

FINANCIAL AUDIT
OF THE
MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

April 1, 1999 through September 30, 1999

EXECUTIVE DIGEST

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

INTRODUCTION

This report contains the results of our financial audit* of the Michigan Economic Development Corporation (MEDC) for the period April 1, 1999 through September 30, 1999.

AUDIT PURPOSE

This financial audit was conducted as part of the constitutional responsibility of the Office of the Auditor General. Financial audits are conducted at various intervals to permit the Auditor General to express an opinion on the State's financial statements.

BACKGROUND

Article VII, Section 28 of the State Constitution and Act 7, P.A. 1967, provided for the creation of MEDC as a public body corporate. MEDC was created by a 10-year contract (interlocal agreement) between a participating local economic development corporation formed under Act 338, P.A. 1974, and the Michigan Strategic Fund (MSF). MEDC is a separate legal entity whose purpose is to stimulate, coordinate, and advance economic development in the State. Under the terms of the agreement, the governance of MEDC resides in an executive committee of 17 members appointed to eight-year, staggered terms by the Governor.

* See glossary at end of report for definition.

As of September 30, 1999, MEDC had 7 corporation employees and 228.5 full-time equated and 13 part-time employees who were detailed* from MSF.

AUDIT OBJECTIVES
AND CONCLUSIONS

Audit Objective: To assess and report on MEDC's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the financial statements, and on its internal control* over financial reporting, based on our audit of the financial statements.

Conclusion: Our assessment of compliance did not disclose any instances of noncompliance that could have a material effect on MEDC's financial statements. Also, our assessment of internal control over financial reporting did not disclose any material weaknesses*. However, our assessment disclosed a reportable condition* regarding MEDC accounting and financial reporting (Finding 1).

Audit Objective: To audit MEDC's financial statements as of and for the six months ended September 30, 1999.

Conclusion: We expressed an unqualified opinion* on MEDC's financial statements.

AUDIT SCOPE

Our audit scope was to examine the financial and other records of the Michigan Economic Development Corporation for the period April 1, 1999 through September 30, 1999. Our audit was conducted in accordance with generally accepted auditing standards and standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included

* See glossary at end of report for definition.

such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

ENTITY RESPONSES

Our audit report includes one finding and recommendation. MEDC's preliminary response indicates that it agrees with the finding and recommendation.

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June 19, 2000

Mr. Doug Rothwell, President and Chief Executive Officer
Michigan Economic Development Corporation
201 North Washington Square
Victor Center, 4th Floor
Lansing, Michigan

Dear Mr. Rothwell:

This is our report on the financial audit of the Michigan Economic Development Corporation for the period April 1, 1999 through September 30, 1999.

This report contains our executive digest; description of entity; audit objectives, audit scope, and entity responses; comments, finding, recommendation, and entity preliminary response; and independent auditor's reports on compliance and on internal control over financial reporting and on the financial statements. This report also contains the Michigan Economic Development Corporation financial statements and notes to the financial statements and a glossary of acronyms and terms.

The entity preliminary response was taken from the entity's response subsequent to our audit fieldwork.

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

AUDITOR GENERAL

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Description of Entity

Article VII, Section 28 of the State Constitution and Act 7, P.A. 1967, provided for the creation of the Michigan Economic Development Corporation (MEDC) as a public body corporate. MEDC was created as of April 5, 1999 by a 10-year contract (interlocal agreement) between a participating local economic development corporation formed under Act 338, P.A. 1974, and the Michigan Strategic Fund. MEDC is a separate legal entity whose purpose is to stimulate, coordinate, and advance economic development in the State. Under the terms of the agreement, the governance of MEDC resides in an executive committee of 17 members appointed to eight-year, staggered terms by the Governor.

As of September 30, 1999, MEDC had 7 corporation employees and 228.5 full-time equated and 13 part-time employees who were detailed from the Michigan Strategic Fund.

Audit Objectives, Audit Scope, and Entity Responses

Audit Objectives

Our financial audit of the Michigan Economic Development Corporation (MEDC) had the following objectives:

1. To assess and report on the MEDC's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the financial statements, and on its internal control over financial reporting, based on our audit of the financial statements.
2. To audit MEDC's financial statements as of and for the six months ended September 30, 1999.

Audit Scope

Our audit scope was to examine the financial and other records of the Michigan Economic Development Corporation for the period April 1, 1999 through September 30, 1999. Our audit was conducted in accordance with generally accepted auditing standards and standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

Entity Responses

Our audit report includes one finding and recommendation. MEDC's preliminary response indicates that it agrees with the finding and recommendation.

The entity preliminary response which follows the recommendation in our report was taken from the entity's written comments and oral discussion subsequent to our audit fieldwork.

COMMENTS, FINDING, RECOMMENDATION, AND ENTITY PRELIMINARY RESPONSE

COMPLIANCE AND INTERNAL CONTROL OVER FINANCIAL REPORTING

COMMENT

Audit Objective: To assess and report on the Michigan Economic Development Corporation's (MEDC's) compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the financial statements, and on its internal control over financial reporting, based on our audit of the financial statements.

Conclusion: Our assessment of compliance did not disclose any instances of noncompliance that could have a material effect on MEDC's financial statements. Also, our assessment of internal control over financial reporting did not disclose any material weaknesses. However, our assessment disclosed a reportable condition regarding MEDC accounting and financial reporting.

FINDING

1. MEDC Accounting and Financial Reporting

MEDC, in conjunction with the Department of Management and Budget (DMB), did not record certain financial transactions properly and in a timely manner. This contributed to inefficiencies and errors that required adjustments in the preparation of the financial statements.

Section 18.1492 of the *Michigan Compiled Laws* requires each entity that falls within the reporting responsibility of the State to submit financial statements for inclusion in the *State of Michigan Comprehensive Annual Financial Report* not later than 90 days following the close of the State's fiscal year (by December 31). Also, Section 18.1494 of the *Michigan Compiled Laws* requires that the statements be prepared in accordance with generally accepted accounting principles.

Executive Order 1999-1 transferred various programs of the Michigan Jobs Commission from the General Fund to the Michigan Strategic Fund (MSF) effective April 5, 1999. This Order also authorized MSF to enter into an interlocal agreement with one or more local public agencies. MSF entered into such an agreement with the Wayne County Economic Development Corporation to form MEDC. MSF then transferred all but one of the General Fund programs and most of its net assets to MEDC. In addition, the Order provided for DMB to record the financial transactions of MSF and MEDC in the State's financial management system in the most efficient manner possible for the remainder of the fiscal year.

DMB and MEDC originally decided not to separate the accounting among the General Fund, MSF, and MEDC until the beginning of the new fiscal year. MSF and MEDC continued to process accounting transactions for the programs previously administered by the Michigan Jobs Commission in the State's General Fund through the end of the fiscal year, even though the responsibilities for the programs had transferred six months earlier. In December 1999, DMB, MSF, and MEDC made the decision to record the transfer of the Michigan Jobs Commission programs' costs and unspent authorization from the General Fund to MSF and then to MEDC and to include MEDC as a component unit in the *State of Michigan Comprehensive Annual Financial Report* in accordance with generally accepted accounting principles. During the first week of January 2000, DMB approved the processing of entries necessary to record the transfers between the General Fund, MSF, and MEDC.

Because of the delays in determining the proper accounting and reporting treatment related to the Executive Order, MEDC and DMB did not have sufficient time to review and verify the propriety of the related accounting transactions needed to properly report the reorganizations and transfers. We noted several errors and additional adjustments relating to transfers, receivables, payables, revenues, and expenditures, which were subsequently corrected. These adjusting entries and delays resulted in MEDC not providing DMB with draft financial statements by December 31, in accordance with Section 18.1492 of the *Michigan Compiled Laws*. DMB received the financial statement drafts the first week of February 2000.

RECOMMENDATION

We recommend that MEDC, in conjunction with DMB, record financial transactions properly and in a timely manner.

ENTITY PRELIMINARY RESPONSE

MEDC informed us that it has resolved the issues noted in the finding and that it will take steps to prevent a recurrence.

FINANCIAL ACCOUNTING AND REPORTING

COMMENT

Audit Objective: To audit MEDC's financial statements as of and for the six months ended September 30, 1999.

Conclusion: We expressed an unqualified opinion on MEDC's financial statements.

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

February 18, 2000

Mr. Doug Rothwell, President and Chief Executive Officer
Michigan Economic Development Corporation
201 North Washington Square
Victor Center, 4th Floor
Lansing, Michigan

Dear Mr. Rothwell:

We have audited the financial statements of the Michigan Economic Development Corporation as of and for the six-month period ended September 30, 1999 and have issued our report thereon dated February 18, 2000. We conducted our audit in accordance with generally accepted auditing standards 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 Michigan Economic Development Corporation's financial statements 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 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 that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Michigan Economic Development Corporation'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 assurance on the internal control over financial reporting. However, we noted a matter involving the 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 the internal control over financial reporting that, in our judgment, could adversely affect the Michigan Economic Development Corporation's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in Finding 1.

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 misstatements 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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are considered to be material weaknesses. However, we believe that the reportable condition described in the previous paragraph is not a material weakness.

This report is intended solely for the information and use of the Michigan Economic Development Corporation'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

Independent Auditor's Report on
the Financial Statements

February 18, 2000

Mr. Doug Rothwell, President and Chief Executive Officer
Michigan Economic Development Corporation
201 North Washington Square
Victor Center, 4th Floor
Lansing, Michigan

Dear Mr. Rothwell:

We have audited the accompanying balance sheet of the Michigan Economic Development Corporation as of September 30, 1999 and the related statement of revenues, expenses, and retained earnings and statement of cash flows for the six-month period then ended. These financial statements are the responsibility of the Michigan Economic Development Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards 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 discussed in Note 1b, the accompanying financial statements present only the Michigan Economic Development Corporation and are not intended to present fairly the financial position and results of operations and cash flows of the State of Michigan or its component unit proprietary funds.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Michigan Economic Development Corporation as of September 30, 1999 and the results of its operations and cash flows for the six months then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated February 18, 2000 on our consideration of the Michigan Economic Development Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants.

AUDITOR GENERAL

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

Balance Sheet

As of September 30, 1999

ASSETS

Current Assets:

Cash		\$ 247,234
Capital Access Program checking		1,752,012
Capital Access Program checking - reserve		13,710,561
Time deposits		95,943,991
Gaming revenue receivable		7,882,631
Amounts due from Michigan Strategic Fund		71,474,465
Investments (Note 2)		27,256,393
Other current assets:		
Mortgages and loans receivable (Note 4)	\$ 190,123	
Interest receivable	1,263,634	
Miscellaneous	<u>16,630</u>	
Total Other Current Assets		<u>1,470,387</u>
Total Current Assets		<u>\$ 219,737,676</u>

Investments (Note 2)	34,481,111
Mortgages and loans receivable (Note 4)	<u>14,882,974</u>
Total Assets	<u><u>\$ 269,101,761</u></u>

LIABILITIES AND FUND EQUITY

Current Liabilities:

Accounts payable and other liabilities	<u>\$ 19,049,445</u>
Total Current Liabilities	<u>\$ 19,049,445</u>

Long-Term Liabilities:

Capital Access Program	\$ 13,724,045
Compensated Absences (Note 1)	<u>1,549,023</u>
Total Other Long-Term Liabilities	<u>\$ 15,273,068</u>
Total Liabilities	<u>\$ 34,322,513</u>

Fund Equity:

Contributed Capital:	
From Michigan Strategic Fund (Note 3)	<u>\$ 162,713,480</u>
Total Contributed Capital	\$ 162,713,480
Unreserved Retained Earnings	<u>72,065,768</u>
Total Fund Equity	<u>\$ 234,779,249</u>

Total Liabilities and Fund Equity	<u><u>\$ 269,101,761</u></u>
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The accompanying notes are an integral part of the financial statements.

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Revenues, Expenses, and Retained Earnings
For the Six-Month Period Ended September 30, 1999

OPERATING REVENUES		
Investment earnings	\$ 3,223,205	
Net increase (decrease) in fair value of investments	3,948,130	
Interest income on loans (Note 5)	341,547	
Interest income	100,532	
Miscellaneous	124,257	
Total Operating Revenues		\$ 7,737,670
OPERATING AND OTHER EXPENSES		
Salaries, wages, and other administrative (Note 1)	\$20,416,696	
Compensated absences (Note 1)	1,549,023	
Total Operating and Other Expenses		21,965,720
Operating Income (Loss)		\$ (14,228,049)
NONOPERATING REVENUES (EXPENSES)		
Federal revenue - NIST	\$ 617,554	
NIST pass-through	(617,554)	
Economic Development Job Training Grants	(22,545,560)	
Detroit Downtown Development Authority	(1,428,519)	
Center for Virtual Learning	(3,570,458)	
Center for Michigan's Renaissance	(2,788,615)	
Research Center Grants	(1,842,780)	
Governor's Career Scholarship Program	(1,125,924)	
Center for Career Training	(3,348,381)	
Marketing and miscellaneous	(3,039,418)	
Capital Access Program	(705,043)	
BIDCO principal credits	(90,802)	
Renaissance Zones	(34,990)	
Total Nonoperating Revenue (Expenses)		(40,520,488)
Income (Loss) Before Operating Transfers		\$ (54,748,537)
OPERATING TRANSFERS		
From Michigan Strategic Fund:		
Gaming revenue (Note 3)	\$25,443,583	
Administrative funds (Note 3)	101,370,722	
Total Operating Transfers In (Out)		126,814,305
Net Income (Loss)		\$ 72,065,768
Retained Earnings - Beginning		0
Retained Earnings - Ending		\$ 72,065,768

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

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Cash Flows
For the Six-Month Period Ended September 30, 1999

CASH FLOWS FROM OPERATING ACTIVITIES	
Operating income (loss)	\$ (14,228,049)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:	
Interest (nonprogram) and investment income	(7,613,414)
Changes in assets and liabilities:	
Amounts due from component unit (MSF)	(79,357,096)
Mortgages and loans receivable (program loans)	(15,073,097)
Other assets	(1,280,264)
Accounts payable and other liabilities	34,322,513
Net cash provided (used) by operating activities	<u>\$ (83,229,407)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Grants received from federal government	\$ 617,600
Nonoperating grants	(41,138,089)
Operating transfers from component unit (MSF)	126,814,305
Equity transfers from component unit (MSF)	162,713,480
Net cash provided (used) by noncapital financing activities	<u>\$ 249,007,296</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Acquisition and construction of capital assets	\$ 0
Net cash provided (used) by capital and related financing activities	<u>\$ 0</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of investment securities	\$ (61,737,504)
Interest and dividends on investments	7,613,414
Net cash provided (used) by investing activities	<u>\$ (54,124,091)</u>
Net cash provided (used) - all activities	\$ 111,653,798
Cash and cash equivalents at beginning of year	
Cash and cash equivalents at end of year	<u><u>\$ 111,653,798</u></u>
RECONCILIATION OF CASH AND CASH EQUIVALENTS	
Per balance sheet classifications:	
Cash	\$ 111,653,798
Equity in Common Cash	
Cash and cash equivalents at end of year	<u><u>\$ 111,653,798</u></u>
SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES	<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

The accounting policies of the Michigan Economic Development Corporation (MEDC) conform to generally accepted accounting principles as applicable to governmental units. The following is a summary of the more significant policies:

a. Reporting Entity

Article VII, Section 28 of the State Constitution and Act 7, P.A. 1967, provided for the creation of MEDC as a public body corporate. MEDC was created by a 10-year contract (interlocal agreement) between a participating local economic development corporation formed under Act 338, P.A. 1974, as amended, and the Michigan Strategic Fund (MSF). MEDC is a separate legal entity whose purpose is to stimulate, coordinate, and advance economic development in the State. Under the terms of the agreement, the governance of MEDC resides in an executive committee of 17 members appointed to eight-year, staggered terms by the Governor.

MEDC is considered to be a component unit of the financial reporting entity of the State of Michigan. The decision to include a potential component unit in the reporting entity is made by applying the criteria set forth in the Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*. The basic criteria include the appointment of a voting majority of the governing board of MEDC; the legal separation of the State and MEDC; the fiscal independence of MEDC; whether exclusion of the unit would make the *State of Michigan Comprehensive Annual Financial Report* misleading; and whether there is a potential for MEDC to provide specific financial benefits to, or impose specific financial burdens on, the State.

b. Basis of Presentation

- (1) Fund Accounting: The accounts of the component units of the State of Michigan are organized on the basis of funds, each of which is considered a separate accounting entity. MEDC's operations are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenses. Government resources are allocated to and accounted for in separate funds, based upon the purposes for which they are to be spent and the means by which spending activities are controlled.
- (2) Proprietary Funds: MEDC is an enterprise fund. Proprietary funds are accounted for on a flow of economic resources measurement focus. The accounting objectives are a determination of net income, financial position, and cash flow. All assets and liabilities associated with proprietary fund activities are included on the balance sheet.

Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises, i.e., where the intent of the governing body is that the costs (expenses) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

The accompanying financial statements present only the Michigan Economic Development Corporation and are not intended to present fairly the financial position and results of operations and cash flows of the State of Michigan or its component unit propriety funds.

c. Basis of Accounting

Proprietary fund types use the accrual basis of accounting. The accrual basis emphasizes the measurement of "net income," (i.e., "capital maintenance" focus). Using this basis, revenues are recognized when

"earned" and expenses are recognized when "incurred." All financial resources and obligations of a fund, whether current or noncurrent, are recorded in the fund.

d. Financial Data

The MSF Board of Directors entered into an interlocal agreement with a local unit of government to create MEDC. MEDC came into existence on April 5, 1999. In accordance with the terms of the agreement, substantial assets, liabilities, and final balances of MSF were transferred to MEDC on May 1, 1999. All revenues received from tribal casino gaming, industrial development revenue bond issuance fees, and other sources since May 1, 1999 are transferred to MEDC on a monthly basis. This interlocal agreement also detailed all State classified employees from MSF to MEDC.

State appropriations available to MSF for this purpose are also made available to MEDC, as needed. MEDC statements include transactions recorded using all appropriated funds, except the Community Development Block Grant (CDBG) Program transactions. The CDBG Program transactions are recorded in MSF as required by the federal granting agency.

MEDC financial statements primarily represent the following:

- (1) Operating Revenues: Amounts received from investment earnings.
- (2) Operating Expenses: Administrative expenses (including payables) incurred out of appropriated funds, except for the CDBG Program, for the period April 1, 1999 through September 30, 1999.
- (3) Nonoperating Revenues (Expenses): Program grants for the period May 1, 1999 through September 30, 1999.
- (4) Operating Transfers: Amounts available to MEDC from State appropriations and recorded in items (2) and (3). Also included are tribal casino gaming revenues collected by MSF and transferred to MEDC during May 1, 1999 through September 30, 1999.

e. Investments

Equity investments in business and industrial development corporations (BIDCOs) are carried at the lower of aggregate cost or fair value. MEDC has determined that cost will be used to approximate fair value.

Other investments are carried at fair value.

f. Compensated Absences

Compensated absences are accrued when incurred in proprietary funds (using the accrual basis of accounting). At September 30, 1999, the accumulated liability for MEDC's State classified employees was estimated to be \$1,549,023.

g. Comparative Data

Since this is the first year of MEDC operation, no comparative totals for the prior year have been presented in the accompanying financial statements.

Note 2 Deposits and Investments

a. General Information

MEDC's investment policy allows investments in the following investment types:

- (1) Securities issued or guaranteed by the U.S. government or its agencies.
- (2) Bonds or other obligations of any U.S. state or any local unit of government of any such state.
- (3) Preferred stock issued by U.S. corporations.
- (4) Repurchase agreements fully collateralized by U.S. government securities.

- (5) Corporate and bank debt including, but not limited to, commercial paper, certificates of deposit, banker's acceptances, and other short-term obligations.
- (6) Corporate notes and bonds.
- (7) Taxable bond funds.
- (8) Money market mutual fund shares that offer daily purchase and redemption and maintain a constant share price.
- (9) Common stock of U.S. corporations.
- (10) Stock mutual funds with portfolios highly concentrated in securities of U.S. corporations.

b. Deposits

GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, requires certain disclosures regarding policies and practices with respect to deposits and investments and the custodial credit risk associated with them.

In accordance with GASB Statement No. 3, deposits are classified into three categories of credit risk as follows:

Category 1: Insured or collateralized with securities held by the entity or by its agent in the entity's name.

Category 2: Collateralized with securities held by the pledging financial institution's trust department or agent in the entity's name.

Category 3: Uncollateralized, including bank balances that are collateralized with securities held by the pledging

financial institution or by its trust department or agent, but not in the entity's name.

MEDC's deposits and investments at September 30, 1999 were:

	<u>Deposits</u>	<u>Investments</u>
Current Deposits and Investments:		
Checking	\$ 247,234	\$
Capital Access Program checking	1,752,012	
Capital Access Program checking - reserve	13,710,561	
Time deposits	95,943,991	
Marketable securities		16,884,265
Venture capital		10,364,512
Total Current Deposits and Investments	<u>\$111,653,798</u>	<u>\$27,248,777</u>
Long-Term Marketable Securities		34,481,111
Total Deposits and Investments	<u><u>\$111,653,798</u></u>	<u><u>\$61,729,888</u></u>

Deposits included in MEDC's bank accounts (without recognition of outstanding checks or deposits in transit) were \$15,709,807 at September 30, 1999. Of that amount, \$3,386,082 was covered by federal depository insurance and was classified in GASB credit risk category 1. The remaining \$12,323,725 was uninsured and uncollateralized at September 30, 1999, and was classified in GASB credit risk category 3.

c. Investments

In accordance with GASB Statement No. 3, investments are also classified into three categories of credit risk as follows:

Category 1: Investments that are insured or registered or for which the securities are held by the entity or its agent in the entity's name.

Category 2: Uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the entity's name.

Category 3: Uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent not in the entity's name.

The following table shows the fair value of investments at September 30, 1999 by investment type and in total and does not include the checking account balances:

Investment Type	GASB Risk Category			Not Categorized	Fair Value
	1	2	3		
Corporate securities	\$	\$	\$124,576,505	\$	\$124,576,505
Government securities			14,871,102		14,871,102
Equity	6,491,788				6,491,788
Equity mutual funds				1,377,588	1,377,588
Other nonmarketable investments				10,364,512	10,364,512
Total Investments	\$6,491,788	\$ 0	\$139,447,607	\$11,742,100	\$157,681,495

Note 3 Transfers

The following items represent equity and operating transfers:

Equity transfer (net assets) from MSF	\$162,713,480
Operating Transfers:	
Gaming revenue (May 1, 1999 through September 30, 1999)	\$ 25,443,583
Administrative	
Expenditures	\$ 29,575,654
Accounts payable	12,623,878
Encumbrances	28,400,704
Technical center grants	30,000,000
Miscellaneous	<u>770,487</u>
Subtotal of Administrative Operating Transfers	\$101,370,722

Note 4 Loans Receivable

Loans receivable consisted of the following at September 30, 1999:

Seed capital loans	\$ 7,800,000
BIDCO	10,948,523
Other loans	25,301,853
Total	<u>\$ 44,050,376</u>
Less: Allowance for uncollectible loans	(28,977,279)
Total Loans Receivable	<u><u>\$ 15,073,097</u></u>

Loans issued by the Michigan Economic Development Authority, a predecessor entity to MEDC, are included in the "Other loans" category. The loans are collateralized, for qualifying projects, on the basis of participating up to 50% with other public or private lenders. The loans are due under varying repayment terms, including interest at predominantly 9.5% per annum.

Inducement loans are collateralized loans bearing interest at predominantly 5% per annum with varying repayment terms.

Seed capital loans are uncollateralized, 10-year term loans (which can be extended) bearing interest at 9% per annum with a balloon payback required at the end of the loan period.

BIDCO and other loans are collateralized loans bearing varying rates of interest and repayment terms.

The current portion of loans receivable includes those payments expected to be received during the next fiscal year.

MEDC provided no additional allowance during the fiscal year ended September 30, 1999 for loans receivable that MEDC expected to be converted to grants or uncollectible. The loans generally provide for no principal or interest payments during the term of the loans. These loans are expected to be converted to grants at the end of their term provided that certain conditions are met by the borrowers. The conditions generally require the borrowers to

continue to conduct their principal business activities in the State of Michigan and submit specified reports to MEDC.

Note 5 Bond Programs

All bond programs are handled by MSF. Income generated from bond issuance fees is transferred to MEDC on a monthly basis.

A portion of the fund equity is committed for the following economic development projects:

Access Technology	\$ 900,000
Capital Access Fund	2,315,138
Center for Career Training	31,301,342
Center for Michigan's Renaissance	12,534,197
Center for Virtual Learning	22,818,511
Detroit Downtown Development Authority	18,187,077
Enterprise Development Fund	1,572,815
Minority Investments	3,490,956
Research	713,608
Total	<u><u>\$93,833,646</u></u>

Note 6 Major Revenue Sources

The MSF revenue transferred to MEDC primarily consists of:

- a. Gaming revenue from the class III electronic games of several casinos operated by Native American tribes located in Michigan.
- b. State appropriations for support staff and economic development activities.

Glossary of Acronyms and Terms

BIDCO	business and industrial development corporation.
CDBG	Community Development Block Grant.
detailed employees	The temporary assignment of employees from a governmental entity to another business entity. Employees in this capacity continue to receive the same compensation and benefits of the original employer, but receive day-to-day direction (work assignments and supervision) from the entity they are detailed to.
DMB	Department of Management and Budget.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial statements of an audited entity are fairly presented in conformity with generally accepted accounting principles.
GASB	Governmental Accounting Standards Board.
internal control	A process, effected by an entity's management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories: (a) reliability of financial reporting, (b) effectiveness and efficiency of operations, and (c) compliance with applicable laws and regulations.
material weakness	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 misstatements 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.

MEDC Michigan Economic Development Corporation.

MSF Michigan Strategic Fund.

NIST National Institute of Standards and Technology.

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 Michigan Economic Development Corporation's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

unqualified opinion An auditor's opinion in which the auditor states, without reservation, that the financial statements are fairly presented in conformity with generally accepted accounting principles.