



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

Audit report information may be accessed at:

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Michigan
Office of the Auditor General
REPORT SUMMARY

Financial Audit

*School Bond Loan Fund and School Loan Bond
 Redemption Fund*

Department of Treasury

October 1, 2002 through September 30, 2005

Report Number:
 27-330-05

Released:
 August 2006

A financial audit determines if the financial statements are fairly presented, considers internal control over financial reporting, and determines compliance with State compliance requirements material to the financial statements. This financial audit of the School Bond Loan Fund and School Loan Bond Redemption Fund was conducted as part of the constitutional responsibility of the Office of the Auditor General.

Financial Statements:

Auditor's Report Issued

We issued an unqualified opinion on the School Bond Loan Fund's and the School Loan Bond Redemption Fund's financial statements.

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Internal Control Over Financial Reporting

We did not report any findings related to internal control over financial reporting.

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**Noncompliance 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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Background:

School Bond Loan Fund

Article IX, Section 16 of the State Constitution and Sections 388.921 - 388.985 of the *Michigan Compiled Laws*

authorized the issuance of State general obligation bonds for loans to school districts. Loans are made for the payment of principal and interest on school district bonds under prescribed circumstances. State bond proceeds are credited to the fund as an "Other Financing Source." When loans are made, transfers are recorded to the State's General Fund, which receives loan repayments. In the General Fund, loans receivable are recorded as assets. The School Aid Fund currently provides debt service financing for the general obligation bonds.

School Loan Bond Redemption Fund

Act 74, P.A. 1955, created this fund to account for debt service on general obligation bonds issued to finance loans to local school districts.

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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>



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Lansing, Michigan 48913

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

Scott M. Strong, C.P.A., C.I.A.
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

August 24, 2006

Mr. Robert J. Kleine
State Treasurer
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Kleine:

This is our report on the financial audit of the School Bond Loan Fund and School Loan Bond Redemption Fund, Department of Treasury, for the period October 1, 2002 through September 30, 2005.

This report contains our report summary; our independent auditor's report on the financial statements; and the School Bond Loan Fund financial statements, School Loan Bond Redemption Fund financial statements, and notes to the financial statements. This report also contains our independent auditor's report on internal control over financial reporting and on compliance and other matters and a glossary of acronyms and terms.

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

AUDITOR GENERAL

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SCHOOL LOAN BOND REDEMPTION FUND
DEPARTMENT OF TREASURY**

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INDEPENDENT AUDITOR'S REPORT AND FINANCIAL STATEMENTS



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

Independent Auditor's Report on the Financial Statements

Mr. Robert J. Kleine
State Treasurer
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Kleine:

We have audited the accompanying financial statements of the School Bond Loan Fund and the School Loan Bond Redemption Fund, Department of Treasury, as of and for the fiscal years ended September 30, 2005, September 30, 2004, and September 30, 2003, as identified in the table of contents. These financial statements are the responsibility of the School Bond Loan Fund's and the School Loan Bond Redemption Fund's management and the Department of Treasury'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 School Bond Loan Fund and the School Loan Bond Redemption Fund and do not purport to, and do not, present fairly the financial position of the State of Michigan or its special revenue funds and debt service funds as of September 30, 2005, September 30, 2004, and September 30, 2003 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 School Bond Loan Fund and the School Loan Bond Redemption Fund as of September 30, 2005, September 30, 2004, and September 30, 2003 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 April 28, 2006 on our consideration of the School Bond Loan Fund's and the School Loan Bond Redemption Fund'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.

AUDITOR GENERAL

April 28, 2006

FINANCIAL STATEMENTS

SCHOOL BOND LOAN FUND
 Department of Treasury
 Balance Sheet
 As of September 30

	<u>2005</u>	<u>2004</u>	<u>2003</u>
ASSETS			
Current Assets:			
Equity in common cash	<u>\$ 1,226,121</u>	<u>\$ 562,230</u>	<u>\$ 4,169,830</u>
Total Assets	<u><u>\$ 1,226,121</u></u>	<u><u>\$ 562,230</u></u>	<u><u>\$ 4,169,830</u></u>
LIABILITIES AND FUND BALANCE			
Current Liabilities:			
Accounts payable and other liabilities	<u>\$ 711,620</u>	<u>\$ 78,466</u>	<u>\$ 51,688</u>
Total Liabilities	<u><u>\$ 711,620</u></u>	<u><u>\$ 78,466</u></u>	<u><u>\$ 51,688</u></u>
Fund Balance:			
Unreserved	<u>\$ 514,502</u>	<u>\$ 483,764</u>	<u>\$ 4,118,141</u>
Total Fund Balance	<u><u>\$ 514,502</u></u>	<u><u>\$ 483,764</u></u>	<u><u>\$ 4,118,141</u></u>
Total Liabilities and Fund Balance	<u><u>\$ 1,226,121</u></u>	<u><u>\$ 562,230</u></u>	<u><u>\$ 4,169,830</u></u>

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

SCHOOL BOND LOAN FUND
Department of Treasury
Statement of Revenues, Expenditures, and Changes in Fund Balance
Fiscal Years Ended September 30

	<u>2005</u>	<u>2004</u>	<u>2003</u>
REVENUES			
Total Revenues	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
EXPENDITURES			
Current:			
General government	<u>\$ 30,329,951</u>	<u>\$ 622,266</u>	<u>\$ 572,218</u>
Total Expenditures	<u>\$ 30,329,951</u>	<u>\$ 622,266</u>	<u>\$ 572,218</u>
Excess of Revenues Over (Under) Expenditures	<u>\$ (30,329,951)</u>	<u>\$ (622,266)</u>	<u>\$ (572,218)</u>
OTHER FINANCING SOURCES (USES)			
Bonds and notes issued (Note 4)	<u>\$ 110,928,593</u>	<u>\$ 150,121,062</u>	<u>\$ 116,765,000</u>
Transfers to other funds	<u>(80,567,904)</u>	<u>(153,133,173)</u>	<u>(112,116,961)</u>
Total Other Financing Sources (Uses)	<u>\$ 30,360,689</u>	<u>\$ (3,012,111)</u>	<u>\$ 4,648,039</u>
Excess of Revenues and Other Sources Over (Under) Expenditures and Other Uses	<u>\$ 30,738</u>	<u>\$ (3,634,377)</u>	<u>\$ 4,075,821</u>
Fund Balance - Beginning of fiscal year	<u>483,764</u>	<u>4,118,141</u>	<u>42,320</u>
Fund Balance - End of fiscal year	<u><u>\$ 514,502</u></u>	<u><u>\$ 483,764</u></u>	<u><u>\$ 4,118,141</u></u>

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

SCHOOL LOAN BOND REDEMPTION FUND

Department of Treasury

Balance Sheet

As of September 30

	<u>2005</u>	<u>2004</u>	<u>2003</u>
ASSETS			
Current Assets:			
Equity in common cash	\$ _____	\$ _____	\$ _____
Total Assets	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
LIABILITIES AND FUND BALANCE			
Current Liabilities:			
Accounts payable and other liabilities	\$ _____	\$ _____	\$ _____
Total Liabilities	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
Fund Balance:			
Unreserved	\$ _____	\$ _____	\$ _____
Total Fund Balance	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
Total Liabilities and Fund Balance	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>

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

SCHOOL LOAN BOND REDEMPTION FUND
Department of Treasury
Statement of Revenues, Expenditures, and Changes in Fund Balance
Fiscal Years Ended September 30

	<u>2005</u>	<u>2004</u>	<u>2003</u>
REVENUES			
Total Revenues	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
EXPENDITURES			
Current:			
General government	\$ 2,287,704	\$ 543,938	\$
Debt Service:			
Bond principal retirement	24,755,000	213,965,000	14,920,000
Bond interest and fiscal charges	16,335,866	16,040,127	18,569,324
Total Expenditures	<u>\$ 43,378,570</u>	<u>\$ 230,549,066</u>	<u>\$ 33,489,324</u>
Excess of Revenues Over (Under) Expenditures	<u>\$ (43,378,570)</u>	<u>\$ (230,549,066)</u>	<u>\$ (33,489,324)</u>
OTHER FINANCING SOURCES (USES)			
Refunding bonds issued (Note 4)	\$ 445,944,278	\$ 139,188,938	\$
Payment to refunded bond escrow agent	(443,656,574)		
Transfers from other funds	41,090,866	91,360,127	33,489,324
Total Other Financing Sources (Uses)	<u>\$ 43,378,570</u>	<u>\$ 230,549,066</u>	<u>\$ 33,489,324</u>
Excess of Revenues and Other Sources Over (Under) Expenditures and Other Uses	\$	\$	\$
Fund Balance - Beginning of fiscal year	<u> </u>	<u> </u>	<u> </u>
Fund Balance - End of fiscal year	<u><u>\$ 0</u></u>	<u><u>\$ 0</u></u>	<u><u>\$ 0</u></u>

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

Notes to the Financial Statements

Note 1 Significant Accounting Policies

a. Reporting Entity

The accompanying financial statements report the financial position and the changes in financial position of the School Bond Loan Fund and the School Loan Bond Redemption Fund as of and for the fiscal years ended September 30, 2005, September 30, 2004, and September 30, 2003.

The Department of Treasury is responsible for administering the School Bond Loan Fund and the School Loan Bond Redemption Fund.

Each of these funds is a part of the State of Michigan's reporting entity. The School Bond Loan Fund is reported as a special revenue fund and the School Loan Bond Redemption Fund is reported as a debt service fund in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*.

The notes accompanying these financial statements relate directly to the School Bond Loan Fund and the School Loan Bond Redemption Fund. The *SOMCAFR* provides more extensive disclosures regarding the State's significant accounting policies; budgeting, budgetary control, and legal compliance; common cash; pension benefits and other postemployment benefits; and other long-term obligations.

b. Measurement Focus, Basis of Accounting, and Presentation

The 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 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 a liability is incurred;

however, certain expenditures related to long-term obligations are recorded only when payment is due and payable.

The accompanying financial statements present only the School Bond Loan Fund and the School Loan Bond Redemption Fund. 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 special revenue funds or its debt service funds in conformity with generally accepted accounting principles.

Note 2 Description of Funds

a. School Bond Loan Fund

Article IX, Section 16 of the State Constitution and Sections 388.921 - 388.985 of the *Michigan Compiled Laws* authorized the issuance of State general obligation bonds for loans to school districts. Loans are made for the payment of principal and interest on school district bonds under prescribed circumstances. State bond proceeds are credited to the fund as an "Other Financing Source."

When loans are made to school districts, transfers are recorded to the State's General Fund. In the General Fund, the loans receivable are recorded as assets. The General Fund receives the loan repayment. The School Aid Fund currently provides debt service financing for the general obligation bonds.

b. School Loan Bond Redemption Fund

Act 74, P.A. 1955, established this fund to account for debt service on general obligation bonds issued to finance loans to local school districts.

Loan repayments from school districts are deposited in the General Fund.

Note 3 Budgeting and Budgetary Control

The School Bond Loan Fund's and the School Loan Bond Redemption Fund's statements of revenues, expenditures, and changes in fund balance do not include amounts for budget and actual. The State of Michigan does not adopt budgets for these funds.

Note 4 Bonds Payable

a. General Long-Term Obligations

Article IX, Section 16 of the State Constitution authorizes the State to borrow (without voter approval) for the purpose of providing loans to school districts. General Fund and School Aid Fund appropriations were made to finance debt principal and interest requirements for general obligation bond issues. These bonds are backed by the full faith and credit of the State.

School loan bonds issued and outstanding at September 30, 2005, September 30, 2004, and September 30, 2003 (in millions):

	Amounts Issued	Amounts Outstanding at September 30			Fiscal Year Maturities		Average Interest Rate
		2005	2004	2003	First Year	Last Year	Percentage
Series 1995	\$180.0	\$17.0	\$ 24.9	\$ 32.4	1997	2007	5.47%
Series 1998	160.0	58.8	65.7	72.4	2001	2012	4.86%
Series 2001 A*	81.3			81.3	2005	2021	variable
Series 2001 C*	45.9		45.9	45.9	2019	2021	variable
Series 2002 A*	50.6		31.0	31.0	2005	2019	variable
Series 2002 B*	47.3		46.5	47.3	2018	2021	variable
Series 2003 A*	61.5			61.5	2019	2021	variable
Series 2003 B*	3.3		3.3	3.3	2008	2010	variable
Series 2003 C*	4.7			4.7	2008	2010	variable
Series 2004 A*	203.2		203.2		2020	2024	variable
Series 2004 B*	35.1		35.1		2020	2024	variable
Series 2005 B*	362.5	362.5			2008	2025	variable
Series 2005 C*	113.1	113.1			2020	2024	variable
Total	<u>\$1,348.5</u>	<u>\$551.4</u>	<u>\$455.6</u>	<u>\$379.8</u>			

* These bonds currently bear interest at a commercial paper rate and are remarketed at each maturity. For the future debt service requirements, interest was estimated at the interest rate in effect at September 30.

b. Refundings and Defeasances

The State has defeased certain bonds through advance refundings* by placing the proceeds of new bonds in irrevocable trust to provide for all future debt service on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds* are not presented as assets or liabilities in the statements and are not included in the debt table in this note.

The State has defeased certain bonds through current refundings* in which the proceeds of the refunding debt are applied immediately to redeem the debt to be refunded.

The following table summarizes the defeased school loan bonds outstanding at September 30, 2005, September 30, 2004, and September 30, 2003 (in millions):

	Amounts Outstanding at September 30		
	2005	2004	2003
Series 1995	\$ 103.3	\$103.3	\$103.3
Series 1998	69.1	69.1	69.1
Series 2001 C	45.9		
Series 2002 A	30.9		
Series 2002 B	46.5		
Series 2003 B	3.3		
Series 2004 A	203.2		
Series 2004 B	25.4		
Series 2004 C	22.0		
Series 2005 A	59.2		
Total	\$ 608.7	\$172.4	\$172.4

c. General Obligation

During fiscal year 2004-05, the State of Michigan issued \$475.6 million of General Obligation Multi-Modal School Loan Bonds Series 2005 B and C maturing in years 2008 through 2025 with a variable interest rate. The

* See glossary at end of report for definition.

maximum interest rate applicable to Series 2005 B is 15% annually and the maximum interest rate applicable to Series 2005 C is 12% annually. From the proceeds, \$436.3 million was used to refund principal and pay interest due on School Loan Bonds Series 2001 C, 2002 A, 2002 B, 2003 B, 2004 A, 2004 B, 2004 C, and 2005 A. The remaining \$39.3 million was transferred to the School Bond Loan Fund to make loans to local school districts and pay issuance costs.

During fiscal year 2003-04, the State of Michigan issued, as a current refunding, \$238.3 million of General Obligation Multi-Modal School Loan Bonds Series 2004 A and B maturing in years 2020 through 2024 with a variable interest rate. The maximum interest rate applicable to the Series 2004 A bonds is 10% annually and the maximum interest rate applicable to the Series 2004 B bonds is 12% annually. From the proceeds, \$104.3 million was deposited into the School Bond Loan Fund: \$96.5 million was used to make loans to school districts and to pay for the cost of the issuance of the bonds and \$7.8 million was transferred to the School Loan Bond Redemption Fund to refund interest on general obligation bonds and school loan bonds. The remaining \$134.0 million was transferred to the School Loan Bond Redemption Fund and was used to refund principal and interest on general obligation and school loan bonds.

During fiscal year 2003-04, the State of Michigan also issued, as a current refunding, \$51.0 million of General Obligation Multi-Modal School Loan Bonds Series 2003 D and E maturing in years 2017 through 2021 with a variable interest rate. The maximum interest rate applicable to the Series 2003 D and E bonds is 12% annually. From the proceeds, \$45.8 was deposited into the School Bond Loan Fund: \$24.0 million was used to make loans to school districts and \$21.8 million was transferred to the School Loan Bond Redemption Fund to make regularly scheduled principal and interest payments and to pay for the cost of the issuance of the bonds. The remaining proceeds of \$5.2 million were transferred to the School Loan Bond Redemption Fund and were used to refund principal and interest on general obligation bonds and school loan bonds. These bonds were issued and completely refunded in fiscal year 2003-04 with the proceeds of School Loan Multi-Modal Bonds Series 2004 A and B.

The variable rate refunded and new debt bear interest rates based upon various periodic market rates and are remarketed at each maturity.

Note 5 Contingent Liabilities for School District Bonds

Sections 388.951 - 388.963 of the *Michigan Compiled Laws* (Act 108, P.A. 1961, as amended) resulted in a contingent liability for the qualified bonds* of school districts. School districts that receive State qualification for their bond issuances are eligible to borrow and the State is required to lend them the amounts necessary for the school districts to avoid default on their qualified bonds. In the event that funds are not available in the School Bond Loan Fund in adequate amounts to make such a loan, the State is required to make loans from the General Fund. The principal amount of qualified bonds outstanding was \$13.8 billion at September 30, 2005; \$13.5 billion at September 30, 2004; and \$12.5 billion at September 30, 2003. Total debt service requirements on these bonds including interest will approximate \$1.3 billion in fiscal year 2005-06, \$1.2 billion in fiscal year 2004-05, and \$1.1 billion in fiscal year 2003-04. The amount of outstanding loans by the State to school districts related to school districts bonds qualified under this program was \$600.7 million as of September 30, 2005; \$527.4 million as of September 30, 2004; and \$414.4 million as of September 30, 2003. Interest due on these loans was \$98.6 million as of September 30, 2005; \$87.7 million as of September 30, 2004; and \$76.7 million as of September 30, 2003.

Note 6 Subsequent Events

During fiscal year 2005-06, the State paid off \$13.0 million of its General Obligation Multi-Modal Taxable School Loan Bonds Series 2005 B.

In addition, during fiscal year 2005-06, the State issued General Obligation Multi-Modal Taxable School Loan Bonds Series 2006 A in the aggregated principal amount of \$66.8 million. The Series 2006 A Bonds were issued in the Commercial Paper Rate Mode. The bonds will mature on March 1, 2025.

Note 7 School Loan Revolving Fund

Effective July 20, 2005, Act 112, P.A. 1961, which implements Article IX, Section 16 of the State Constitution, was amended to provide that, after the

* See glossary at end of report for definition.

effective date, the proceeds of the sale of notes or bonds issued by the State to make loans to school districts shall be deposited in the School Loan Revolving Fund established by the Michigan Municipal Bond Authority pursuant to Section 16c of Act 227, P.A. 1985, as amended. Act 112 further provides that, unless amounts on deposit in the School Loan Revolving Fund are insufficient for the purpose of making loans to school districts, the State Treasurer may satisfy the requirements of Article IX, Section 16 of the State Constitution by causing loans to school districts to be made from the School Loan Revolving Fund.

Act 227 authorizes the Michigan Municipal Bond Authority to issue bonds or notes to fund the School Loan Revolving Fund. Any money repaid by school districts on loans made from the School Loan Revolving Fund shall be deposited in the School Loan Revolving Fund. The School Loan Revolving Fund may also be funded by contributions from the State, including contributions resulting from the assignment by the State of the right to receive loan repayments on qualified loans made by the State from the School Bond Loan Fund prior to the effective date. Funds deposited in the School Loan Revolving Fund may be used only to make qualified loans to school districts, to fund a reserve fund, to secure bonds or notes issued by the Michigan Municipal Bond Authority to provide funds for the School Loan Revolving Fund, to provide a surety for the payment of bonds or notes that provide direct or indirect State sponsorship or support to a school district, and to pay the cost of administering the School Loan Revolving Fund.

During fiscal year 2004-05, the State transferred \$30 million from bond proceeds out of the School Bond Loan Fund into the School Loan Revolving Fund for start-up.

INDEPENDENT AUDITOR'S REPORT ON
INTERNAL CONTROL AND COMPLIANCE



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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

Mr. Robert J. Kleine
State Treasurer
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Kleine:

We have audited the financial statements of the School Bond Loan Fund and the School Loan Bond Redemption Fund, Department of Treasury, as of and for the fiscal years ended September 30, 2005, September 30, 2004, and September 30, 2003, as identified in the table of contents, and have issued our report thereon dated April 28, 2006. 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 School Bond Loan Fund's and the School Loan Bond Redemption Fund's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

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

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

April 28, 2006

GLOSSARY

Glossary of Acronyms and Terms

advance refunding	A method of eliminating a bond issue as an obligation of the issuer by issuing a new bond issue and using the proceeds to purchase government obligations which are escrowed and used to provide debt service on the original issue at a future time.
current refunding	The issuance of new debt whose proceeds are used to repay previously issued debt.
defeased bonds	Bonds that are advance refunded bonds. Debt service is provided by escrowed funds and the defeased advance refunded bonds are no longer an obligation of the issuer.
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.
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 misstatements caused by error or fraud in amounts that would be material in relation to the financial schedules and/or financial statements may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

qualified bonds

School district bonds issued to fund capital improvement projects which have been approved by the Department of Treasury and a local election. A school district with qualified bonds is eligible to borrow and the State is required to lend it any amount necessary to avoid default on bond principal and interest payments.

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 initiate, record, process, and report financial data consistent with the assertions of management in the financial schedules and/or financial statements.

SOMCAFR

State of Michigan Comprehensive Annual Financial Report.

