

Office of the Auditor General
Financial Audit Report

Transition in the Office of State Treasurer
Department of Treasury

As of April 18, 2015

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



OAG

Office of the Auditor General

Report Summary

Financial Audit
Transition in the Office of State Treasurer
Department of Treasury
As of April 18, 2015

Report Number:
271-0256-15

Released:
February 2016

A financial audit determines if the financial schedules are fairly presented. This financial audit of the Transition in the Office of State Treasurer was required by Section 12.10 of the *Michigan Compiled Laws*.

Auditor's Report Issued

UNMODIFIED OPINION

MODIFIED OPINION

We issued an unmodified opinion on the schedule of cash and investments in the possession or under the control of the State Treasurer and collateral pledged to the State Treasurer to reflect that it was fairly presented, in all material respects, in accordance with accounting principles generally accepted in the United States of America.

Background

Section 12.10 of the *Michigan Compiled Laws* requires the Auditor General to perform an audit of cash and investments in the possession or under the control of the State Treasurer upon a vacancy in the Office of State Treasurer. R. Kevin Clinton vacated the Office of State Treasurer as of April 18, 2015, and Nick A. Khouri was appointed State Treasurer as of April 19, 2015.

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

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

Doug A. Ringler, CPA, CIA
Auditor General

Laura J. Hirst, CPA
Deputy Auditor General



OAG

Office of the Auditor General

201 N. Washington Square, Sixth Floor • Lansing, Michigan 48913 • Phone: (517) 334-8050 • www.audgen.michigan.gov

Doug A. Ringler, CPA, CIA
Auditor General

February 23, 2016

Mr. Nick A. Khouri
State Treasurer
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Khouri:

I am pleased to provide this financial audit report on the Transition in the Office of State Treasurer, Department of Treasury, as of April 18, 2015. This audit is required by Section 12.10 of the *Michigan Compiled Laws*.

This report contains our report summary, our independent auditor's report on the financial schedule, the schedule of cash and investments in the possession or under the control of the State Treasurer and collateral pledged to the State Treasurer as of April 18, 2015, and a glossary of abbreviations and terms.

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

Sincerely,

A handwritten signature in black ink that reads 'Doug Ringler'. The signature is written in a cursive style with a large, prominent 'D'.

Doug Ringler
Auditor General

TABLE OF CONTENTS

TRANSITION IN THE OFFICE OF STATE TREASURER

	<u>Page</u>
Report Summary	1
Report Letter	3
Independent Auditor's Report on the Financial Schedule	8
Transition in the Office of State Treasurer Financial Schedule	
Schedule of Cash and Investments in the Possession or Under the Control of the State Treasurer and Collateral Pledged to the State Treasurer as of April 18, 2015	10
Note to the Financial Schedule	11
Glossary of Abbreviations and Terms	14

INDEPENDENT AUDITOR'S REPORT AND FINANCIAL SCHEDULE



OAG

Office of the Auditor General

201 N. Washington Square, Sixth Floor • Lansing, Michigan 48913 • Phone: (517) 334-8050 • www.audgen.michigan.gov

Doug A. Ringler, CPA, CIA
Auditor General

Independent Auditor's Report on the Financial Schedule

Mr. Nick A. Khouri
State Treasurer
Richard H. Austin Building
Lansing, Michigan

Dear Mr. Khouri:

Report on the Financial Schedule

We have audited the accompanying schedule of cash and investments in the possession or under the control of the State Treasurer and collateral pledged to the State Treasurer as of April 18, 2015 and the related note to the financial schedule.

Management's Responsibility for the Financial Schedule

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

Auditor's Responsibility

Our responsibility is to express an opinion on this financial schedule based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedule is free from material misstatement.

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

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

Opinion

In our opinion, the financial schedule referred to in the first paragraph presents fairly, in all material respects, the cash and investments in the possession or under the control of the State Treasurer and collateral pledged to the State Treasurer as of April 18, 2015 in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the accompanying schedule of cash and investments in the possession or under the control of the State Treasurer and collateral pledged to the State Treasurer was prepared solely for the purpose of complying with Section 12.10 of the *Michigan Compiled Laws*, which requires an audit of cash and investments in the possession or under the control of the State Treasurer upon a vacancy in the Office of State Treasurer. Accordingly, this schedule does not purport to, and does not, constitute a complete financial presentation of the State of Michigan, the Department of Treasury, or any individual fund of the State of Michigan. Our opinion is not modified with respect to this matter.

Sincerely,

A handwritten signature in black ink that reads "Doug Ringler". The signature is written in a cursive, flowing style.

Doug Ringler
Auditor General
February 8, 2016

TRANSITION IN THE OFFICE OF STATE TREASURER
Schedule of Cash and Investments in the Possession or Under the Control
of the State Treasurer and Collateral Pledged to the State Treasurer
As of April 18, 2015

<u>State Treasurer's Common Cash</u>	
Demand deposits	\$ 1,721,181,314
Prime commercial paper	2,019,478,152
Emergency loans	122,191,101
Total cash and equities	<u>\$ 3,862,850,567</u>
Outstanding warrants	(755,921,613)
Total State Treasurer's common cash available	<u>\$ 3,106,928,954</u>
<u>Other Cash and Cash Equivalents</u>	
Mackinac Bridge Authority	\$ 2,154,194
Michigan Education Trust	110,394,152
Unclaimed Property Division	
Total other cash and cash equivalents	<u>\$ 112,548,346</u>
<u>Specific Funds' Investments</u>	
Game and Fish Lifetime License Trust Fund	\$ 1,296,732
Michigan Veterans' Trust Fund	49,492,754
Game and Fish Protection Trust Fund	203,326,874
Michigan Natural Resources Trust Fund	615,618,842
Michigan State Parks Endowment Fund	196,675,971
Children's Trust Fund	20,016,549
Michigan Nongame Fish and Wildlife Fund	5,259,857
State Lottery Fund	229,362,079
Michigan Education Trust Plans B and C	104,757,692
Michigan Education Trust Plan D	773,176,335
Mackinac Bridge Authority	68,136,265
Legislative Retirement Fund	176,706,371
State Police Pension Benefits Fund	1,275,948,141
State Police OPEB Fund	86,410,128
State Employees' Pension Benefits Fund	11,105,652,376
State Employees' OPEB Fund	1,219,125,960
Public School Employees' Pension Benefits Fund	44,505,922,263
Public School Employees' OPEB Fund	3,877,698,702
Judges' Pension Benefits Fund	270,679,369
Judges' OPEB Fund	802,575
Gifts, Bequests, and Deposits Investment Fund	12,077
Children With Special Needs Fund	20,058,984
Escheats Fund	6,948,580
Total specific funds' investments	<u>\$ 64,813,085,476</u>
Total cash and investments in the possession or under the control of the State Treasurer	<u>\$ 68,032,562,776</u>
<u>Collateral Pledged to the State Treasurer</u>	
For insurance companies	\$ 418,552,000
For State deposits	2,470,368,000
For Michigan Education Trust	5,000,000
For Michigan Department of Health and Human Services	88,500,000
Total collateral pledged to the State Treasurer	<u>\$ 2,982,420,000</u>

The accompanying note is an integral part of the financial schedule.

NOTE TO THE FINANCIAL SCHEDULE

Note 1

Significant Accounting Policies

a. Reporting Entity

This report was prepared solely for the purpose of complying with Section 12.10 of the *Michigan Compiled Laws*, which requires an audit of cash and investments in the possession or under the control of the State Treasurer upon a vacancy in the Office of State Treasurer. R. Kevin Clinton vacated the Office of State Treasurer as of April 18, 2015, and Nick A. Khouri was appointed State Treasurer as of April 19, 2015.

For financial reporting purposes, this report includes cash and investment balances under the control of the State Treasurer of various funds and component units that are included within the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)* reporting entity.

b. Basis of Accounting and Financial Schedule Presentation

The schedule of cash and investments in the possession or under the control of the State Treasurer and collateral pledged to the State Treasurer reports the cash and investments in the possession or under the control of the State Treasurer and the collateral pledged to the State Treasurer as of April 18, 2015. This report is a special purpose financial presentation prepared to comply with Section 12.10 of the *Michigan Compiled Laws* and does not constitute a complete presentation of assets, liabilities, revenues, and expenses but is otherwise prepared in conformity with accounting principles generally accepted in the United States of America. Accordingly, this schedule does not purport to, and does not, constitute a complete financial presentation of the State of Michigan, the Department of Treasury, or any individual fund of the State of Michigan.

Cash and investments on the schedule are accounted for using accounting rules promulgated by the Governmental Accounting Standards Board.

c. Description of Cash, Investments, and Pledged Collateral

State Treasurer's Common Cash: The State Treasurer, under the authority provided by State statute, manages the State's common cash. The pooling of cash allows the State Treasurer to invest money not needed to pay immediate obligations so that investment earnings on available cash are maximized. Pool investments are not segregated by fund; rather, each contributing fund's balance is treated as equity in the common cash.

Outstanding warrants represent those State warrants issued and outstanding at April 18, 2015. For the purposes of this schedule, these warrants are deducted from the State Treasurer's common cash pool because they represent an obligation of the pool and the amount is not considered available to meet future obligations.

Other Cash and Cash Equivalents: The State Treasurer has various responsibilities that result in the possession or control of cash and cash equivalents. These responsibilities consist of:

- (1) Serving as the treasurer for the Mackinac Bridge Authority.
- (2) Performing fiscal agent services for the Michigan Education Trust.
- (3) Serving as administrator for unclaimed property escheated to the Unclaimed Property Division.

Specific Funds' Investments: Specific funds' investments include both short-term and long-term investments. The State Treasurer, under the authority provided by State statutes, manages most investments for the State of Michigan, which consist of stocks, corporate and government bonds and notes, mortgages, real estate, venture capital, mutual funds, and other investments. In July 2004, the investments of the State retirement funds for public school employees, State employees, State police, and judges were consolidated to an investment pool structure. These retirement funds' investments represent a pro-rata share based on ownership of the investment pools.

Collateral Pledged to the State Treasurer: The State Treasurer manages collateral pledged for the following purposes:

- (1) Collateral pledged by insurance companies as a condition of conducting business in the State.
- (2) Collateral pledged by banks to secure deposits of State money.
- (3) Collateral pledged by banks to secure demand deposits of the Michigan Education Trust.
- (4) Collateral pledged by a bank to secure the Michigan Department of Health and Human Services' child support collections.

d. Valuation of Investments and Collateral Pledged to the State Treasurer

The State's common cash pool investments include prime commercial paper, reported at amortized cost, and special loan programs, reported using cost-based measures.

Long-term investments are reported at fair value and short-term investments are reported at amortized cost except for the State retirement funds using the investment pool structure, which are reported at the fair value of the various investment pools. The fair value of the investment pools is calculated using the value of the securities and other assets within the pools, which includes appreciation of asset values, accrued income, and amounts owed or due from the sale of securities as of the close of business on April 18, 2015.

The fair value of investments traded on a national or an international exchange is calculated using quoted market prices. Investments not traded on a national or an international exchange are valued based on either equivalent values of comparable investments with similar yield or risk or at an estimated fair value.

Collateral pledged to the State Treasurer is reported at par value (the face value of the bonds). On April 18, 2015, collateral pledged by insurance companies included cash in the amount of \$350,000, which was also included in demand deposits of the State Treasurer's common cash.

GLOSSARY OF ABBREVIATIONS AND TERMS

financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules of an audited entity are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.
generally accepted accounting principles (GAAP)	A technical accounting term that encompasses the conventions, rules, guidelines, and procedures necessary to define accepted accounting practice at a particular time; also cited as "accounting principles generally accepted in the United States of America."
Governmental Accounting Standards Board (GASB)	An arm of the Financial Accounting Foundation established to promulgate standards of financial accounting and reporting with respect to activities and transactions of state and local governmental entities.
modified opinion	A qualified opinion, an adverse opinion, or a disclaimer of opinion.
OPEB	Other Postemployment Benefits.
unmodified opinion	The opinion expressed by the auditor when the auditor, having obtained sufficient appropriate audit evidence, concludes that the financial schedules are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.

