MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT

FINANCIAL AUDIT
OF THE

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

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

Fiscal Years Ended September 30, 2012 and September 30, 2011

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

271-0406-13

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

Michigan

Office of the Auditor General

REPORT SUMMARY

Financial Audit

Michigan Economic Development Corporation
(A Discretely Presented Component Unit of the State of Michigan)

Fiscal Years Ended September 30, 2012 and September 30, 2011

Report Number:
271-0406-13

Released:
February 2013

A financial audit determines if the financial statements are fairly presented; considers internal control over financial reporting; and determines compliance with requirements material to the financial statements. This financial audit of the Michigan Economic Development Corporation (MEDC) was conducted as part of the constitutional responsibility of the Office of the Auditor General.

Financial Statements:

Auditor's Report Issued

We issued an unqualified opinion on MEDC's basic financial statements.

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Internal Control Over Financial Reporting

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

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Noncompliance and Other Matters Material to the Financial Statements

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

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Background:

Article VII, Section 28 of the Michigan Constitution and Act 7, P.A. 1967, provided for the creation of MEDC as a public body corporate. MEDC was created in April 1999 by a 10-year contract (interlocal agreement, as amended) between a participating local economic development corporation formed under Act 338, P.A. 1974, as amended, and the Michigan Strategic Fund (MSF). Article VI of the interlocal agreement provides for the automatic renewal of this initial 10-year term for two renewal periods of five years each. In April 2009, this interlocal agreement was automatically renewed for another five years. MEDC is a separate legal entity created to promote smart economic growth by developing strategies and providing services to create and retain good jobs and a high quality of life for Michigan residents. Under the terms of the agreement, the governance of MEDC resides in an Executive Committee of 20 members appointed to eight-year, staggered terms by the Governor.

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

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

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

Scott M. Strong, C.P.A., C.I.A.
Deputy Auditor General

STATE OF MICHIGAN
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

February 5, 2013

Mr. Michael A. Finney, President and Chief Executive Officer
and
Mr. Doug Rothwell, Executive Committee Chair
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Finney and Mr. Rothwell:

This is our report on the financial audit of the Michigan Economic Development Corporation (MEDC), a discretely presented component unit of the State of Michigan, for the fiscal years ended September 30, 2012 and September 30, 2011.

This report contains our report summary, our independent auditor's report on the financial statements, the MEDC management's discussion and analysis, and the MEDC basic financial statements. This report also contains our independent auditor's report on internal control over financial reporting and on compliance and other matters and a glossary of acronyms and terms.

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

Sincerely,

Thomas H. McTavish

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

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MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

GLOSSARY

INDEPENDENT AUDITOR'S REPORT

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

Independent Auditor's Report on
the Financial Statements

Mr. Michael A. Finney, President and Chief Executive Officer
and
Mr. Doug Rothwell, Executive Committee Chair
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Finney and Mr. Rothwell:

We have audited the accompanying basic financial statements of the Michigan Economic Development Corporation, a discretely presented component unit of the State of Michigan, as of and for the fiscal years ended September 30, 2012 and September 30, 2011, as identified in the table of contents. 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 auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the financial statements present only the Michigan Economic Development Corporation and do not purport to, and do not, present fairly the financial position of the State of Michigan or its component units as of September 30, 2012 and September 30, 2011, the changes in its financial position, or, where applicable, its cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Michigan Economic Development Corporation as of September 30, 2012 and September 30, 2011 and the changes in its financial position and its cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 24, 2013 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 grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 11 through 15 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Management has omitted the management's discussion and analysis for fiscal year 2010-11 that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Sincerely,

Thomas H. McTavish

Thomas H. McTavish, C.P.A.
Auditor General
January 24, 2013

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Michigan Economic Development Corporation's (MEDC's) management has prepared this discussion and analysis of the financial performance of MEDC for the period October 1, 2011 through September 30, 2012. MEDC is a public body corporate and a discretely presented component unit of the financial reporting entity of the State of Michigan. MEDC's management is responsible for the basic financial statements and this discussion.

Using the Financial Report

This financial report is prepared in accordance with Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*.

The reporting standards require a statement of net assets; a statement of revenues, expenses, and changes in fund net assets; and a statement of cash flows. This financial report includes the reports of independent auditors, management's discussion and analysis, the basic financial statements, and notes to the financial statements. Amounts reported in the financial statements include both the MEDC corporate funds as well as the State funds made available to MEDC.

The financial statements are interrelated and represent the financial status of MEDC. The statement of net assets presents assets and liabilities as of the end of the fiscal year. The statement of revenues, expenses, and changes in fund net assets presents the revenues earned and expenses incurred during the fiscal year. The statement of cash flows presents information related to cash in-flows and out-flows summarized by operating, capital and related financing, and investing activities.

Analysis of Financial Activities

The assets of MEDC exceeded its liabilities by $124.8 million at September 30, 2012 and by $119.6 million at September 30, 2011. As of September 30, 2012, $5.5 million of this amount was in equity in common cash of the State of Michigan.

Condensed Financial Information
From the Statement of Net Assets
As of September 30

	2012	2011
Current assets	$ 73,365,742	$ 68,893,537
Noncurrent assets		
Loans receivable (net)	$ 14,134,062	$ 15,270,842
Investments	38,019,404	34,614,621
Capital assets (net)	8,469,281	8,906,176
Advances to primary government	1,500,000	1,500,000
Interest receivable	118,061	99,611
Total noncurrent assets	$ 62,240,809	$ 60,391,249
Total assets	$ 135,606,551	$ 129,284,787
Current liabilities	$ 9,798,435	$ 8,800,649
Long-term liabilities	1,014,615	930,150
Total liabilities	$ 10,813,049	$ 9,730,798
Net assets		
Invested in capital assets	$ 8,469,281	$ 8,906,176
Unrestricted net assets	116,324,220	110,647,813
Total net assets	$ 124,793,501	$ 119,553,988

Current assets primarily consist of amounts held in cash, money market accounts, and short-term investments by MEDC; funds in the State of Michigan's equity in common cash; short-term loans receivable; amounts due from the Michigan Strategic Fund (MSF); and receivables for tribal gaming revenues. Interest earned on funds retained in the common cash pool of the State of Michigan is the income of the State and is not transferred to MEDC.

Current assets increased by $4.5 million in fiscal year 2011-12 due to an increase in new investments less a reduction in equity in common cash.

Loans receivable (net) include the long-term portion of the outstanding loans, net of loan loss provisions. Long-term loans receivable had a net decrease of $1.1 million in fiscal year 2011-12, primarily due to some loans being recategorized from long-term to short-term as their maturities were coming due within 12 months.

Capital assets (net) at September 30, 2012 included the cost of the MEDC headquarters building, furniture, trademark, and information technology equipment, net of depreciation.

Advances to primary government at September 30, 2012 represented the amount given to the Department of Treasury as an advance to implement the Public Private Partnership Program.

Current liabilities at September 30, 2012 increased by $1.0 million, primarily consisting of accounts payable at year-end, including payroll obligations.

Long-term liabilities mostly represent long-term compensated absences.

Overall, **net assets** increased by $5.2 million during fiscal year 2011-12 as a result of the preceding activities.

Condensed Financial Information
From the Statement of Revenues, Expenses, and Changes in Fund Net Assets
For the Fiscal Years Ended September 30

	2012	2011
Operating revenues		
Operating grants and contributions	$ 60,394,402	$ 60,543,947
Interest and investment earnings	4,889,617	1,637,338
Other operating revenues	4,509,569	4,008,005
Total operating revenues	$ 69,793,589	$ 66,189,290
Operating expenses		
Salaries, wages, and other administrative expenses	$ 33,143,051	$ 32,188,403
Payments to MSF and primary government	9,319	8,657
Operating grants	31,401,706	32,438,492
Total operating expenses	$ 64,554,076	$ 64,635,553
Operating income (loss)	$ 5,239,513	$ 1,553,737
Change in net assets	$ 5,239,513	$ 1,553,737
Total net assets - Beginning	119,553,988	118,000,251
Total net assets - Ending	$ 124,793,501	$119,553,988

Operating grants and contributions included $0.2 million in federal grants, $16.8 million received from State funding for the economic development programs, and $43.3 million in tribal gaming revenue and miscellaneous fees transferred from MSF. Tribal gaming and fees revenue increased by $4.0 million compared to fiscal year 2010-11 primarily due to the operation of Gun Lake Casino during the entire fiscal year. The State General Fund revenue reduction of $3.4 million is primarily due to eliminations in General Fund funding of the Michigan Promotion Program.

Other operating revenues primarily consist of $3.2 million in tribal gaming revenue from the Keweenaw Bay Indian Community and $0.6 million from the Department of Technology, Management, and Budget for the Call Center operations. Tribal gaming revenue increased by $0.9 million due to a refund of funds held by the tribe in the resolution of a dispute with the Michigan Department of Treasury.

Operating grants for fiscal year 2011-12 included grant commitments for the Michigan Manufacturing Technical Center, Next Energy, Small Business Technical Development Center grants, and marketing program expenses.

Condensed Financial Information
From the Statement of Cash Flows
For the Fiscal Years Ended September 30

	2012	2011
Cash provided (used) by:		
Operating activities	$ 2,622,437	$(10,589,935)
Capital and related financing activities	(100,000)	(148,936)
Investing activities	(8,349,800)	8,174,502
Net increase (decrease) in cash	$ (5,827,363)	$ (2,564,369)
Cash and cash equivalents at beginning of fiscal year	38,931,347	41,495,716
Cash and cash equivalents at end of fiscal year	$ 33,103,984	$ 38,931,347

Cash and cash equivalents at end of fiscal year 2011-12 of $33.1 million primarily included $27.6 million in checking and money market accounts in Bank of America and $5.5 million equity in the State of Michigan common cash.

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BASIC FINANCIAL STATEMENTS

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Net Assets
As of September 30

	2012	2011
ASSETS		
Current assets:		
Cash (Note 2)	$ 27,219,790	$ 28,719,926
Equity in common cash (Note 2)	5,521,340	10,071,283
Money market fund (Note 2)	362,854	140,139
Tribal gaming receivable	1,230,000	1,300,000
Amounts due from MSF	19,293,748	18,675,434
Amount due from primary government	22,062	105,127
Loans receivable (net) (Note 3)	5,789,207	5,142,153
Investments (Note 2)	13,032,611	4,048,285
Other current assets:		
Interest receivable	531,772	355,727
Miscellaneous	362,358	335,464
Total current assets	$ 73,365,742	$ 68,893,537
Noncurrent assets:		
Loans receivable (net) (Note 3)	$ 14,134,062	$ 15,270,842
Investments (Note 2)	38,019,404	34,614,621
Capital assets (net) (Note 4)	8,469,281	8,906,176
Advances to primary government	1,500,000	1,500,000
Interest receivable	118,061	99,611
Total noncurrent assets	$ 62,240,809	$ 60,391,249
Total assets	$ 135,606,551	$ 129,284,787
LIABILITIES		
Current liabilities:		
Accounts payable and other liabilities	$ 8,149,327	$ 7,546,816
Compensated absences (Note 5)	1,446,187	1,111,300
Amounts due to primary government	158,584	142,532
Amounts due to MSF	44,337	
Total current liabilities	$ 9,798,435	$ 8,800,649
Long-term liabilities:		
Compensated absences (Note 5)	$ 912,342	$ 782,904
Amounts due to primary government	102,273	147,245
Total long-term liabilities	$ 1,014,615	$ 930,150
Total liabilities	$ 10,813,049	$ 9,730,798
NET ASSETS		
Invested in capital assets	$ 8,469,281	$ 8,906,176
Unrestricted net assets	116,324,220	110,647,813
Total net assets	$ 124,793,501	$ 119,553,988

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

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Revenues, Expenses, and Changes in Fund Net Assets
For the Fiscal Years Ended September 30

	2012	2011
OPERATING REVENUES (Note 1)		
Operating grants and contributions		
Federal revenue	$ 209,284	$ 1,005,985
Payments from MSF - State appropriated programs	16,849,368	20,233,264
Payments from MSF - Tribal gaming and fees	43,335,750	39,304,698
Total operating grants and contributions	$ 60,394,402	$ 60,543,947
Interest and investment earnings		
Investment earnings	$ 1,499,764	$ 1,011,775
Net increase (decrease) in fair value of investments	2,734,040	228,962
Interest income on loans	655,813	396,601
Total interest and investment earnings	$ 4,889,617	$ 1,637,338
Other operating revenues		
Tribal gaming	$ 3,229,018	$ 2,319,287
Other operating revenues	1,280,551	1,688,719
Total other operating revenues	$ 4,509,569	$ 4,008,005
Total operating revenues	$ 69,793,589	$ 66,189,290
OPERATING EXPENSES (Note 1)		
Salaries, wages, and other administrative expenses	$ 33,143,051	$ 32,188,403
Payments to primary government	9,319	8,657
Operating grants	31,401,706	32,438,492
Total operating expenses	$ 64,554,076	$ 64,635,553
Operating income (loss)	$ 5,239,513	$ 1,553,737
Change in net assets	$ 5,239,513	$ 1,553,737
Total net assets - Beginning	119,553,988	118,000,251
Total net assets - Ending	$ 124,793,501	$ 119,553,988

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

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Cash Flows
For the Fiscal Years Ended September 30

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Payments to employees	$ (26,253,708)	$ (21,226,607)
Payments to suppliers	(5,872,709)	(10,768,302)
Tribal gaming revenue	3,299,018	2,285,287
Other operating revenue	1,992,535	2,576,545
Grants received from federal government	209,284	1,708,897
Operating grants	(30,309,469)	(37,667,285)
Payments to primary government	(9,319)	(8,657)
Payments from MSF	59,566,805	52,510,187
Net cash provided (used) by operating activities	$ 2,622,437	$ (10,589,935)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets (Note 4)	$ (100,000)	$ (148,936)
Net cash provided (used) by capital and related financing activities	$ (100,000)	$ (148,936)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases, sales, and maturities of investment securities (net)	$ (9,655,068)	$ 7,335,483
Interest and dividends on investments	1,305,269	839,019
Net cash provided (used) by investing activities	$ (8,349,800)	$ 8,174,502
Net cash provided (used) - All activities	$ (5,827,363)	$ (2,564,369)
Cash and cash equivalents at beginning of year	38,931,347	41,495,716
Cash and cash equivalents at end of year	$ 33,103,984	$ 38,931,347
RECONCILIATION OF CASH AND CASH EQUIVALENTS		
Per statement of net assets classifications:		
Cash	$ 27,219,790	$ 28,719,926
Equity in common cash	5,521,340	10,071,283
Money market funds	362,854	140,139
Cash and cash equivalents at end of year	$ 33,103,984	$ 38,931,347
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:		
Operating income (loss)	$ 5,239,513	$ 1,553,737
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Interest (nonprogram) and investment income	(1,305,269)	(839,019)
Depreciation	536,894	668,970
Net increase (decrease) in fair value of investments	(2,734,040)	(228,962)
Changes in assets and liabilities:		
Amounts due from MSF and tribal gaming revenue receivable	(548,314)	(7,061,775)
Loans receivable (program loans)	489,725	(1,494,454)
Amounts due from federal agencies		702,912
Other assets	(138,324)	318,469
Accounts payable and other liabilities	1,082,251	(4,209,813)
Net cash provided (used) by operating activities	$ 2,622,437	$ (10,589,935)
SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES		
Increase (decrease) in fair value of investments	$ 1,331,364	$ (1,122,410)
Net noncash provided (used) by investing, capital, and financing activities	$ 1,331,364	$ (1,122,410)

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

Note 1 Significant Accounting Policies

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

a. Reporting Entity

Article VII, Section 28 of the Michigan Constitution and Act 7, P.A. 1967, provided for the creation of MEDC as a public body corporate. MEDC was created in April 1999 by a 10-year contract (interlocal agreement, as amended) between a participating local economic development corporation formed under Act 338, P.A. 1974, as amended, and the Michigan Strategic Fund (MSF). Article VI of the interlocal agreement provides for the automatic renewal of this initial 10-year term for two renewal periods of five years each. In April 2009, this interlocal agreement was automatically renewed for another five years. MEDC is a separate legal entity created to promote smart economic growth by developing strategies and providing services to create and retain good jobs and a high quality of life for Michigan residents. Under the terms of the agreement, the governance of MEDC resides in an Executive Committee of 20 members appointed to eight-year, staggered terms by the Governor.

MEDC is a discretely presented component unit of the financial reporting entity of the State of Michigan. MEDC is a component unit in the State of Michigan reporting entity because the primary government appoints the governing board of MEDC and there is a potential for MEDC to provide specific financial benefits to, or impose specific financial burdens on, the State.

b. Financial Statement Presentation

The basic financial statements have been prepared in accordance with GAAP as prescribed by the Governmental Accounting Standards Board (GASB).

MEDC follows the business type activities reporting requirements of GASB Statement No. 34, which provides for a statement of net assets; a statement of revenues, expenses, and changes in fund net assets; and a statement of cash flows.

MEDC's operations 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.

MEDC follows the accounting rules promulgated by GASB. In addition, MEDC follows all Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins issued on or before November 30, 1989, unless pronouncements conflict with or contradict GASB Statements. The FASB pronouncements issued after November 30, 1989 are not followed in the preparation of the accompanying financial statements.

The accompanying financial statements present only MEDC. Accordingly, they do not purport to, and do not, present fairly the financial position and the changes in financial position and cash flows of the State of Michigan or its component units in conformity with GAAP.

c. Measurement Focus and Basis of Accounting

The financial statements contained in this report are presented using the economic resources measurement focus and the full accrual basis of accounting as provided by GAAP applicable to governments. Under the full accrual basis of accounting, revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows.

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 fund balances of MSF were transferred to MEDC on May 1, 1999. All revenues received by MSF from tribal gaming, private activity bond (PAB) (previously known as industrial development revenue bond [IDRB]) issuance fees, and Michigan Economic Growth Authority and Brownfield fees are transferred to MEDC on a monthly basis. This interlocal agreement also detailed all of MSF's State classified employees to MEDC. State appropriations available to MSF for this purpose are also made available to MEDC, as needed.

MEDC financial statements primarily present the following:

(1) Cash and Cash Equivalents: The amount reported as "Cash and cash equivalents at end of year" on the statement of cash flows is equal to the total of the amounts reported on the statement of net assets for the line items entitled "Cash," "Equity in common cash," and "Money market fund."

(2) Amounts Due From MSF: Amounts due from MSF include the tribal gaming revenue.

(3) Investments: MEDC reports investments in the money market fund, corporate securities, exchange-traded funds (ETFs), and equities at fair value and venture capital investments using cost-based measures unless fair value is readily determinable.

(4) Loans Receivable: Loans receivable are reported net of allowance for losses.

(5) Capital Assets: Capital assets, which mainly include a building, furniture, and equipment, are reported at historical cost, net of depreciation.

(6) Current Liabilities: Current liabilities primarily include accounts payable established for program and administrative expenses and the current portion of compensated absences.

(7) Long-Term Liabilities: Long-term liabilities include compensated absences for employees' unused sick, banked, and annual leave payable when employees terminate employment.

(8) Operating Revenues: Operating revenues include revenues from federal grants, other restricted sources, amounts available to MEDC from State appropriations, tribal gaming revenue, and investment earnings. Also included in operating revenues are tribal gaming and fees collected by MSF and transferred to MEDC for PAB issuance, the Michigan Economic Growth Authority, and Brownfield programs during the fiscal year.

(9) Operating Expenses: Operating expenses include expenses related to program grants funded by State appropriations transferred to MEDC and MEDC nonappropriated funds. Also included in operating expenses are administrative expenses incurred from State appropriations transferred to MEDC.

Note 2 Deposits and Investments

a. Deposits

Deposits held by MEDC consisted of the following:

	As of September 30	
	2012	2011
Equity in common cash	$ 5,521,340	$ 10,071,283
Checking account	1,425,629	946,958
Money market account	25,794,162	27,772,968
Total deposits	$ 32,741,130	$ 38,791,209

Custodial Credit Risk: Governmental accounting standards require disclosures related to custodial credit risks for deposits. Custodial credit risk for deposits is the risk that, in the event of a bank failure, MEDC's deposits may not be returned to it. Deposits are exposed to custodial credit risk if they are not covered by depository insurance and are uncollateralized, collateralized with securities held by the pledging financial institution, or collateralized with securities held by the pledging financial institution's trust department or agent but not in MEDC's name.

Deposits included in MEDC's bank accounts (without recognition of outstanding checks or deposits in transit) were $28,430,379 at September 30, 2012 ($29,082,120 at September 30, 2011). Of that amount, $25,044,162 at September 30, 2012 ($27,022,968 at September 30, 2011) was uninsured and uncollateralized. There were no deposits collateralized with securities held by the pledging financial institution or by the pledging financial institution's trust department or agent but not in MEDC's name. MEDC has no policy for controlling custodial credit risk.

MEDC's deposits included in the State of Michigan's equity in common cash are managed by the State Treasurer. The State Treasurer's policy requires financial institutions to secure State funds with collateral, to be organized under federal or State law, and to maintain an office in Michigan. The policy also restricts deposits to a maximum of 50% of the financial institution's net worth. As of September 30, 2012 and September 30, 2011, 100% and 99.7%, respectively, of the State's common cash were either covered by federal depository insurance or collateralized with securities held in the State's name by the State's agent. Additional details on this policy are described in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*.

b. Investments

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, 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.

MEDC investments in the money market fund, corporate securities, ETFs, and equities are reported at fair value. The fair value is determined by the investment custodian and provided to MEDC in monthly statements. MEDC investments in venture capital are generally reported using cost-based measures unless fair value is readily determinable.

MEDC makes grant and loan commitments as a part of its economic development mission. These commitments are paid from the proceeds of the investments held in short-term and long-term securities. The timing of cash required for program commitments is dependent upon the completion of projects, and MEDC attempts to match investment maturities with its cash flow needs to meet grant commitments. For this reason, investments have frequent turnover and the purchases, and proceeds from sales and maturities, of all investments are shown as a net balance on the statement of cash flows.

The following table shows the fair value of investments at September 30, 2012 and September 30, 2011 by investment type and in total:

	Fair Value as of September 30	
Type of Investment	2012	2011
Money market fund	$ 362,854	$ 140,139
Corporate securities	30,312,772	22,858,339
Equities	52,920	93,504
Mutual funds (ETFs)	12,174,309	8,984,716
Venture capital - Limited partner	2,956,409	2,956,119
Venture capital - Stocks	5,555,605	3,770,229
Total investments	$ 51,414,869	$ 38,803,046

Governmental accounting standards require disclosures for investments for interest rate risk, custodial credit risk, credit risk, foreign currency risk, and concentration of credit risk:

1) Interest Rate Risk: Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of those investments. MEDC does not have a policy regarding interest rate risk. As of September 30, 2012, the average maturities of investments exposed to interest rate risk were as follows:

		Investment Maturities	
Investment Type	Fair Value	Less Than 1 Year	1 to 5 Years
Money market fund	$ 362,854	$ 362,854	
Corporate securities	$ 30,312,772	$ 13,032,609	$ 17,280,163

As of September 30, 2011, the average maturities of investments exposed to interest rate risk were as follows:

		Investment Maturities	
Investment Type	Fair Value	Less Than 1 Year	1 to 5 Years
Money market fund	$ 140,139	$ 140,139	
Corporate securities	$ 22,858,339	$ 4,048,285	$ 18,810,054

2) Custodial Credit Risk: Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, MEDC will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of MEDC, and are held by either the counterparty or the counterparty's trust department or agent but not in MEDC's name.

   As of September 30, 2012 and September 30, 2011, MEDC's investments in corporate securities, mutual funds, equities, and venture capital stocks were not exposed to custodial credit risk because they are registered in MEDC's name and held by the U.S. Trust - Bank of America. MEDC's investments in venture capital limited partnerships were excluded from custodial credit risk because they were not an investment security.

3) Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. GAAP requires disclosures of the credit quality ratings of investments in debt securities. MEDC had the following policy for controlling credit risk of debt securities in fiscal years 2011-12 and 2010-11. Short-term investments (less than one year) shall have a credit rating of not less than A-1/P-1 at the time of purchase. Long-term investments shall have a credit rating equal to BBB or better at the time of purchase. The average quality rating of the fixed income portfolio shall have a credit rating of BBB or better.

The following table shows the credit quality ratings of investments in debt securities as of September 30, 2012:

Investment Type	Fair Value	Credit Quality Rating: Standard & Poor's	Credit Quality Rating: Moody's Investors Service
Corporate securities	$ 1,302,063	AA+	A1
	2,313,530	AA-	AA2
	5,230,750	A+	A1
	4,666,960	A+	A2
	1,049,610	A+	AA3
	4,156,829	A	A2
	4,145,200	A-	A2
	4,914,780	A-	A3
	1,024,470	A-	BAA2
	1,508,580	BBB+	A3
Mutual funds (ETFs)	12,174,309	NR	NR
Money market fund	362,854	NR	NR
Total investments	$ 42,849,934		

The following table shows the credit quality ratings of investments in debt securities as of September 30, 2011:

Investment Type	Fair Value	Credit Quality Rating: Standard & Poor's	Credit Quality Rating: Moody's Investors Service
Corporate securities	$ 2,300,403	AA+	AA2
	797,063	AA	AA2
	1,077,880	AA	AA1
	1,017,080	AA	A1
	1,022,680	AA-	AA3
	1,052,290	AA-	AA2
	2,062,745	AA-	A2
	3,303,398	A+	AA3
	2,133,260	A+	A1
	1,076,950	A	A1
	3,854,711	A	A2
	3,159,880	A-	A3
Mutual funds (ETFs)	8,984,716	NR	NR
Money market fund	140,139	NR	NR
Total investments	$ 31,983,195		

4) Foreign Currency Risk: Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of investments or deposits. As of September 30, 2012 and September 30, 2011, MEDC did not have any investments in foreign securities.

5) Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributable to the magnitude of MEDC's investments with a single issuer. MEDC does not have a policy limiting the dollar value of investments with a single issuer.

At September 30, 2012, MEDC had investments in the following fixed income corporate securities for more than 5% of MEDC's total investments:

Name of Issuer	Amount	Percent of Investments
MetLife Inc.	$2,626,725	5.1%
Barclays Bank	$2,576,730	5.0%

At September 30, 2011, MEDC had investments in the following fixed income corporate securities for more than 5% of MEDC's total investments:

Name of Issuer	Amount	Percent of Investments
JP Morgan Chase	$2,266,808	5.8%
MetLife Inc.	$2,136,360	5.5%

Note 3 Loans Receivable

Loans receivable consisted of the following:

	As of September 30	
	2012	2011
Urban Land Assembly Fund loans	$ 5,241,652	$ 5,329,376
Life Sciences Program	946,170	1,790,176
Michigan Core Community Fund Program	7,454,340	7,677,759
Follow-on Fund	4,696,470	3,731,000
Other loans	7,949,919	8,249,966
Total	$ 26,288,551	$ 26,778,277
Less: Allowance for uncollectible loans	(6,365,282)	(6,365,282)
Total loans receivable	$ 19,923,269	$ 20,412,995

Loans included in the "Other loans" category are collateralized, for qualifying projects, on the basis of participating up to 50% with other public or private lenders. The current portion of loans receivable includes those payments expected to be received during the next fiscal year.

Note 4 Capital Assets

MEDC recorded its capital assets at cost and depreciates applicable capital assets over their useful lives using the straight-line depreciation method (30 years for building and improvement, 3 years for furniture and equipment).

Capital asset activities for the fiscal year ended September 30, 2012 were as follows:

Capital Assets	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Intangibles	$	$ 100,000	$	$ 100,000
Total capital assets, not being depreciated	$ 0	$ 100,000	$ 0	$ 100,000
Building and improvement	$ 13,086,970	$	$	$ 13,086,970
Furniture	2,997,422			2,997,422
Non-information technology equipment	78,265			78,265
Information technology equipment	1,419,114			1,419,114
Capital assets (cost)	$ 17,581,771	$ 0	$ 0	$ 17,581,771
Less accumulated depreciation for:				
Building and improvement	$ (4,391,197)	$ (436,608)	$	$ (4,827,805)
Furniture	(2,962,783)	(34,638)		(2,997,422)
Non-information technology equipment	(78,265)			(78,265)
Information technology equipment	(1,243,349)	(65,648)		(1,308,997)
Total accumulated depreciation	$ (8,675,595)	$ (536,894)	$ 0	$ (9,212,489)
Capital assets (net)	$ 8,906,176	$ (436,894)	$ 0	$ 8,469,281

Capital asset activities for the fiscal year ended September 30, 2011 were as follows:

Capital Assets	Beginning Balance	Increases	Decreases	Ending Balance
Building and improvement	$ 13,086,970	$	$	$ 13,086,970
Furniture	2,952,968	44,453		2,997,422
Non-information technology equipment	78,265			78,265
Information technology equipment	1,314,631	104,482		1,419,114
Capital assets (cost)	$ 17,432,835	$ 148,936	$ 0	$ 17,581,771
Less accumulated depreciation for:				
Building and improvement	$ (3,954,590)	$ (436,608)	$	$ (4,391,197)
Furniture	(2,845,433)	(117,350)		(2,962,783)
Non-information technology equipment	(78,265)			(78,265)
Information technology equipment	(1,128,338)	(115,011)		(1,243,349)
Total accumulated depreciation	$ (8,006,626)	(668,970)	$ 0	$ (8,675,595)
Capital assets (net)	$ 9,426,209	$ (520,034)	$ 0	$ 8,906,176

Note 5 Long-Term Liabilities

Long-term liabilities are accrued when incurred. The following table summarizes compensated absences liabilities of MEDC for the fiscal years ended September 30, 2012 and September 30, 2011, respectively:

	Fiscal Year 2011-12				
	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated absences	$1,894,205	$1,217,518	$ 753,194	$2,358,529	$1,446,187

	Fiscal Year 2010-11				
	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated absences	$2,560,917	$701,265	$1,367,978	$1,894,205	$1,111,300

Note 6 Pension Plans and Other Postemployment Benefits

a. Classified Employees

State classified employees detailed to MEDC are covered by one of two single employer plans offered by the State of Michigan: the State Employees' Defined Benefit Retirement Plan or the State Employees' Defined Contribution Retirement Plan (Plans). Detailed information regarding the Plans' descriptions, accounting policies, vesting and eligibility requirements, actuarial cost methods and assumptions, funding status and requirements, and 10-year historical trend information are provided in the Plans' detailed financial reports.

In addition to the Plans, State classified employees have the option to invest a portion of their salaries into 401(k) and 457 deferred compensation plans. Generally, MEDC does not make any contributions to the deferred compensation plans.

State statutes provide retired employees with other postemployment benefits, such as health, dental, vision, and life insurance coverage based on vesting and other requirements. The cost of retiree health care and other benefits is allocated by the Office of Retirement Services and funded on a pay-as-you-go basis.

For the State Employees' Defined Benefit Retirement Plan, MEDC was billed and paid an average 50.85% and 37.38% of its payroll costs for pension charges and retiree postemployment benefits in fiscal years 2011-12 and 2010-11, respectively. As of April 1, 2012, defined benefit plan members were required to contribute 4% of their payroll toward their pension benefit. For the State Employees' Defined Contribution Retirement Plan, MEDC is required to make a contribution of 4% of the annual payroll and to match employee contributions up to 3% of annual covered payroll.

In addition, MEDC also contributed 9.30% towards other postemployment benefits in fiscal year 2011-12 for most State employees. MEDC made no contributions toward other postemployment benefits in fiscal year 2010-11.

The Plans' detailed financial statements can be obtained from the Office of Retirement Services, Department of Technology, Management, and Budget, 7150 Harris Drive, P.O. Box 30171, Lansing, Michigan 48909.

b. Nonclassified Employees

MEDC offers a defined contribution plan (under Section 401(a) of the Internal Revenue Code) to nonclassified employees after one year of service. MEDC also offers a deferred compensation plan (under Section 457 of the Internal Revenue Code) to nonclassified employees upon employment. Both plans are administered by Alerus Retirement Solutions, a third party administrator, and the employees manage their own investments. Other than making contributions to the 401(a) retirement plan, MEDC does not have any other pension benefit obligation liability. Nonclassified employees do not have any other postemployment benefits.

On August 5, 1999, the MEDC Executive Committee approved an employer contribution rate of 8% of an employee's gross wages to the 401(a) retirement plan for eligible employees. Vesting of the benefits occurs over a five-year period. During fiscal year 2007-08, the MEDC Executive Committee approved a 12% contribution rate for employees in senior vice president positions. All contributions are made on a biweekly basis. Employees cannot contribute to this plan.

MEDC makes no contributions to the 457 deferred compensation plan. Only employees make contributions to the plan.

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL AND COMPLIANCE

STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
(517) 334-8050
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

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

Mr. Michael A. Finney, President and Chief Executive Officer
and
Mr. Doug Rothwell, Executive Committee Chair
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Finney and Mr. Rothwell:

We have audited the accompanying basic financial statements of the Michigan Economic Development Corporation, a discretely presented component unit of the State of Michigan, as of and for the fiscal years ended September 30, 2012 and September 30, 2011, as identified in the table of contents, and have issued our report thereon dated January 24, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the Michigan Economic Development Corporation is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Michigan Economic Development Corporation's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Michigan Economic Development Corporation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Michigan Economic Development Corporation's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control 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. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over financial reporting 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 financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined in the preceding paragraph.

<u>Compliance and Other Matters</u>
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 grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Governor, the Legislature, the Michigan Economic Development Corporation Executive Committee, management, and others within the entity 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.

Sincerely,

Thomas H. McTavish

Thomas H. McTavish, C.P.A.
Auditor General
January 24, 2013

GLOSSARY

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.
exchange-traded fund (ETF)	Securities representing mutual funds that are traded like stocks on the exchanges.
Financial Accounting Standards Board (FASB)	An arm of the Financial Accounting Foundation established to promulgate standards of financial accounting and reporting with respect to activities and transactions of private-sector entities, including business and not-for-profit organizations.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial statements of an audited entity are presented fairly, in all material respects, in conformity with the disclosed basis of accounting.
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.

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.
material misstatement	A misstatement in the financial statements that causes the 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 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 a material misstatement of the financial statements will not be prevented, or detected and corrected, on a timely basis.
MEDC	Michigan Economic Development Corporation.
MSF	Michigan Strategic Fund.
private activity bond (PAB)	A category of municipal bonds distinguished from public purpose bonds in the Tax Reform Act of 1986.
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.
unqualified opinion	An auditor's opinion in which the auditor states that the financial statements presenting the basic financial information of the audited agency are fairly presented in conformity with the disclosed basis of accounting.

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STATE OF MICHIGAN

OFFICE of the AUDITOR GENERAL