



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 can be accessed at:

<http://audgen.michigan.gov>



Michigan
Office of the Auditor General
REPORT SUMMARY

Report on the Provisions of the Single Audit Act

Report Number:
271-0341-11

Michigan Finance Authority

(A Discretely Presented Component Unit of the State of Michigan)

October 1, 2008 through September 30, 2010

Released:
June 2011

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

Financial Statements:

We have audited the basic financial statements of the Michigan Finance Authority for the fiscal year ended September 30, 2010 and have issued an unqualified opinion dated February 3, 2011. We have also audited the basic financial statements of the Michigan Higher Education Assistance Authority, the basic financial statements of the Michigan Higher Education Student Loan Authority, and the basic financial statements of the Michigan Public Educational Facilities Authority as of and for the fiscal year ended September 30, 2009 and have issued unqualified opinions dated December 22, 2009, December 21, 2009, and May 3, 2010, respectively.

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Auditor's Report Issued

We issued an unqualified opinion on the Authority's schedule of expenditures of federal awards in relation to the basic financial statements taken as a whole.

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Internal Control Over Financial Reporting

We have also issued an independent auditor's report on internal control over financial reporting and on compliance and other matters for the fiscal year ended September 30, 2010 thereon dated

February 3, 2011. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses.

In addition, we have issued independent auditor's reports on internal control over financial reporting and on compliance and other matters for the Michigan Higher Education Assistance Authority, the Michigan Higher Education Student Loan Authority, and the Michigan Public Educational Facilities Authority for the fiscal year ended September 30, 2009 thereon dated December 22, 2009, December 21, 2009, and May 3, 2010, respectively. We identified a material weakness in internal control over financial reporting related to the Michigan Public Educational Facilities Authority. We also identified a significant deficiency related to the Michigan Higher Education Assistance Authority.

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**Noncompliance and Other Matters
Material to the Financial Statements**

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

~ ~ ~ ~ ~

Federal Awards:

Auditor's Report Issued on Compliance

We audited 4 programs as major programs and issued 4 unqualified opinions. The Authority expended a total of \$298.8 million in federal awards during the two-year period ended September 30, 2010. The federal programs audited as major programs are identified at the bottom of this summary.

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Internal Control Over Major Programs

We did not identify any deficiencies in internal control over federal program compliance that we consider to be material weaknesses. However, we did identify significant deficiencies (Findings 1 and 2).

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Required Reporting of Noncompliance

We identified instances of noncompliance that are required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133 (Findings 1 and 2).

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Background:

The Michigan Finance Authority is a discretely presented component unit of the State of Michigan that consolidated certain public finance authorities in Michigan in accordance with Executive Order No. 2010-2, effective May 30, 2010. The Authority combined the operations of 10 different public finance authorities (Michigan Forest Finance Authority, Michigan Higher Education Assistance Authority, Michigan Higher Education Facilities Authority, Michigan Higher Education Student Loan Authority, Michigan Municipal Bond Authority, Michigan Public Educational Facilities Authority, Michigan State Hospital Finance Authority, Michigan Tobacco Settlement Finance Authority, Michigan Underground Storage Tank Financial Assurance Authority, and State Higher Education Facilities Commission). In addition, the authorization to finance the facilities of public and private schools formerly under the Michigan Strategic Fund and to issue bonds and notes on behalf of the State Land Bank Fast Track Authority was transferred to the Authority.

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We audited the following programs as major programs:

<u>CFDA Number</u>	<u>Program Title</u>	<u>Compliance Opinion</u>
84.032G	Federal Family Education Loans - Guaranty Agency	Unqualified
84.032L	Federal Family Education Loans - Lender	Unqualified
84.185A	Byrd Honors Scholarships	Unqualified
84.354	Credit Enhancement for Charter School Facilities	Unqualified

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



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

June 17, 2011

Mr. Andy Dillon, State Treasurer and Chair
Michigan Finance Authority Board of Directors
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Dillon:

This is our report on the provisions of the Single Audit Act as applicable to the Michigan Finance Authority, a discretely presented component unit of the State of Michigan, for the period October 1, 2008 through September 30, 2010. We have also audited the Authority's financial statements for the fiscal year ended September 30, 2010 and have issued a separate report thereon dated February 3, 2011. In addition, we have audited the financial statements of the Michigan Higher Education Assistance Authority, the financial statements of the Michigan Higher Education Student Loan Authority, and the financial statements of the Michigan Public Educational Facilities Authority as of and for the fiscal year ended September 30, 2009 and have issued our reports thereon dated December 22, 2009, December 21, 2009, and May 3, 2010, respectively.

This report contains our report summary; our independent auditor's report on compliance with requirements that could have a direct and material effect on each major program, on internal control over compliance, and on the schedule of expenditures of federal awards in accordance with U.S. Office of Management and Budget Circular A-133; the Authority's schedule of expenditures of federal awards; and our schedule of findings and questioned costs. In addition, the report contains the Authority's summary schedule of prior audit findings, its corrective action plan, and a glossary of acronyms and terms.

Our findings and recommendations are contained in Section III 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 plan to address the audit recommendations and submit it within 60 days after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

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

AUDITOR GENERAL

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INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE,
INTERNAL CONTROL OVER COMPLIANCE,
AND THE SCHEDULE OF
EXPENDITURES OF FEDERAL AWARDS



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AUDITOR GENERAL

Independent Auditor's Report on Compliance With
Requirements That Could Have a Direct and Material Effect on
Each Major Program, on Internal Control Over Compliance,
and on the Schedule of Expenditures of Federal Awards in
Accordance With OMB Circular A-133

Mr. Andy Dillon, State Treasurer and Chair
Michigan Finance Authority Board of Directors
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Dillon:

Compliance

We have audited the Michigan Finance Authority's compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Authority's major federal programs for the two-year period ended September 30, 2010. The Authority's major federal programs are 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 of its major federal programs is the responsibility of the Authority's management. Our responsibility is to express an opinion on the Authority's compliance based on our audit.

We did not audit the Michigan Finance Authority's compliance with the following compliance requirements applicable to the Federal Family Education Loans Program, *CFDA 84.032L*: reporting and special tests and provisions (individual record review; loan origination and lender loan fees; interest benefits; special allowance payments; loan sales, purchases, and transfers; enrollment reports; payment processing; due diligence by lenders in the collection of delinquent loans; timely claim filings by lenders or servicers; and curing due-diligence and timely filing violations). Third-party servicers Great Lakes Educational Loan Services Inc., NelNet Inc., and Sallie Mae Inc. performed these compliance requirements for the Authority and have obtained audits performed under the December 1996 Audit Guide, *Compliance Audits (Attestation Engagements) for Lenders and Lender Servicers Participating in the Federal Family Education Loan Program (Lender Audit Guide)*, issued by the U.S. Department of Education. Great Lakes Educational Loan Services Inc. lender audits covered the periods October 1, 2008 through September 30, 2009 and October 1, 2009 through September 30, 2010, and NelNet Inc. and Sallie Mae Inc. lender audits covered the periods January 1, 2008 through December 31, 2008, January 1, 2009 through December 31, 2009, and January 1, 2010 through December 31, 2010. Our report does not include the results of the other accountants' examinations of the third-party servicers' compliance with such requirements.

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 first 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 Authority'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 Authority's compliance with those requirements.

In our opinion, the Michigan Finance Authority complied, in all material respects, with the compliance requirements referred to in the first paragraph that could have a direct and material effect on each of its major federal programs for the two-year period ended September 30, 2010. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs in Findings 1 and 2.

Internal Control Over Compliance

Management of the Authority 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 Authority's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the 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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined in the preceding paragraph. However, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies as described in the accompanying schedule of findings and questioned costs in Findings 1 and 2. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Michigan Finance Authority as of and for the fiscal year ended September 30, 2010 and have issued our report thereon dated February 3, 2011. We have also audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Michigan Higher Education Assistance Authority, the financial statements of the business-type activities and each proprietary fund of the Michigan Higher Education Student Loan Authority, and the basic financial statements of the Michigan Public Educational Facilities Authority as of and for the fiscal year ended September 30, 2009 and have issued our reports thereon dated December 22, 2009, December 21, 2009, and May 3, 2010, respectively. Our audits were performed for the purpose of forming our opinions on the financial statements that collectively comprise the Michigan Finance Authority's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the Authority's basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

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

This report is intended solely for the information and use of the Governor, the Legislature, the Michigan Finance Authority Board of Directors, management, others within the entity, 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

May 27, 2011 – As pertaining to Compliance and Internal Control Over Compliance

February 3, 2011 – As pertaining to the Schedule of Expenditures of Federal Awards

FINANCIAL SCHEDULE

MICHIGAN FINANCE AUTHORITY
Schedule of Expenditures of Federal Awards (Notes 1, 2, and 3)
For the Period October 1, 2008 Through September 30, 2010

Federal Agency/Program	CFDA *	Directly Expended for the		Total Expended for the Two-Year Period
		Fiscal Year Ended September 30		
	Number	2009	2010	
U.S. Department of Education (USDOE)				
Direct Programs (Note 4):				
Federal Family Education Loans - Guaranty Agency (Note 5)	84.032G			
Loan Loss Reinsured by USDOE		\$ 149,428,680	\$ 137,570,887	\$ 286,999,567
Account Maintenance Fees		2,706,866	2,437,063	5,143,929
Loan Processing and Issuance Fees		2,783,213	1,381,147	4,164,360
Loan Recoveries - Net of Amounts Returned to USDOE		3,244,177	3,562,428	6,806,605
Loans Repurchased and Rehabilitated		2,482,912	8,108,030	10,590,942
Total Federal Family Education Loans - Guaranty Agency		<u>\$ 160,645,848</u>	<u>\$ 153,059,555</u>	<u>\$ 313,705,403</u>
Federal Family Education Loans - Lender (Note 5)	84.032L			
Interest Subsidy Payments		\$ 21,310,927	\$ 14,547,149	\$ 35,858,076
Special Allowance Payments		(27,308,773)	(31,391,951)	(58,700,724)
Total Federal Family Education Loans - Lender		<u>\$ (5,997,846)</u>	<u>\$ (16,844,802)</u>	<u>\$ (22,842,648)</u>
Byrd Honors Scholarships	84.185A	\$ 1,360,500	\$ 0	\$ 1,360,500
Credit Enhancement for Charter School Facilities (Note 6)	84.354	3,158,710	6,621,357	6,621,357
Total U.S. Department of Education		<u>\$ 159,167,212</u>	<u>\$ 142,836,110</u>	<u>\$ 298,844,612</u>
Total Expenditures of Federal Awards		<u><u>\$ 159,167,212</u></u>	<u><u>\$ 142,836,110</u></u>	<u><u>\$ 298,844,612</u></u>

* CFDA is defined as *Catalog of Federal Domestic Assistance*.

The accompanying notes are an integral part of this schedule.

Notes to the Schedule of Expenditures of Federal Awards

Note 1 Reporting Entity

The Michigan Finance Authority is a discretely presented component unit of the State of Michigan that consolidated certain public finance authorities in Michigan in accordance with Executive Order No. 2010-2, effective May 30, 2010. The Authority combined the operations of 10 different public finance authorities (Michigan Forest Finance Authority, Michigan Higher Education Assistance Authority, Michigan Higher Education Facilities Authority, Michigan Higher Education Student Loan Authority, Michigan Municipal Bond Authority, Michigan Public Educational Facilities Authority, Michigan State Hospital Finance Authority, Michigan Tobacco Settlement Finance Authority, Michigan Underground Storage Tank Financial Assurance Authority, and State Higher Education Facilities Commission). In addition, the authorization to finance the facilities of public and private schools formerly under the Michigan Strategic Fund and to issue bonds and notes on behalf of the State Land Bank Fast Track Authority was transferred to the Authority.

The Authority is governed by its own Board of Directors, comprised of seven members, consisting of the State Treasurer as chair and six appointees of the Governor with the advice and consent of the State Senate. The Board provides overall governing direction for the Authority. The Authority is not empowered to create, in any fashion, debt or liabilities on behalf of the State or to pledge the full faith and credit of the State. All administrative functions of the Authority, including budgeting, procurement, personnel, and management functions, are under the direction and supervision of the State Treasurer.

The Authority is empowered to borrow money and to issue its bonds and notes to provide sources of funding for loans to governmental units and school districts. In addition, the Authority may issue bonds and notes to provide sources of funding for nonpublic-nonprofit institutions of higher education, governmental units, and eligible health care providers and facilities and to undertake or continue public and capital improvements by assisting governmental units in financing and marketing municipal debt and tax-exempt bonds.

The Authority is also empowered to complement and supplement the student loan efforts of Michigan private lenders by making loans and acquiring loans made to students and their parents, thereby enhancing access to higher education. The Authority's Michigan Guaranty Agency was formed for the purpose of guaranteeing loans to qualified students and parents of qualified students made through approved financial institutions.

Note 2 Basis of Presentation

This schedule of expenditures of federal awards (SEFA) presents the federal grant activity of the Michigan Finance Authority on the accrual basis of accounting and in accordance with the requirements of U.S. Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Note 3 Significant Accounting Policies

The SEFA is prepared in accordance with accounting principles generally accepted in the United States of America. The accrual basis of accounting is used in connection with federal expenditures reported on the SEFA. Differences may exist between federal expenditures shown on the SEFA and related federal expenditures on federal financial reports because of additional accrual amounts recorded after the preparation of the federal financial reports for the fiscal year.

Note 4 Descriptions of Programs

Federal Family Education Loans - Guaranty Agency: The Authority receives federal loan reinsurance revenue from the U.S. Department of Education according to the following schedule for all eligible default claims purchased by the Authority:

Annual Default Rate	Federal Reinsurance
0% to less than 5%	95%
5% to less than 9%	95% of claims up to 5%, 85% of claims equal to or greater than 5% but less than 9%
9% or greater	95% of claims up to 5%, 85% of claims equal to or greater than 5% but less than 9%, and 75% of claims equal to or greater than 9%

For claims filed on loans guaranteed prior to October 1, 1998, the reinsurance rates of 95%/85%/75% reflected in the preceding schedule are increased to 98%/88%/78%, respectively. For claims filed on loans guaranteed prior to October 1, 1993, the reinsurance rates are increased to 100%/90%/80%, respectively. The federal government has defined the default rate to be the default claims presented to the federal government during the federal fiscal year ending September 30, divided by loans in repayment at the beginning of the federal fiscal year, plus certain other adjustments. The default rates, as defined above, for the fiscal years ended September 30, 2010 and September 30, 2009, did not exceed 5%. Death and disability claims are 100% reinsured regardless of the default rate.

Effective October 1, 1998, the Higher Education Amendments of 1998 established an account maintenance fee based on 0.12% of the original principal amount of outstanding loans. The account maintenance fee is paid to the Authority on a quarterly basis by the federal government. This fee is recognized as revenue and recorded in the operating fund. Effective October 1, 2003, the account maintenance fee was reduced to 0.10% of the original principal amount of outstanding loans. Effective October 1, 2007, the account maintenance fee was reduced to 0.06% of the original principal amount of outstanding loans.

The 1998 Amendments also established a loan processing and issuance fee. Loan processing and issuance fee payments are based on the net guarantee amount, less cancellations, multiplied by 0.65%. The loan processing and issuance fee is paid to the Authority on a quarterly basis by the federal government. This fee is recognized as revenue and recorded in the operating fund. Effective October 1, 2003, the loan processing and issuance fee was reduced to 0.40% of net guarantees, less cancellations.

Effective October 1, 2007, the retention rate decreased from 23% to 16% as required by the 2007 College Cost Reduction and Access Act. The Authority is entitled to retain 16% of collections received for defaulted loans for which federal reinsurance has been received.

The Authority is entitled to retain 18.5% of principal and 100% of interest and collections costs for rehabilitated loans.

Federal Family Education Loans - Lenders: The Federal Family Education Loans (FFEL) Program provides the Authority with interest on subsidized student loans during the period a student is attending school or during certain other allowable grace and deferment periods. In addition, the FFEL Program provides funding (special allowance) that is primarily an incentive payment in order that money market conditions or interest rates will not impede the origination of student loans. For loans first disbursed on or after October 1, 2007, the College Cost Reduction and Access Act reduced the special allowance factors and the Deficit Reduction Act of 2005 required that, if the resulting special allowance calculation was negative, the negative special allowance must be paid to the U.S. Department of Education.

Byrd Honors Scholarships: The Byrd Honors Scholarships Program provides outstanding high school seniors who show promise of continued academic achievement with scholarships to support postsecondary education in an effort to recognize and promote student excellence and achievement.

The Michigan Higher Education Assistance Authority administered the Byrd Honors Scholarships Program through September 30, 2009 and, accordingly, the SEFA includes Byrd Honors Scholarships Program grant activity for the fiscal year ended September 30, 2009. Executive Order No. 2010-2, effective May 30, 2010, transferred the Byrd Honors Scholarships Program to the Department of Treasury and, accordingly, the Byrd Honors Scholarships Program grant activity for the fiscal year ended September 30, 2010 is included in the SEFA of the financial audit, including the provisions of the Single Audit Act, of the Department of Treasury (271-0100-11).

Credit Enhancement for Charter School Facilities: The Authority used its Credit Enhancement for Charter School Facilities grant to establish the Michigan Charter School Credit Enhancement Fund to guarantee revenue bonds issued to provide financing for the acquisition, construction, repair, or renovation of Michigan charter school facilities.

The Authority drew down the entire federal grant amount of \$6,531,246 in fiscal year 2007-08 and recorded deferred revenue. The Authority recognized federal revenue and expenses when it placed the federal grant funds into debt service reserve funds for individual charter school bond issuances.

The SEFA includes Credit Enhancement for Charter School Facilities grant activity for the fiscal year ended September 30, 2009 for comparative purposes only. These expenditures were audited as part of the financial audit, including the provisions of the Single Audit Act, of the Michigan Public Educational Facilities Authority (271-0275-10) for the two-year period ended September 30, 2009 with opinion letters dated May 3, 2010.

Note 5 Loans Outstanding

The Authority had the following FFEL Program loan balances and guarantees outstanding at September 30, 2010 and September 30, 2009. These loan balances and guarantees are not included in the federal expenditures presented in the SEFA:

Federal Program Title	CFDA Number	Loan Amounts Outstanding at September 30	
		2010	2009
Federal Family Education Loans:			
Guaranty Agency	84.032G	\$3,824,759,128	\$4,408,441,615
Lender	84.032L	\$1,596,597,817	\$1,767,223,937

Note 6 SEFA Expenditures - Credit Enhancement for Charter School Facilities

During fiscal year 2009-10, the Authority used \$3,452,321 to establish a debt service reserve fund for \$45,080,000 of limited obligation bonds issued for 6 charter schools. During fiscal year 2008-09, the Authority used \$1,000,000 to establish a debt service reserve fund for \$10,720,000 of limited obligation bonds issued for 1 charter school. During fiscal year 2007-08, the Authority used \$1,974,750 to establish debt service reserve funds for \$25,865,000 of limited obligation bonds issued for 5 charter schools. In addition, the Authority incurred administrative expenses of \$837, \$247, and \$488 in fiscal years 2009-10, 2008-09, and 2007-08, respectively.

The U.S. Department of Education program guidance for the Credit Enhancement for Charter School Facilities grant indicates that the value of federal awards expended is the total of the following amounts:

- (a) The amount in the reserve fund at the beginning of the grantee fiscal year; plus
- (b) Any funds drawn down in the grantee's fiscal year to add to the reserve fund; plus
- (c) Any earnings on the reserve account.

The following table indicates the amounts used to calculate the SEFA expenditures:

	Fiscal Year		
	2009-10	2008-09	2007-08
Reserve fund beginning balance	\$3,158,710	\$2,128,510	\$ 0
Funds placed in reserve fund during the fiscal year	3,453,158	1,000,247	1,975,238
Reserve account earnings	9,489	29,953	153,272
Total	\$6,621,357	\$3,158,710	\$2,128,510

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section I: Summary of Auditor's Results

Financial Statements

Type of auditor's report issued:	Unqualified*
Internal control* over financial reporting:	
Material weaknesses* identified?	No
Significant deficiencies* identified?	None reported
Noncompliance or other matters material to the financial schedules?	No

Federal Awards

Internal control over major programs:	
Material weaknesses* identified?	No
Significant deficiencies* identified?	Yes
Type of auditor's report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with U.S. Office of Management and Budget* (OMB) Circular A-133, Section 510(a)?	Yes

Identification of major programs:

<u>CFDA* Number</u>	<u>Name of Federal Program</u>
84.032G	Federal Family Education Loans - Guaranty Agency
84.032L	Federal Family Education Loans - Lender
84.185A	Byrd Honors Scholarships
84.354	Credit Enhancement for Charter School Facilities

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

* See glossary at end of report for definition.

Section II: Findings Related to the Financial Statements

We did not report any findings related to the financial statements in our financial audit* of the Michigan Finance Authority.

The status of the findings related to the financial statements that were reported in prior single audits* is disclosed in the summary schedule of prior audit findings.

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

OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, requires the auditor to test key controls at a level that would provide sufficient evidence that the established control structure would provide a high probability that material federal program noncompliance would be prevented or detected and corrected. This requires that the auditor set the tolerable exception rate of occurrence at a very low level. During the audit fieldwork, the auditor, in close consultation with the auditee, identifies the key controls that the auditee has established to ensure federal program compliance. In those cases in which the auditor's tests of key controls identify exception rates in excess of the tolerable exception rate of occurrence, the auditor must generally report the observed exception rate in the report finding.

Further, Circular A-133 requires the auditor to report in this section of the audit report known questioned costs that are greater than \$10,000 for a type of compliance requirement for a major program and known questioned costs that are less than \$10,000 for a type of compliance requirement for a major program if it is likely that total questioned costs would exceed \$10,000.

As a result of these low required reporting thresholds, the reader may note that, in some cases, the observed exception rates of occurrence and reported known questioned costs appear insignificant in relation to the overall federal expenditures of the auditee. After the audit report is filed with the federal audit clearinghouse, the responsible federal agency is required to issue a management decision within six months of the receipt of the audit report. The management decision may include a request for the return of the known questioned costs.

* See glossary at end of report for definition.

FINDING (2711101MFA)

1. Byrd Honors Scholarships, CFDA 84.185A

U.S. Department of Education	CFDA 84.185A: Byrd Honors Scholarships
Award Number: P185A080023	Award Period: 07/01/2008 - 06/30/2009
	Known Questioned Costs: \$0

The Department of Treasury's internal control over the Byrd Honors Scholarships Program did not ensure compliance with federal laws and regulations regarding reporting. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of the Byrd Honors Scholarships Program awards.

All administrative functions of the Michigan Finance Authority, including budgeting, procurement, personnel, and management functions, are under the direction and supervision of the State Treasurer within the Department of Treasury.

Federal expenditures for the Byrd Honors Scholarships Program totaled \$1.4 million for the one-year period ended September 30, 2009. In fiscal year 2008-09, the Department of Treasury awarded scholarships to 894 eligible students and distributed all of the funds to the institutions of higher education that the students attended.

The Department of Treasury's internal control did not ensure the accuracy of the performance report submitted for the reporting period ended September 30, 2009. As a result, the Department reported inaccurate information on the 2009 annual performance report.

Title 34, Part 654, Section 60 of the *Code of Federal Regulations** (CFR) requires the reporting of information deemed necessary by the federal awarding agency. The Department of Treasury is required to submit an annual performance report that highlights expenditures, number of students (full-time and part-time) receiving a scholarship award, and carry-over funds.

* See glossary at end of report for definition.

Our review of the 2009 annual performance report disclosed the following reporting errors:

Report Category	Reported Amount	Correct Amount	Difference
Carry-over funds from previous period	\$ 163,892	\$ 0	\$ 163,892
New grant funds awarded to recipients	1,178,263	1,360,500	(182,237)
Total grant funds awarded	\$ 1,342,155	\$ 1,360,500	\$ (18,345)
Number of full-time students receiving award	866	858	8
Number of part-time students receiving award	28	36	(8)
Proposed carry-over funds from this period	\$ 182,237	\$ 0	\$ 182,237

These reporting errors occurred because the Department of Treasury advanced payments at the end of each fiscal year and then deducted these payments when completing the federal report.

RECOMMENDATION

We recommend that the Department of Treasury improve its internal control over the Byrd Honors Scholarships Program to ensure compliance with federal laws and regulations regarding reporting.

FINDING (2711102MFA)

2. Credit Enhancement for Charter School Facilities, CFDA 84.354

U.S. Department of Education	CFDA 84.354: Credit Enhancement for Charter School Facilities
Award Number: U354A070002	Award Period: 07/13/2007 - 07/13/2032
	Known Questioned Costs: \$0

The Michigan Finance Authority's internal control over the Credit Enhancement for Charter School Facilities Program did not ensure compliance with federal laws and regulations regarding procurement and suspension and debarment. Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of the Credit Enhancement for Charter School Facilities Program awards.

Federal expenditures for the Credit Enhancement for Charter School Facilities Program totaled approximately \$3.5 million for the one-year period ended September 30, 2010.

Federal regulation 34 *CFR* 80.35 prohibits the Authority from contracting with or making subawards to any party that is suspended or debarred. The Authority did not have procedures to verify that charter schools were not suspended or debarred.

We reviewed the federal Excluded Parties List System and verified that the charter schools awarded grant funds for the Credit Enhancement for Charter School Facilities Program were not suspended or debarred during the fiscal year. As a result, we have not reported any questioned costs for this item.

RECOMMENDATION

We recommend that the Authority improve its internal control over the Credit Enhancement for Charter School Facilities Program to ensure compliance with federal laws and regulations regarding procurement and suspension and debarment.

The status of the findings related to federal awards that were reported in prior single audits is disclosed in the summary schedule of prior audit findings.

OTHER SCHEDULES

MICHIGAN FINANCE AUTHORITY
Summary Schedule of Prior Audit Findings
As of May 27, 2011

PRIOR AUDIT FINDINGS RELATED TO THE FINANCIAL STATEMENTS

Audit Findings That Have Been Fully Corrected:

Audit Period: October 1, 2008 through September 30, 2009

Finding Number: 1 (Michigan Higher Education Assistance Authority - 271-0272-10M)

Finding Title: Controls Over Financial Reporting

Finding: The Michigan Higher Education Assistance Authority did not have sufficient procedures to ensure that late financial transactions were included in the financial statements.

Agency Comments: The Michigan Finance Authority implemented additional procedures with the Department of Treasury related to the recording of late financial transactions. In addition, the Authority added a task to its internal fiscal year-end closing schedule to contact the Department of Treasury's Finance and Accounting Division to obtain verification of any late financial transactions to allow for adjustments in the Authority's draft financial statements.

Audit Period: October 1, 2007 through September 30, 2009

Finding Number: 2711001 (Michigan Public Educational Facilities Authority - 271-0275-10)

Finding Title: Internal Control Over Financial Transactions

Finding: The Michigan Public Educational Facilities Authority's internal control did not ensure that it recorded financial transactions in accordance with generally accepted accounting principles.

Agency Comments: The Michigan Finance Authority implemented internal control procedure changes to allow for additional oversight for individual transactions and review of interim financial statements to ensure that assets, liabilities, income, and expenses are properly classified.

Audit Period: October 1, 2006 through September 30, 2008

Finding Number: 2008/2007-1 (Michigan Higher Education Assistance Authority - Plante & Moran, PPLC)

Finding Title: Cut-Off Procedures For Claims Payable

Finding: During the audit, an error in the cut-off procedures for claims payable was noted.

Agency Comments: The Michigan Finance Authority enhanced its cut-off procedures to ensure that potential errors will be detected internally.

Audit Period: October 1, 2006 through September 30, 2008

Finding Number: 2008/2007-1 (Michigan Higher Education Student Loan Authority - Plante & Moran, PPLC)

Finding Title: Arbitrage Liability

Finding: An error in the calculation of the arbitrage liability was identified during the audit. An audit adjustment of \$1.5 million was required to decrease the arbitrage liability.

Agency Comments: The Michigan Finance Authority implemented a review procedure to ensure that potential errors will be detected internally.

PRIOR AUDIT FINDINGS RELATED TO FEDERAL AWARDS

Audit Findings That Have Been Fully Corrected:

- Audit Period:** October 1, 2007 through September 30, 2009
- Finding Number:** 2711002 (Michigan Public Educational Facilities Authority - 271-0275-10)
- Finding Title:** Credit Enhancement for Charter School Facilities, *CFDA* 84.354
- Finding:**
- a. The Michigan Public Educational Facilities Authority's internal control did not ensure that it limited the debt service reserve funds provided to charter schools to the maximum of \$500,000.
 - b. The Michigan Public Educational Facilities Authority's internal control did not ensure that program income was deposited into the Authority's reserve account and used for program purposes.
 - c. The Michigan Public Educational Facilities Authority's internal control did not ensure that the significant information it provided in the annual reports to the U.S. Department of Education was complete and accurate.
 - d. The Michigan Public Educational Facilities Authority's internal control did not ensure that it complied with Credit Enhancement for Charter School Facilities Program federal laws and regulations regarding special tests and provisions requirements for targeted charter schools, project time line, and investment types.
- Agency Comments:**
- a. The Michigan Finance Authority received approval from the U.S. Department of Education for the one charter school in fiscal year 2008-09 and the three charter schools in fiscal year 2009-10 that exceeded the \$500,000 debt service reserve fund limit. In the future, the Authority will adhere to its \$500,000 debt service reserve fund limitation.

- b. The Michigan Finance Authority received the \$2,800 in earnings from the six charter schools and has since developed a policy to ensure the timely collection of earnings from all charter schools.
- c. The Michigan Finance Authority has submitted a revised annual report to the U.S. Department of Education to correct past and current reporting errors, inconsistencies, and omissions. The Authority has also developed review procedures to ensure complete and accurate subsequent annual reports.
- d. The Michigan Finance Authority has taken corrective action regarding the use of low-risk investment securities and disclosure requirements. For targeted charter schools and performance agreement time lines, the Authority did not receive a sufficient number of charter school credit enhancement applications necessary to apply a selection methodology and, subsequently, all grant funds have now been committed.

Audit Period: October 1, 2006 through September 30, 2008

Finding Number: 2008/2007-2 (Michigan Higher Education Assistance Authority - Plante & Moran, PPLC)

Finding Title: Records Accuracy

Finding: Four loans from a sample of 27 were found to have a different status, last name, or loan servicer than indicated in the Michigan Higher Education Assistance Authority's records.

Agency Comments: The Michigan Finance Authority continues to work with its service provider to diligently monitor loan activity to ensure the accuracy of its records.

Audit Period: October 1, 2004 through September 30, 2006
Finding Number: 2006/2005-1 (Michigan Higher Education Assistance Authority - Plante & Moran, PPLC)

Finding Title: Change in Loan Status Notification

Finding: Federal Family Education Loans (FFEL): Lenders and servicers are not processing the paperwork to notify the Michigan Higher Education Assistance Authority of changes in loan status for all loans.

Agency Comments: The Michigan Finance Authority continues to work with its lenders and service provider to process paperwork in a timely manner and ensure the accuracy of loan statuses in its records.

Audit Period: October 1, 2006 through September 30, 2008
Finding Number: 2008/2007-2 (Michigan Higher Education Student Loan Authority - Plante & Moran, PPLC)

Finding Title: Compliance Report Finding Follow-Up

Finding: The Michigan Higher Education Student Loan Authority received the appropriate compliance reports from its servicers; however, 1 of the 6 reports that was received included several findings. The Authority did not perform timely follow-up related to these findings.

Agency Comments: The Michigan Finance Authority developed a new process to track all external reports, including servicer compliance reports, and identify issues requiring follow-up. This process is also used to document ongoing monitoring of issue status and when resolution occurred.

MICHIGAN FINANCE AUTHORITY

Corrective Action Plan

As of June 8, 2011

FINDINGS RELATED TO THE FINANCIAL STATEMENTS

The Office of the Auditor General has audited the financial statements of the Michigan Finance Authority for the fiscal year ended September 30, 2010 and has issued a separate report thereon dated February 3, 2011.

There were no findings related to the financial statements for fiscal year 2009-10.

FINDINGS RELATED TO FEDERAL AWARDS

Finding Number: 2711101MFA
Finding Title: Byrd Honors Scholarships, *CFDA* 84.185A

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

Planned Corrective Action: Necessary corrections have been made to the payment process that led to the errors on the report. The reporting for the next cycle will include carry-over funds.

Anticipated Completion Date: September 30, 2011

Responsible Individual: Anne Wohlfert, Director, Office of Scholarships and Grants

Finding Number: 2711102MFA
Finding Title: Credit Enhancement for Charter School Facilities, *CFDA* 84.354

Management Views: The Michigan Finance Authority disagrees with the audit finding.

The Michigan Finance Authority, by definition (as confirmed by the U.S. Department of Education), does not contract with or make subawards to charter schools. Further, for all bond transactions which Credit Enhancement for Charter School Facilities' funds were utilized, the Authority required the charter schools to represent and warrant that they met all applicable federal program requirements.

Planned Corrective Action: The Authority will continue to rely on representations from the charter schools. However, the language in the documents will be modified to specifically address the suspension and debarment question. The Authority will also review the federal Excluded Parties List System to verify that charter schools are not suspended or debarred.

Anticipated Completion Date: June 1, 2011

Responsible Individual: John Barton, Assistant Director, Authority Finance Division

GLOSSARY

Glossary of Acronyms and Terms

Authority	Michigan Finance Authority.
<i>Catalog of Federal Domestic Assistance (CFDA)</i>	The catalog that provides a full listing, with detailed program descriptions, of all federal programs available to state and local governments.
<i>Code of Federal Regulations (CFR)</i>	The codification of the general and permanent rules published by the departments and agencies of the federal government.
deficiency in internal control over federal program compliance	The design or operation of a control over compliance that does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis.
deficiency in internal control over financial reporting	The design or operation of a control that does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.
FFEL	Federal Family Education Loans.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules and/or financial statements of an audited entity are presented fairly in all material respects in conformity with the disclosed basis of accounting.
internal control	A process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

low-risk auditee	As provided for in OMB Circular A-133, an auditee that may qualify for reduced federal audit coverage if it receives an annual single audit and it meets other criteria related to prior audit results. In accordance with State statute, this single audit was conducted on a biennial basis; consequently, this auditee is not considered a low-risk auditee.
material misstatement	A misstatement in the financial schedules and/or financial statements that causes the schedules and/or statements to not present fairly the financial position or the changes in financial position or cash flows in conformity with the disclosed basis of accounting.
material noncompliance	Violations of laws, regulations, contracts, and grants that could have a direct and material effect on major federal programs or on financial schedule and/or financial statement amounts.
material weakness in internal control over federal program compliance	A deficiency, or a combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.
material weakness in internal control over financial reporting	A deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that material misstatement of the financial schedules and/or financial statements will not be prevented, or detected and corrected, on a timely basis.
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.

SEFA

schedule of expenditures of federal awards.

significant deficiency
in internal control over
federal program
compliance

A deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

significant deficiency
in internal control over
financial reporting

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.

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 that 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.

unqualified opinion

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

- a. The financial schedules and/or financial statements presenting the basic financial information of the audited agency are fairly presented in conformity with the disclosed basis of accounting; or

- b. The financial schedules and/or financial statements presenting supplemental financial information are fairly stated in relation to the basic financial schedules and/or financial statements. In issuing an "in relation to" opinion, the auditor has applied auditing procedures to the supplemental financial schedules and/or financial statements to the extent necessary to form an opinion on the basic financial schedules and/or financial statements, but did not apply auditing procedures to the extent that would be necessary to express an opinion on the supplemental financial schedules and/or financial statements taken by themselves; or

- c. The audited agency complied, in all material respects, with the cited requirements that are applicable to each major federal program.

USDOE

U.S. Department of Education.

U.S. Office of
Management and
Budget (OMB)

A cabinet-level office that assists the President in overseeing the preparation of the federal budget and in supervising its administration in executive branch agencies.

