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 Year Ended September 30, 2014

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Doug A. Ringler, CPA, CIA
AUDITOR GENERAL

271-0406-15

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

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Report Summary

Financial Audit

Michigan Economic Development Corporation

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

Fiscal Year Ended September 30, 2014

Report Number:
271-0406-15

Released:
February 2015

The Michigan Economic Development Corporation (MEDC) was created as a separate legal entity in April 1999 by an interlocal agreement between a participating local economic development corporation formed under Act 338, P.A. 1974, as amended, and the Michigan Strategic Fund. This financial audit of MEDC was conducted as part of the constitutional responsibility of the Office of the Auditor General.

Auditor's Report Issued
UNMODIFIED OPINION ☒ MODIFIED OPINION ☐
We issued an unmodified opinion on MEDC's basic financial statements to reflect that they were fairly presented, in all material respects, in accordance with accounting principles generally accepted in the United States of America.

Report on Internal Control, Compliance, and Other Matters
We will issue our Report on Internal Control, Compliance, and Other Matters within 60 days under a separate cover.

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

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

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Doug A. Ringler, CPA, CIA
Auditor General

February 13, 2015

Mr. Steven Arwood, Chief Executive Officer
and
Mr. Doug Rothwell, Executive Committee Chair
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Arwood 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 year ended September 30, 2014.

This report contains our report summary, our independent auditor's report on the financial statements and other reporting required by *Government Auditing Standards*, the MEDC management's discussion and analysis, the MEDC basic financial statements, and a glossary of abbreviations and terms.

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

Sincerely,

Doug Ringler

Doug Ringler
Auditor General

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MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

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INDEPENDENT AUDITOR'S REPORT

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Doug A. Ringler, CPA, CIA
Auditor General
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Independent Auditor's Report on the Financial Statements
and Other Reporting Required by *Government Auditing Standards*

Mr. Steven Arwood, Chief Executive Officer
and
Mr. Doug Rothwell, Executive Committee Chair
Michigan Economic Development Corporation
300 North Washington Square
Lansing, Michigan

Dear Mr. Arwood and Mr. Rothwell:

Report on the Financial Statements

We have audited the accompanying financial statements of the Michigan Economic Development Corporation, a discretely presented component unit of the State of Michigan, as of and for the fiscal year ended September 30, 2014 and the related notes to the financial statements, which collectively comprise the Michigan Economic Development Corporation's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements 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 statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, 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 statements 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 statements.

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 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, 2014 and the changes in financial position and cash flows for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note 1 to the financial statements, 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, 2014, the changes in its financial position, or, where applicable, its cash flows for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

As discussed in Note 2 to the financial statements, the Michigan Economic Development Corporation adopted Governmental Accounting Standards Board Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, for the fiscal year ended September 30, 2014. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, as listed in the table of contents, 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we will also issue a report 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Michigan Economic Development Corporation's internal control over financial reporting and compliance.

Sincerely,

Doug Ringler

Doug Ringler
Auditor General
January 30, 2015

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, 2013 through September 30, 2014. 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 accounting principles generally accepted in the United States of America (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB).

The reporting requirements of GASB require a statement of net position; a statement of revenues, expenses, and changes in net position; and a statement of cash flows. This financial report includes the independent auditor's report, 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 position presents assets and liabilities as of the end of the fiscal year. The statement of revenues, expenses, and changes in fund net position 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 $130.7 million at September 30, 2014 and by $129.5 million at September 30, 2013. As of September 30, 2014, $22.9 million of this amount was in equity in common cash of the State of Michigan.

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

	2014	2013
Current assets	$ 79,749,723	$ 79,641,841
Noncurrent assets		
Collateral deposit	$ 368,462	$ 400,000
Loans receivable (net)	4,026,772	6,098,435
Investments	52,417,951	44,104,232
Capital assets (net)	7,531,916	7,989,406
Advances to primary government		1,500,000
Interest receivable		52,620
Total noncurrent assets	$ 64,345,101	$ 60,144,692
Total assets	$144,094,824	$139,786,533
Current liabilities	$ 12,332,727	$ 9,236,591
Long-term liabilities	1,103,725	1,072,001
Total liabilities	$ 13,436,452	$ 10,308,592
Net position		
Net investment in capital assets	$ 7,531,916	$ 7,989,406
Unrestricted	123,126,456	121,488,535
Total net position	$130,658,372	$129,477,941

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.

Loans receivable (net) includes the current and long-term portion of the outstanding loans, net of loan loss provisions. Net loans receivable decreased by $1.8 million, which was primarily due to an increase in loan loss provisions or write-offs of $1.0 million, and conversions of loans receivable to investments of $0.4 million. An explanation of loan loss provisions and other write-offs is included within the analysis of the statement of revenues, expenses, and changes in net position.

Capital assets (net) at September 30, 2014 included the cost of the MEDC headquarters building, furniture, trademark, and information technology equipment, net of depreciation.

Advances to primary government outstanding of $1.5 million at September 30, 2013 represented the amount given as an advance to implement the Public Private Partnership Program at the State level. This amount was written off as uncollectible during fiscal year 2014 based on an evaluation made by the Program administrator.

Current liabilities at September 30, 2014, which primarily consist of accounts payable at year-end, including payroll obligations, increased by $3.1 million. This increase was primarily related to accounts payable at year-end for the new Skilled Trades Training Program.

Long-term liabilities mostly represent the long-term portion of compensated absences.

Overall, **net position** increased by $1.2 million during fiscal year 2014 as a result of the preceding activities.

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

	2014	2013
Operating revenues		
Operating grants and contributions	$ 82,277,096	$ 74,706,857
Interest and investment earnings	(92,587)	2,949,122
Other operating revenues	5,141,230	4,533,742
Total operating revenues	$ 87,325,738	$ 82,189,721
Operating expenses		
Salaries, wages, and other administrative expenses	$ 39,731,263	$ 34,168,609
Loan loss provisions and other write-offs	2,436,189	8,901,803
Payments to MSF and primary government	10,457	159,819
Operating grants	43,967,397	34,275,050
Total operating expenses	$ 86,145,307	$ 77,505,282
Operating income (loss)	$ 1,180,432	$ 4,684,439
Change in net position	$ 1,180,432	$ 4,684,439
Total net position - Beginning	129,477,941	124,793,501
Total net position - Ending	$130,658,372	$129,477,941

Operating grants and contributions included $40.5 million received from State appropriated funding for the economic development programs and $41.8 million in tribal gaming revenue and miscellaneous fees transferred from MSF. The revenue from State appropriated programs funding increased by $14.2 million primarily due to additional General Fund appropriations for the new Skilled Trades Training Program and increase to Jobs Creation Services line items for specific earmarks. The revenue from tribal gaming revenues and miscellaneous fees decreased by $6.6 million primarily due to decreased casino revenues and fees received by MSF.

Other operating revenues primarily consist of $2.3 million in tribal gaming revenue from the Keweenaw Bay Indian Community; $0.7 million from the Department of

Technology, Management, and Budget for the Call Center operations; and $0.9 million in lease revenues from the Michigan Life Science and Innovation Center (MLSIC), a building managed by MEDC on behalf of the Michigan Land Bank Fast Track Authority (a discretely presented component unit of the State of Michigan). All MLSIC building related expenditures are included in other administrative expenses.

Loan loss provisions and other write-offs primarily includes $1.5 million in an advance to implement the Public Private Partnership Program written off as uncollectible and $0.6 million in loss provisions related to uncollectible loans.

Operating grants for fiscal year 2014 included disbursements of grant commitments for the Michigan Manufacturing Technical Center, Next Energy, and Small Business Technical Development Center grants; matching funds for federal competitive grants; and Skilled Trades Training Program, Export Program, Talent Development Program, marketing, and other program expenses.

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

	2014	2013
Cash provided (used) by:		
Operating activities	$ (8,238,423)	$ 12,486,887
Capital and related financing activities		(10,403)
Investing activities	(3,064,919)	(1,166,392)
Net increase (decrease) in cash	$ (11,303,343)	$ 11,310,092
Cash and cash equivalents at beginning of year	44,414,076	33,103,984
Cash and cash equivalents at end of year	$ 33,110,734	$ 44,414,076

Cash and cash equivalents at end of fiscal year 2014 of $33.1 million included $10.2 million in checking and money market accounts in Bank of America and $22.9 million equity in the State of Michigan common cash.

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BASIC FINANCIAL STATEMENTS

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Net Position
As of September 30, 2014

ASSETS		
Current assets:		
Cash (Note 3)	$	10,007,500
Equity in common cash (Note 3)		22,892,069
Money market fund (Note 3)		211,165
Tribal gaming receivable		1,228,159
Amounts due from MSF		36,466,062
Amount due from primary government		688,987
Loans receivable (net) (Note 5)		2,351,026
Investments (Note 3)		5,281,530
Other current assets:		
Interest receivable		416,336
Miscellaneous		206,890
Total current assets	$	79,749,723
Noncurrent assets:		
Collateral deposit	$	368,462
Loans receivable (net) (Note 5)		4,026,772
Investments (Note 3)		52,417,951
Capital assets (net) (Note 6)		7,531,916
Total noncurrent assets	$	64,345,101
Total assets	$	144,094,824
LIABILITIES		
Current liabilities:		
Accounts payable and other liabilities	$	10,246,342
Compensated absences (Note 7)		1,212,162
Amounts due to primary government		253,339
Amounts due to MSF		620,883
Total current liabilities	$	12,332,727
Long-term liabilities:		
Compensated absences (Note 7)	$	1,091,396
Amounts due to primary government		12,328
Total long-term liabilities	$	1,103,725
Total liabilities	$	13,436,452
NET POSITION		
Net investment in capital assets	$	7,531,916
Unrestricted		123,126,456
Total net position	$	130,658,372

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

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Revenues, Expenses, and Changes in Net Position
For the Fiscal Year Ended September 30, 2014

OPERATING REVENUES (Note 1)		
Operating grants and contributions		
Payments from MSF - State appropriated programs	$	40,466,676
Payments from MSF - Tribal gaming and fees		41,810,420
Total operating grants and contributions	$	82,277,096
Interest and investment earnings		
Investment earnings	$	1,244,042
Net increase (decrease) in fair value of investments		(1,726,725)
Interest income on loans		390,096
Total interest and investment earnings	$	(92,587)
Other operating revenues		
Tribal gaming	$	2,309,657
Other operating revenues		2,831,572
Total other operating revenues	$	5,141,230
Total operating revenues	$	87,325,738
OPERATING EXPENSES (Note 1)		
Salaries, wages, and other administrative expenses	$	39,731,263
Loan loss provisions and other write-offs		2,436,189
Payments to primary government		10,457
Operating grants		43,967,397
Total operating expenses	$	86,145,307
Operating income (loss)	$	1,180,432
Change in net position	$	1,180,432
Total net position - Beginning		129,477,941
Total net position - Ending	$	130,658,372

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

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
Statement of Cash Flows
For the Fiscal Year Ended September 30, 2014

CASH FLOWS FROM OPERATING ACTIVITIES		
Payments to employees	$	(27,614,770)
Payments to suppliers		(10,918,874)
Tribal gaming revenue		2,281,498
Other operating revenue		2,705,559
Operating grants		(40,676,014)
Payments to primary government		(10,457)
Payments from MSF		65,994,636
Net cash provided (used) by operating activities	$	(8,238,423)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets (Note 6)	$	
Net cash provided (used) by capital and related financing activities	$	0
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases, sales, and maturities of investment securities (net)	$	(4,439,614)
Interest and dividends on investments		1,374,694
Net cash provided (used) by investing activities	$	(3,064,919)
Net cash provided (used) - All activities	$	(11,303,343)
Cash and cash equivalents at beginning of year		44,414,076
Cash and cash equivalents at end of year	$	33,110,734
RECONCILIATION OF CASH AND CASH EQUIVALENTS		
Per statement of net position classifications:		
Cash	$	10,007,500
Equity in common cash		22,892,069
Money market fund		211,165
Cash and cash equivalents at end of year	$	33,110,734
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:		
Operating income (loss)	$	1,180,432
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Interest (nonprogram) and investment income		(1,374,694)
Depreciation		457,489
Net increase (decrease) in fair value of investments		1,726,725
Changes in assets and liabilities:		
Amounts due from MSF and tribal gaming revenue receivable		(16,310,619)
Loans receivable (program loans)		3,308,304
Collateral deposit		31,538
Other assets		(385,457)
Accounts payable and other liabilities		3,127,859
Net cash provided (used) by operating activities	$	(8,238,423)
SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES		
Loans converted to equity	$	380,384
Increase (decrease) in fair value of investments		(2,101,834)
Net noncash provided (used) by investing, capital, and financing activities	$	(1,721,450)

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 2014, this interlocal agreement was automatically renewed for another five years. MEDC is a separate legal entity created to promote 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 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, which provide for a statement of net position; a statement of revenues, expenses, and changes in net position; 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.

The accompanying financial statements present only MEDC. Accordingly, they do not purport to, and do not, present fairly the financial position, the changes in financial position, or, where applicable, cash flows of the State of Michigan or its other 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 accrual basis of accounting as provided by GAAP applicable to governments. Under the 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) 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 position 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, equities, and exchange-traded funds (ETFs) 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 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 and loan loss provisions and other write-off expenses.

Note 2 Accounting Changes

During the fiscal year ended September 30, 2014, MEDC implemented GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees.* This statement requires a government that extends a nonexchange financial guarantee to recognize a liability when qualitative factors and historical data, if any, indicate that it is more likely than not that the government will be required to make a payment on the guarantee. The effects of applying this standard are disclosed in Note 4.

Note 3 Deposits and Investments

a. Deposits

Deposits held by MEDC at September 30, 2014 were as follows:

Equity in common cash	$22,892,069
Checking account	4,709,667
Money market fund	5,666,295
Total deposits	$33,268,031

Custodial Credit Risk: Governmental accounting standards require disclosures related to custodial credit risk 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 $11,443,426 at September 30, 2014. Of that amount, $153,926 at September 30, 2014 was uninsured and uncollateralized. There were deposits of $10,351,916 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, 2014, 100% of the State's common cash was 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 at fair value as determined by MEDC's portfolio managers based on site visits, review of companies' available financial data/reports, and professional judgment.

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, 2014 by investment type and in total:

Investment Type	Fair Value
Money market fund	$ 211,165
Corporate securities	36,195,513
Equities	60,776
Mutual funds (ETFs)	14,842,825
Venture capital - Limited partnerships	2,244,166
Venture capital - Stocks	4,356,186
Total investments	$57,910,631

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, 2014, 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	$ 211,165	$ 211,165	
Corporate securities	$ 36,195,513	$ 5,281,528	$ 30,913,986

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, 2014, 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 Bank of America - Merrill Lynch. 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 year 2014. 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, 2014:

		Credit Quality Rating	
Investment Type	Fair Value	Standard & Poor's	Moody's Investors Service
Corporate securities	$ 753,128	AA+	A1
	1,003,630	AA-	A1
	1,000,830	AA-	AA2
	3,564,610	AA-	AA3
	1,534,890	AA	AA2
	3,011,370	AA	AA3
	4,010,640	A+	A1
	2,005,000	A+	A2
	997,090	A-	A1
	1,023,330	A-	A3
	3,612,590	A-	BAA1
	1,098,100	A	A1
	11,581,745	A	A2
	998,560	A	A3
Mutual funds (ETFs)	14,842,825	Unrated	Unrated
Money market fund	211,165	Unrated	Unrated
Total investments	$51,249,503		

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, 2014, 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's investment policy limits investments in securities in a single issuer, other than those issued by the

U.S. government or its agencies and in money market mutual funds, to a maximum of 5% of its total portfolio. MEDC had investments in the following companies for more than 5% of MEDC's total investments at September 30, 2014:

Name of Issuer	Amount	Percentage of Investments
Coca-Cola Company	$ 3,011,370	5.2%
Intel Corporation	$ 2,990,280	5.2%

Note 4 Nonexchange Financial Guarantee

MEDC extended a nonexchange financial guarantee by entering into a collateral deposit contract during fiscal year 2012. The MEDC Executive Committee has the legal authority to enter into these types of transactions and to delegate authority for the administration of the contracts. MEDC has a contractual relationship with the lender that has extended credit to a borrower under a separate loan agreement.

Under the terms of the contract between MEDC and the lender, MEDC has guaranteed 100% of the loan amount for the length of the 10-year borrowing period. On a quarterly basis, MEDC reconciles its collateral deposit balance with the lender and collects any monies that are contractually owed back to MEDC. Based on information obtained by MEDC from the lender regarding the likelihood of default, MEDC did not recognize any liability for this deposit. MEDC has separate subordinated guarantee agreements with each of the borrower's owners, which provides MEDC with the right to recover its funds in the event of default. As of September 30, 2014, the guarantee amount outstanding for this collateral deposit guarantee was $368,462.

Note 5 Loans Receivable

Loans receivable held by MEDC as of September 30, 2014 consisted of the following:

Loan Category	Loans Receivable
Urban Land Assembly Fund loans	$ 5,119,973
Life Sciences Program	327,883
Michigan Core Community Fund Program	5,622,457
Follow-On Fund	2,976,022
Other loans	6,949,778
Total	$ 20,996,114
Less: Allowance for uncollectible loans	(14,618,316)
Total loans receivable	$ 6,377,798

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 6 Capital Assets

MEDC records 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).

Furniture and equipment are capitalized when the cost of individual items exceeds $5,000.

Capital asset activities for the fiscal year ended September 30, 2014 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	$ 100,000	$ 0	$ 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	1,429,517			1,429,517
Capital assets (cost)	$ 17,592,174	$ 0	$ 0	$ 17,592,174
Less accumulated depreciation for:				
Building and improvement	$ (5,264,413)	$ (436,608)	$	$ (5,701,021)
Furniture	(2,997,422)			(2,997,422)
Non-information technology equipment	(78,265)			(78,265)
Information technology equipment	(1,362,668)	(20,881)		(1,383,550)
Total accumulated depreciation	$ (9,702,768)	$ (457,489)	$ 0	$(10,160,257)
Capital assets (net)	$ 7,989,406	$ (457,489)	$ 0	$ 7,531,916

Note 7 Long-Term Liabilities

Long-term liabilities are accrued when incurred. The following table summarizes compensated absences liabilities of MEDC for the fiscal year ended September 30, 2014:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated absences	$2,181,300	$914,674	$792,415	$2,303,559	$1,212,162

Note 8 Pension Plans and Other Postemployment Benefits

a. Classified Employees

State classified employees who work for MEDC are covered by one of two single employer pension 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. MEDC does not make any contributions to the deferred compensation plans for employees in the State Employees' Defined Benefit Retirement Plan.

Prior to April 1, 2012, State statutes provided 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 is funded by the State on a prefunded basis.

For the State Employees' Defined Benefit Retirement Plan, MEDC paid an average of 3.26% of its payroll costs for pension charges in fiscal year 2014. As of April 1, 2012, defined benefit plan members were required to contribute 4% of their compensation 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. MEDC transferred $325,577 of its payroll costs for its employer contribution for the defined contribution plan in fiscal year 2014. In addition, MEDC contributed 46.97% of its payroll costs toward other postemployment benefits for most State employees in fiscal year 2014.

The Plans' detailed financial statements may be obtained from visiting <http://www.michigan.gov/ors>, by writing to the Office of Retirement Services, Department of Technology, Management, and Budget, P.O. Box 30171, Lansing, Michigan 48909, or by calling (800) 381-5111.

b. Nonclassified Employees

MSF reimburses MEDC for MEDC nonclassified employees working on MSF programs. 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, neither MEDC nor MSF 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. MSF reimburses MEDC for an employer contribution rate of 8% of an employee's gross wages to the 401(a) retirement plan for eligible employees. During fiscal year 2008, 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 made $914,239 in contributions to the 401(a) retirement plan during fiscal year 2014 and was reimbursed approximately $350,000 of this amount from MSF.

Neither MEDC nor MSF make any contributions to the 457 deferred compensation plan. Only employees make contributions to this plan.

GLOSSARY

exchange-traded fund (ETF)	Securities representing mutual funds that are traded like stocks on the exchanges.
financial audit	An audit that is designed to provide reasonable assurance about whether the basic financial statements 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.
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 basic financial statements that causes the statements to not present fairly the financial position or the changes in financial position, and, where applicable, cash flows thereof, in accordance with the applicable financial reporting framework.

MEDC	Michigan Economic Development Corporation.
MLSIC	Michigan Life Science and Innovation Center.
modified opinion	A qualified opinion, an adverse opinion, or a disclaimer of opinion.
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.
unmodified opinion	The opinion expressed by the auditor when the auditor, having obtained sufficient appropriate audit evidence, concludes that the basic financial statements are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.

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STATE OF MICHIGAN

OFFICE of the AUDITOR GENERAL