447</u>
\$	\$	\$	\$	\$ 46,164	\$ 48,224
				4,253	4,310
				10,260	9,577
				39,388	38,333
				10,497	9,658
				223	125
				794	641
				24,218	21,681
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 135,796</u>	<u>\$ 132,549</u>
\$ 162	\$ 72	\$ 197	\$ 113	\$ 70,472	\$ 63,273
<u>\$ 162</u>	<u>\$ 72</u>	<u>\$ 197</u>	<u>\$ 113</u>	<u>\$ 2,317,702</u>	<u>\$ 2,088,443</u>
\$	\$	\$	\$	\$ 87,860	\$ 49,196
				1,036	1,012
				687	743
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 89,583</u>	<u>\$ 50,951</u>
\$	\$	\$	\$	\$ 0	\$ 70
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 70</u>
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 89,583</u>	<u>\$ 51,020</u>
<u>\$ 162</u>	<u>\$ 72</u>	<u>\$ 197</u>	<u>\$ 113</u>	<u>\$ 2,407,285</u>	<u>\$ 2,139,463</u>

DEPARTMENT OF STATE
Schedule of Sources and Disposition of General Fund Authorizations
Fiscal Years Ended September 30
(In Thousands)

	<u>2002</u>	<u>2001</u>
SOURCES OF AUTHORIZATIONS (Note 3)		
General purpose appropriations	\$ 16,913	\$ 66,805
Balances carried forward	17,213	22,937
Restricted financing sources	148,070	110,731
Total	<u>\$ 182,196</u>	<u>\$ 200,472</u>
 DISPOSITION OF AUTHORIZATIONS (Note 3)		
Expenditures and transfers out	<u>\$ 169,022</u>	<u>\$ 180,379</u>
Balances carried forward:		
Multi-year projects	\$ 2,620	\$ 5,383
Encumbrances	5,027	5,471
Restricted revenues - authorized	860	833
Restricted revenues - not authorized/used	2,976	6,094
Total balances carried forward (Note 3b.)	<u>\$ 11,483</u>	<u>\$ 17,782</u>
Balances lapsed	<u>\$ 1,691</u>	<u>\$ 2,312</u>
Total	<u>\$ 182,196</u>	<u>\$ 200,472</u>

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

Notes to the Financial Schedules

Note 1 Significant Accounting Policies

a. Reporting Entity

The accompanying financial schedules report the results of the governmental operations of the Department of State for the fiscal years ended September 30, 2002 and September 30, 2001. The governmental operations of the Department are accounted for principally in the State's General Fund and are reported on in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*. In addition, the Department is responsible for collecting fees for various funds, as discussed in Note 2.

The notes accompanying these financial schedules relate directly to the Department of State. The *SOMCAFR* provides more extensive general disclosures regarding the State's Summary of Significant Accounting Policies; Budgeting, Budgetary Control, and Legal Compliance; and Pension Benefits and Other Postemployment Benefits.

On May 29, 2001, the Governor issued Executive Order No. 2001-1, which resulted in the transfer, effective August 5, 2001, of the Department of State's responsibilities associated with the administration of State historical sites, State archives, and State cultural resources and treasures. The transfer moved approximately \$8.3 million of the Department's appropriations, including one major federal program (Historic Preservation Fund Grants-In-Aid, *CFDA* No. 15.904) to the newly created Department of History, Arts and Libraries. The transfer was accounted for as of October 1, 2001. As a result of this transfer, only the fiscal year 2000-01 financial schedules for the Department of State include the financial activity associated with the administration of the State historical sites, State archives, and State cultural resources and treasures. The fiscal year 2001-02 financial activity associated with the administration of the State historical sites, State archives, and State cultural resources and treasures is included in the Department of History, Arts and Libraries' fiscal year 2001-02 financial schedules.

b. Measurement Focus, Basis of Accounting, and Presentation

The financial schedules contained in this report are presented using the current financial resources measurement focus and the modified accrual basis of accounting, as provided by generally accepted accounting principles applicable to governments. 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 the liability is incurred; however, certain expenditures related to long-term obligations are recorded only when payment is due and payable.

The accompanying financial schedules include only the revenues and transfers for the Department of State's General Fund, the School Aid Fund, other special revenue fund, private purpose trust fund, and permanent fund accounts and the sources and disposition of authorizations for the Department's General Fund accounts. Accordingly, these financial schedules do not purport to, and do not, constitute a complete financial presentation of the Department or the State's General Fund, School Aid Fund, other special revenue funds, private purpose trust funds, or permanent funds in accordance with generally accepted accounting principles.

Note 2 Schedule of Revenues and Transfers

The Department of State is responsible for collecting taxes and other revenues related to its own operations and those of certain other State departments. These revenues are accounted for in the General Fund, the School Aid Fund, other special revenue funds, a private purpose trust fund, and a permanent fund. The other special revenue funds include the Michigan Transportation Fund, State Trunkline Fund, Michigan State Waterways Fund, Marine Safety Fund, Michigan Nongame Fish and Wildlife Fund, Vietnam Veterans' Memorial Monument Fund, and Assigned Claims Facility and Plan Fund. The private purpose trust fund is the Gifts, Bequests, and Deposits Investment Fund. The permanent fund is the Children's Trust Fund. The amounts shown in the schedule of revenues and transfers represent only the amounts collected by the Department of State and do not represent total revenues and transfers for the funds.

Note 3 Schedule of Sources and Disposition of General Fund Authorizations

The various elements of the schedule of sources and disposition of General Fund authorizations are defined as follows:

- a. General purpose appropriations: Original appropriations and any supplemental appropriations that are financed by General Fund/general purpose revenues.
- b. Balances carried forward: Authorizations for multi-year projects, encumbrances, restricted revenues - authorized, and restricted revenues - not authorized/used that were not spent as of the end of the prior fiscal year. These authorizations are available for expenditure in the current fiscal year for the purpose of the carry-forward without additional legislative authorization, except for the restricted revenues - not authorized/used. As discussed in Note 1a., \$569,000 of Department of State balances carried forward from fiscal year 2000-01 were moved to the Department of History, Arts and Libraries' financial schedules in fiscal year 2001-02.
- c. Restricted financing sources: Collections of restricted revenues, restricted transfers, and restricted intrafund expenditure reimbursements to finance programs as detailed in the appropriations act. These financing sources are authorized for expenditure up to the amount appropriated. Depending upon program statute, any amounts received in excess of the appropriation are, at year-end, either converted to general purpose financing sources and made available for general appropriation in the next fiscal year or carried forward to the next fiscal year as either restricted revenues - authorized or restricted revenues - not authorized/used.
- d. Multi-year projects: Unexpended authorizations financed by general purpose appropriations for work projects and capital outlay projects that are carried forward to subsequent fiscal years for the completion of the projects. Significant carry-forwards of this type for fiscal year 2001-02 were for the Qualified Voter File (\$1.4 million) and the Information Technology Rearchitecture (\$707,000). Significant carry-forwards of this type for fiscal year 2000-01 were for the Uniform Commercial Code (UCC) Standards (\$2.0 million), the Qualified Voter File (\$1.5 million), and the Information Technology Rearchitecture (\$783,000).

- e. Encumbrances: General purpose appropriations and transfers from other funds carried forward to finance payments for goods or services ordered in the old fiscal year but not received by fiscal year-end.
- f. Restricted revenues - authorized: Revenues that, by statute or the State Constitution, are restricted and authorized for use to a particular program or activity. Generally, these revenues may be expended upon receipt without additional legislative authorization. This line also includes encumbrances that are financed with these restricted revenues. Significant carry-forwards of this type for fiscal year 2001-02 were encumbrances funded by fees for looking up driver and vehicle records (\$550,000) and the sale of Vehicle Code books (\$186,000). Significant carry-forwards of this type for fiscal year 2000-01 were for the Heritage Publications Fund (\$396,000), the sale of Vehicle Code books (\$166,000), and the museum store (\$160,000).
- g. Restricted revenues - not authorized/used: Revenues that, by statute, are restricted for use to a particular program or activity. The Department may not expend the revenues without additional legislative authorization. However, the Department had no restricted revenues subject to additional legislative authorization.

This line also includes the carry-forward of restricted revenues to finance encumbrances and work projects for the program that collects the revenues. Significant carry-forwards of this type for fiscal year 2001-02 were the interdepartmental grant from the Michigan Transportation Fund (\$863,000), fees for looking up driver and vehicle records (\$757,000), fees for automobile repair facilities (\$577,000), and fees for filing UCC liens on personal property (\$400,000). Significant carry-forwards of this type for fiscal year 2000-01 were fees for looking up driver and vehicle records (\$2.2 million), the interdepartmental grant from the Michigan Transportation Fund (\$1.4 million), fees for automobile repair facilities (\$703,000), fees for filing UCC liens on personal property (\$631,000), and driver fees (\$611,000).

- h. Balances lapsed: Authorizations that were unexpended and unobligated at the end of the fiscal year. These amounts are available for legislative appropriation in the subsequent fiscal year.

Note 4 Contingencies - Litigation

County Road Association of Michigan et al. v John M. Engler et al.: On March 6, 2002, the County Road Association of Michigan and the Chippewa County Road Commission filed a complaint in Ingham County Circuit Court challenging various provisions of Executive Order No. 2001-9. The Executive Order was proposed by the Governor and approved by the appropriations committees of both houses of the Legislature on November 6, 2001 for the purpose of reducing appropriated expenditures to balance the State budget. The complaint consists of five counts, one of which relates specifically to the Department of State. This complaint alleges that Executive Order No. 2001-9 violated Article IX, Section 9 of the State Constitution, by unlawfully allowing the Department of State to bill the Michigan Department of Transportation for expenses in excess of those necessary to collect motor vehicle taxes and fees. The plaintiffs seek preliminary and permanent injunctive relief to nullify particular provisions of Executive Order No. 2001-9 and to restore funding to the Michigan Transportation Fund. The aggregate amount at stake is \$20 million. If the Circuit Court awards the relief sought, the State will have to provide an alternate source of funding to balance the budget and make up revenue shortfalls of \$20 million. At the end of 2002, a supplemental appropriation (Act 746, P.A. 2002) was processed, which included boilerplate language to allow the Department of State to bill the Michigan Department of Transportation for collection costs.

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SUPPLEMENTAL
FINANCIAL SCHEDULES

DEPARTMENT OF STATE
Schedule of Revenues - Other Special Revenue Funds
Fiscal Years Ended September 30
(In Thousands)

	Michigan		State Trunkline Fund		Michigan State		Marine Sa
	Transportation Fund				Waterways Fund		
	2002	2001	2002	2001	2002	2001	2002
REVENUES							
Taxes:							
Resident motor vehicle taxes	\$ 766,999	\$ 734,084	\$	\$	\$	\$	\$
Nonresident motor vehicle taxes	60,348	42,920					
Total Taxes	<u>\$ 827,347</u>	<u>\$ 777,004</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
From Licenses and Permits:							
Motor vehicle operator and chauffeur licenses	\$	\$	\$ 12,491	\$ 13,486	\$	\$	\$
Motor vehicle annual license transfer fee	10,260	9,577					
Motor vehicle title fees	36,445	34,648					
Watercraft registrations					5,354	4,926	5,144
Fundraising plate donations							
Fundraising plate service fees	794	641					
Other	10,514	9,756					
Total From Licenses and Permits	<u>\$ 58,013</u>	<u>\$ 54,622</u>	<u>\$ 12,491</u>	<u>\$ 13,486</u>	<u>\$ 5,354</u>	<u>\$ 4,926</u>	<u>\$ 5,144</u>
Miscellaneous	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Total Revenues	<u><u>\$ 885,360</u></u>	<u><u>\$ 831,626</u></u>	<u><u>\$ 12,491</u></u>	<u><u>\$ 13,486</u></u>	<u><u>\$ 5,354</u></u>	<u><u>\$ 4,926</u></u>	<u><u>\$ 5,144</u></u>

The amounts shown represent only the amounts collected by the Department of State and do not represent total revenues for the funds.

fety Fund	Michigan Nongame Fish and Wildlife Fund		Vietnam Veterans' Memorial Monument Fund		Assigned Claims Facility and Plan Fund		Total	
	2002	2001	2002	2001	2002	2001	2002	2001
\$	\$	\$	\$	\$	\$	\$	\$ 766,999	\$ 734,084
							60,348	42,920
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 827,347</u>	<u>\$ 777,004</u>
\$	\$	\$	\$	\$	\$	\$	\$ 12,491	\$ 13,486
							10,260	9,577
							36,445	34,648
4,733							10,497	9,658
	223	125					223	125
							794	641
							10,514	9,756
<u>\$ 4,733</u>	<u>\$ 223</u>	<u>\$ 125</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 81,223</u>	<u>\$ 77,891</u>
\$ 0	\$ 0	\$ 0	\$ 54	\$ 36	\$ 68,273	\$ 60,755	\$ 68,327	\$ 60,790
<u>\$ 4,733</u>	<u>\$ 223</u>	<u>\$ 125</u>	<u>\$ 54</u>	<u>\$ 36</u>	<u>\$ 68,273</u>	<u>\$ 60,755</u>	<u>\$ 976,898</u>	<u>\$ 915,685</u>

DEPARTMENT OF STATE
 Schedule of Revenues - Private Purpose Trust Fund
Fiscal Years Ended September 30
 (In Thousands)

REVENUES	Gifts, Bequests, and Deposits Investment Fund	
	2002	2001
Miscellaneous:		
History donations	\$	\$ 44
Mann House trust		27
Museum donations		1
Fundraising plate fees	162	
Total Revenues	\$ 162	\$ 72

The amounts shown represent only the amounts collected by the Department of State and do not represent total revenues for the fund.

DEPARTMENT OF STATE
 Schedule of Revenues - Permanent Fund
Fiscal Years Ended September 30
 (In Thousands)

REVENUES	Children's Trust Fund	
	2002	2001
Miscellaneous:		
Fundraising plate fees	\$ 197	\$ 113
Total Revenues	\$ 197	\$ 113

The amounts shown represent only the amounts collected by the Department of State and do not represent total revenues for the fund.

DEPARTMENT OF STATE
Schedule of Certain General Fund Assets and Liabilities
As of September 30
(In Thousands)

	<u>2002</u>	<u>2001</u>
ASSETS		
Accounts Receivable:		
From services provided	\$ 2,850	\$ 4,449
From district courts	\$ 408	\$ 665
From federal agencies		\$ 311
From other funds	\$ 20,000	
Checks returned for not sufficient funds	\$ 834	\$ 2,052
Miscellaneous	\$ 5,825	\$ 4,531
LIABILITIES		
Deferred revenue	\$ 24	\$ 302
Accounts payable	\$ 668	\$ 620
Unearned receipts payable	\$ 60	\$ 415
Due to other funds	\$ 67	\$ 8
Due to component units	\$ 54	\$ 60
Amounts held for others	\$ 289	
Amounts held for other jurisdictions	\$ 5,274	\$ 4,639

This schedule is not a balance sheet and is not intended to report financial position. The schedule presents certain General Fund assets and liabilities that are the responsibility of the Department of State. The schedule does not include assets and liabilities that are accounted for centrally by the State, such as equity in Common Cash, cash in transit, warrants outstanding, and payroll liabilities.

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DEPARTMENT OF STATE
Schedule of Expenditures of Federal Awards (1)
For the Period October 1, 2000 through September 30, 2002
(In Thousands)

Federal Agency/Program	CFDA (2) Number	<u>For the Fiscal Year Ended September 30, 2001</u>		
		Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
<u>U.S. Department of Commerce</u>				
Direct Program:				
Coastal Zone Management Administration Awards	11.419	\$ 4	\$	\$ 4
Total U.S. Department of Commerce		\$ 4	\$ 0	\$ 4
<u>U.S. Department of the Interior</u>				
Direct Program:				
Historic Preservation Fund Grants-In-Aid	15.904	\$ 751	\$ 90	\$ 841
Total U.S. Department of the Interior		\$ 751	\$ 90	\$ 841
<u>U.S. Department of Transportation</u>				
Direct Program:				
Highway Planning and Construction	20.205	\$ 3	\$	\$ 3
Total U.S. Department of Transportation		\$ 3	\$ 0	\$ 3
Total Expenditures of Federal Awards		<u>\$ 758</u>	<u>\$ 90</u>	<u>\$ 848</u>

(1) Basis of Presentation: This schedule includes the federal grant activity of the Department of State and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial schedules.

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

(3) On May 29, 2001, the Governor issued Executive Order No. 2001-1 which resulted in the transfer of the Department of State's responsibilities associated with administration of State historical sites, State archives, and State cultural resources and treasures effective August 5, 2001. The transfer was accounted for as of October 1, 2001 and moved all three federal programs to the newly created Department of History, Arts and Libraries. As a result of this transfer, the Department of State did not have any federal grant activity for the fiscal year ended September 30, 2002.

For the Fiscal Year Ended September 30, 2002 (3)

<u>Directly Expended</u>	<u>Distributed to Subrecipients</u>	<u>Total Expended and Distributed</u>	<u>Total Expended and Distributed for the Two-Year Period</u>
\$	\$	\$	\$ 4
0	0	0	4
\$	\$	\$	\$ 841
0	0	0	841
\$	\$	\$	\$ 3
0	0	0	3
<u>0</u>	<u>0</u>	<u>0</u>	<u>848</u>



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

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

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

April 4, 2003

The Honorable Terri Lynn Land
Secretary of State
Treasury Building
Lansing, Michigan

Dear Secretary Land:

We have audited the financial schedules of the Department of State for the fiscal years ended September 30, 2002 and September 30, 2001, as identified in the table of contents, and have issued our report thereon dated April 4, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Department's financial schedules are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial schedule amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial schedules and not to provide assurance on internal control over financial reporting. However, we noted a matter involving internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over financial reporting that, in our judgment, could adversely affect the Department's ability to record,

process, summarize, and report financial data consistent with the assertions of management in the financial schedules. The reportable condition is described in the accompanying schedule of findings and questioned costs as Finding 1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial schedules being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control over financial reporting would not necessarily disclose all matters in internal control over financial reporting that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition identified in the previous paragraph is not a material weakness.

This report is intended solely for the information and use of the State's management, the Legislature, and federal awarding agencies 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



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

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

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

April 4, 2003

The Honorable Terri Lynn Land
Secretary of State
Treasury Building
Lansing, Michigan

Dear Secretary Land:

Compliance

We have audited the compliance of the Department of State with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each major federal program for the two-year period ended September 30, 2002. The Department'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 Department's management. Our responsibility is to express an opinion on the Department's compliance based on our audit.

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

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

Internal Control Over Compliance

The management of the Department 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 Department's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of internal control over compliance would not necessarily disclose all matters in internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the State's management, the Legislature, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS*

Section I: Summary of Auditor's Results

Financial Schedules

Type of auditor's report issued: Unqualified*

Internal control* over financial reporting:

Material weaknesses* identified? No

Reportable condition* identified that is not considered to be
a material weakness? Yes

Noncompliance material to the financial schedules? No

Federal Awards

Internal control over major programs:

Material weaknesses identified? No

Reportable conditions identified that are not considered to be
material weaknesses? None reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in
accordance with U.S. Office of Management and Budget (OMB)
Circular A-133, Section 510(a)? No

* See glossary at end of report for definition.

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program</u>
15.904	Historic Preservation Fund Grants-In-Aid

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

Auditee qualified as a low-risk auditee*? No

Section II: Findings Related to the Financial Schedules

FINDING (230301)

1. Internal Auditor Independence

The Department of State's internal auditor was not organizationally independent.

Section 18.1486(2) of the *Michigan Compiled Laws* requires each department's internal auditor to report to and be under the general supervision of the department head.

The Department's internal auditor was under the day-to-day supervision of the director of the Bureau of Legal Services but also reported to the chief operating officer. During our audit period, the chief operating officer also served as the Director of Department Services Administration, whose responsibilities include the oversight of the Department's accounting, budgeting, financial reporting, and human resource activities. This is considered a weakness in the Department's internal control because it impairs the internal auditor's independence with respect to audits of these activities.

The Department's internal auditor retired on October 30, 2002, and the position remained vacant as of the end of our audit fieldwork. The director of the Bureau of Legal Services assumed the responsibilities of the internal auditor. However, to avoid any future independence impairments, the internal auditor should be under the general supervision of the Secretary of State.

* See glossary at end of report for definition.

RECOMMENDATION

We recommend that the Department provide for organizational independence of its internal auditor.

Section III: Findings and Questioned Costs Related to Federal Awards

We did not report any findings related to federal awards.

OTHER SCHEDULES

DEPARTMENT OF STATE
Summary Schedule of Prior Audit Findings
As of September 30, 2002

There were no findings in the prior Department of State Single Audit.

DEPARTMENT OF STATE
Corrective Action Plan
As of May 27, 2003

FINDINGS RELATED TO THE FINANCIAL SCHEDULES

Finding Number: 230301
Finding Title: Internal Auditor Independence

Management Views: The Department of State agrees with the finding.

Corrective Action: The Department will realign the internal auditor reporting structure in such a way to provide organizational independence.

Anticipated Completion Date: July 2003

Responsible Individual: Brian DeBano, Chief of Staff

FINDINGS RELATED TO FEDERAL AWARDS

There were no findings related to federal awards for fiscal years 2000-01 and 2001-02.

Glossary of Acronyms and Terms

CFDA	<i>Catalog of Federal Domestic Assistance.</i>
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules and/or financial statements of an audited entity are fairly presented in conformity with the disclosed basis of accounting.
internal control	A process, effected by management, designed to provide reasonable assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
low-risk auditee	As provided for in OMB Circular A-133, an auditee that may qualify for reduced federal audit coverage if it receives an annual Single Audit and it meets other criteria related to prior audit results. In accordance with State statute, this Single Audit was conducted on a biennial basis; consequently, this auditee is not considered a low-risk auditee.
material misstatement	A misstatement in the financial schedules and/or financial statements that causes the schedules and/or statements to not present fairly the financial position or the results of operations or cash flows in conformity with the disclosed basis of accounting.
material noncompliance	Violations of laws and regulations that could have a direct and material effect on major federal programs or on financial schedule and/or financial statement amounts.
material weakness	A reportable condition related to the design or operation of internal control that does not reduce to a relatively low level the risk that either misstatements caused by error or fraud in amounts that would be material in relation to the financial schedules and/or financial statements or noncompliance with

applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

OMB

U.S. Office of Management and Budget.

questioned cost

A cost that is questioned by the auditor because of an audit finding: (1) which resulted from a violation or possible violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the use of federal funds, including funds used to match federal funds; (2) where the costs, at the time of the audit, are not supported by adequate documentation; or (3) where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

reportable condition

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

Single Audit

A financial audit, performed in accordance with the Single Audit Act Amendments of 1996, that is designed to meet the needs of all federal grantor agencies and other financial report users. In addition to performing the audit in accordance with the requirements of auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in

Government Auditing Standards issued by the Comptroller General of the United States, a Single Audit requires the assessment of compliance with requirements that could have a direct and material effect on a major federal program and the consideration of internal control over compliance in accordance with OMB Circular A-133.

SOMCAFR

State of Michigan Comprehensive Annual Financial Report.

subrecipient

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

UCC

Uniform Commercial Code.

unqualified opinion

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

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