



# 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, 2013



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

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

Audit report information can be accessed at:

*<http://audgen.michigan.gov>*



Michigan  
Office of the Auditor General  
**REPORT SUMMARY**

*Financial Audit*

*Michigan Economic Development Corporation*  
*(A Discretely Presented Component Unit of the State of Michigan)*  
*Fiscal Year Ended September 30, 2013*

Report Number:  
271-0406-14

Released:  
February 2014

*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 unmodified opinion on MEDC's basic financial statements.

~ ~ ~ ~ ~

**Internal Control Over Financial Reporting and on Compliance and Other Matters**

In accordance with *Government Auditing Standards*, we will also issue a report on our consideration of MEDC'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.

~ ~ ~ ~ ~

**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 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.

~ ~ ~ ~ ~

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  
OFFICE OF THE AUDITOR GENERAL  
201 N. WASHINGTON SQUARE  
LANSING, MICHIGAN 48913  
(517) 334-8050  
FAX (517) 334-8079

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

February 7, 2014

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 year ended September 30, 2013.

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,

A handwritten signature in black ink that reads 'Thomas H. McTavish'.

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



## TABLE OF CONTENTS

### MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

	<u>Page</u>
INTRODUCTION	
Report Summary	1
Report Letter	3
INDEPENDENT AUDITOR'S REPORT	
Independent Auditor's Report on the Financial Statements and Other Reporting Required by <i>Government Auditing Standards</i>	8
MANAGEMENT'S DISCUSSION AND ANALYSIS	
Management's Discussion and Analysis	11
BASIC FINANCIAL STATEMENTS	
Statement of Net Position	18
Statement of Revenues, Expenses, and Changes in Net Position	19
Statement of Cash Flows	20
Notes to the Financial Statements	21
GLOSSARY	
Glossary of Abbreviations and Terms	35



# INDEPENDENT AUDITOR'S REPORT



STATE OF MICHIGAN  
OFFICE OF THE AUDITOR GENERAL  
201 N. WASHINGTON SQUARE  
LANSING, MICHIGAN 48913  
(517) 334-8050  
FAX (517) 334-8079

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

Independent Auditor's Report on the Financial Statements  
and Other Reporting Required by *Government Auditing Standards*

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:

**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, 2013 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, 2013 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 Matter**

As discussed 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 other component units as of September 30, 2013, the changes in financial position, or, where applicable, 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.

**Other Matter****Required Supplementary Information**

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.

**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,



Thomas H. McTavish, C.P.A.  
Auditor General  
January 24, 2014

# 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, 2012 through September 30, 2013. 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 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 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 \$129.5 million at September 30, 2013 and by \$124.8 million at September 30, 2012. As of September 30, 2013, \$11.9 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

	2013	2012
Current assets	\$ 79,641,841	\$ 73,365,742
Noncurrent assets		
Collateral deposit	\$ 400,000	\$
Loans receivable (net)	6,098,435	14,134,062
Investments	44,104,232	38,019,404
Capital assets (net)	7,989,406	8,469,281
Advances to primary government	1,500,000	1,500,000
Interest receivable	52,620	118,061
Total noncurrent assets	\$ 60,144,692	\$ 62,240,809
 Total assets	 \$139,786,533	 \$135,606,551
Current liabilities	\$ 9,236,591	\$ 9,798,435
Long-term liabilities	1,072,001	1,014,615
Total liabilities	\$ 10,308,592	\$ 10,813,049
Net position		
Net investment in capital assets	\$ 7,989,406	\$ 8,469,281
Unrestricted	121,488,535	116,324,220
 Total net position	 \$129,477,941	 \$124,793,501

**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 \$6.3 million in fiscal year 2012-13 due to a net increase in equity in common cash and cash on hand less a reduction in short-term investments and loans receivable.

**Loans receivable (net)** includes the current and long-term portion of the outstanding loans, net of loan loss provisions. Net loans receivable decreased by \$11.7 million, which was primarily due to an increase in loan loss provisions or write-offs of \$8.0 million and an increase in conversions of loans receivable to investments and grants of \$2.9 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, 2013 included the cost of the MEDC headquarters building, furniture, trademark, and information technology equipment, net of depreciation.

**Advances to primary government** at September 30, 2013 represented the amount given to the Department of Treasury as an advance to implement the Public Private Partnership Program.

**Current liabilities** at September 30, 2013, which primarily consist of accounts payable at year-end, including payroll obligations, decreased by \$562,000.

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

Overall, **net position** increased by \$4.7 million during fiscal year 2012-13 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

	2013	2012
Operating revenues		
Operating grants and contributions	\$ 74,706,857	\$ 60,394,402
Interest and investment earnings	2,949,122	4,889,617
Other operating revenues	4,533,742	4,509,569
Total operating revenues	\$ 82,189,721	\$ 69,793,589
Operating expenses		
Salaries, wages, and other administrative expenses	\$ 34,168,609	\$ 33,143,051
Loan loss provisions and other write-offs	8,901,803	
Payments to MSF and primary government	159,819	9,319
Operating grants	34,275,050	31,401,706
Total operating expenses	\$ 77,505,282	\$ 64,554,076
Operating income (loss)	\$ 4,684,439	\$ 5,239,513
Change in net position	\$ 4,684,439	\$ 5,239,513
Total net position - Beginning	124,793,501	119,553,988
Total net position - Ending	\$129,477,941	\$124,793,501

**Operating grants and contributions** included \$26.3 million received from State appropriated funding for the economic development programs and \$48.4 million in tribal gaming revenue and miscellaneous fees transferred from MSF. The revenue from State appropriated programs funding increased by \$9.4 million primarily due to additional General Fund appropriations for the Community Ventures Program.

**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 \$0.8 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 loss provisions related to loans made to the City of Detroit from the Michigan Core Community Fund Program (\$5.0 million) and the Urban Land Assembly Fund (\$2.0 million) in 2001. In light of the City of Detroit's bankruptcy filing, MEDC has recorded loss provisions for the full loan amounts. MEDC has taken steps to file its creditor claims in the bankruptcy case.

**Operating grants** for fiscal year 2012-13 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; as well as 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

	2013	2012
Cash provided (used) by:		
Operating activities	\$ 12,486,887	\$ 2,622,437
Capital and related financing activities	(10,403)	(100,000)
Investing activities	(1,166,392)	(8,349,800)
Net increase (decrease) in cash	\$ 11,310,092	\$ (5,827,363)
Cash and cash equivalents at beginning of fiscal year	33,103,984	38,931,347
Cash and cash equivalents at end of fiscal year	\$ 44,414,076	\$ 33,103,984

**Cash and cash equivalents** at end of fiscal year 2012-13 of \$44.4 million included \$32.5 million in checking and money market accounts in Bank of America and \$11.9 million equity in the State of Michigan common cash.



# BASIC FINANCIAL STATEMENTS

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION  
Statement of Net Position  
As of September 30, 2013

**ASSETS**

Current assets:	
Cash (Note 2)	\$ 31,013,118
Equity in common cash (Note 2)	11,935,750
Money market fund (Note 2)	1,465,209
Tribal gaming receivable	1,200,000
Amounts due from MSF	20,183,602
Amount due from primary government	202,829
Loans receivable (net) (Note 3)	2,087,667
Investments (Note 2)	10,882,360
Other current assets:	
Interest receivable	494,368
Miscellaneous	176,938
Total current assets	<u>\$ 79,641,841</u>
Noncurrent assets:	
Collateral deposit	\$ 400,000
Loans receivable (net) (Note 3)	6,098,435
Investments (Note 2)	44,104,232
Capital assets (net) (Note 4)	7,989,406
Advances to primary government	1,500,000
Interest receivable	52,620
Total noncurrent assets	<u>\$ 60,144,692</u>
Total assets	<u>\$ 139,786,533</u>

**LIABILITIES**

Current liabilities:	
Accounts payable and other liabilities	\$ 7,858,612
Compensated absences (Note 5)	1,166,600
Amounts due to primary government	211,379
Total current liabilities	<u>\$ 9,236,591</u>
Long-term liabilities:	
Compensated absences (Note 5)	\$ 1,014,701
Amounts due to primary government	57,301
Total long-term liabilities	<u>\$ 1,072,001</u>
Total liabilities	<u>\$ 10,308,592</u>

**NET POSITION**

Net investment in capital assets	\$ 7,989,406
Unrestricted	<u>121,488,535</u>
Total net position	<u>\$ 129,477,941</u>

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, 2013

**OPERATING REVENUES (Note 1)**

<u>Operating grants and contributions</u>	
Payments from MSF - State appropriated programs	\$ 26,280,017
Payments from MSF - Tribal gaming and fees	48,426,840
Total operating grants and contributions	<u>\$ 74,706,857</u>
 <u>Interest and investment earnings</u>	
Investment earnings	\$ 1,539,686
Net increase (decrease) in fair value of investments	1,125,653
Interest income on loans	283,782
Total interest and investment earnings	<u>\$ 2,949,122</u>
 <u>Other operating revenues</u>	
Tribal gaming	\$ 2,327,542
Other operating revenues	2,206,200
Total other operating revenues	<u>\$ 4,533,742</u>
Total operating revenues	<u>\$ 82,189,721</u>

**OPERATING EXPENSES (Note 1)**

Salaries, wages, and other administrative expenses	\$ 34,168,609
Loan loss provisions and other write-offs	8,901,803
Payment to MSF	151,051
Payments to primary government	8,768
Operating grants	34,275,050
Total operating expenses	<u>\$ 77,505,282</u>
 Operating income (loss)	 <u>\$ 4,684,439</u>
 Change in net position	 \$ 4,684,439
 Total net position - Beginning	 <u>124,793,501</u>
 Total net position - Ending	 <u>\$ 129,477,941</u>

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, 2013

**CASH FLOWS FROM OPERATING ACTIVITIES**

Payments to employees	\$ (27,443,722)
Payments to suppliers	(6,448,350)
Tribal gaming revenue	2,357,542
Other operating revenue	2,494,634
Operating grants	(32,130,401)
Payments to MSF	(151,051)
Payments to primary government	(8,768)
Payments from MSF	73,817,003
Net cash provided (used) by operating activities	\$ 12,486,887

**CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES**

Acquisition and construction of capital assets (Note 4)	\$ (10,403)
Net cash provided (used) by capital and related financing activities	\$ (10,403)

**CASH FLOWS FROM INVESTING ACTIVITIES**

Purchases, sales, and maturities of investment securities (net)	\$ (2,808,923)
Interest and dividends on investments	1,642,531
Net cash provided (used) by investing activities	\$ (1,166,392)
Net cash provided (used) - All activities	\$ 11,310,092
Cash and cash equivalents at beginning of year	33,103,984
Cash and cash equivalents at end of year	\$ 44,414,076

**RECONCILIATION OF CASH AND CASH EQUIVALENTS**

Per statement of net position classifications:	
Cash	\$ 31,013,118
Equity in common cash	11,935,750
Money market fund	1,465,209
Cash and cash equivalents at end of year	\$ 44,414,076

**RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:**

Operating income (loss)	\$ 4,684,439
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:	
Interest (nonprogram) and investment income	(1,642,531)
Depreciation	490,279
Net increase (decrease) in fair value of investments	(1,125,653)
Changes in assets and liabilities:	
Amounts due from MSF and tribal gaming revenue receivable	(859,854)
Loans receivable (program loans)	11,737,167
Collateral deposit	(400,000)
Other assets	107,497
Accounts payable and other liabilities	(504,457)
Net cash provided (used) by operating activities	\$ 12,486,887

**SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES**

Loans converted to equity	\$ 1,767,768
Increase (decrease) in fair value of investments	(113,184)
Net noncash provided (used) by investing, capital, and financing activities	\$ 1,654,585

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

## Notes to the Financial Statements

### Note 1 Significant Accounting Policies

The accounting policies of the Michigan Economic Development Corporation (MEDC) conform to 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 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, 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 and the changes in financial position and 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 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) 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 Deposits and Investments

a. Deposits

Deposits held by MEDC at September 30, 2013 were as follows:

Equity in common cash	\$11,935,750
Checking account	2,553,689
Money market account	28,859,429
	<hr/>
Total deposits	<u>\$43,348,868</u>

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 \$31,358,903 at September 30, 2013. Of that amount, \$30,229,133 at September 30, 2013 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, 2013, 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 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, 2013 by investment type and in total:

Investment Type	Fair Value
Money market fund	\$ 1,465,209
Corporate securities	32,761,868
Equities	39,121
Mutual funds (ETFs)	12,556,657
Venture capital - Limited partnerships	2,324,059
Venture capital - Stocks	7,304,885
Total investments	<u>\$56,451,801</u>

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, 2013, the average maturities of investments exposed to interest rate risk were as follows:

Investment Type	Fair Value	Investment Maturities	
		Less Than 1 Year	1 to 5 Years
Money market fund	\$ 1,465,209	\$ 1,465,209	-
Corporate securities	\$32,761,868	\$10,882,358	\$21,879,510

- 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, 2013, 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 year 2012-13. 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, 2013:

Investment Type	Fair Value	Credit Quality Rating	
		Standard & Poor's	Moody's Investors Service
Corporate securities	\$ 777,900	AA+	A1
	1,002,300	AA+	AA3
	1,025,920	AA-	AA2
	2,046,000	AA-	AA3
	6,134,880	A+	A1
	1,032,460	A+	A2
	1,134,500	A	A1
	5,901,893	A	A2
	1,983,000	A	A3
	985,480	A-	A1
	1,007,780	A-	A2
	7,217,430	A-	A3
	2,512,325	BBB+	BAA1
Mutual funds (ETFs)	12,556,657	Unrated	Unrated
Money market fund	1,465,209	Unrated	Unrated
Total investments	<u>\$46,783,734</u>		

- 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, 2013, 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, 2013, MEDC did not have investments in the fixed income corporate securities for more than 5% of MEDC's total investments with a single issuer.

Note 3 Loans Receivable

Loans receivable held by MEDC as of September 30, 2013 consisted of the following:

Loan Category	Loans Receivable
Urban Land Assembly Fund loans	\$ 5,148,928
Life Sciences Program	327,883
Michigan Core Community Fund Program	6,060,738
Follow-On Fund	3,669,022
Other loans	7,351,789
Total	\$ 22,558,362
Less: Allowance for uncollectible loans	(14,372,260)
Total loans receivable	\$ 8,186,102

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).

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

Capital asset activities for the fiscal year ended September 30, 2013 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	1,419,114	10,403		1,429,517
Capital assets (cost)	\$ 17,581,771	\$ 10,403	\$ 0	\$ 17,592,174
Less accumulated depreciation for:				
Building and improvement	\$ (4,827,805)	\$ (436,608)	\$	\$ (5,264,413)
Furniture	(2,997,422)			(2,997,422)
Non-information technology equipment	(78,265)			(78,265)
Information technology equipment	(1,308,997)	(53,671)		(1,362,668)
Total accumulated depreciation	\$ (9,212,489)	\$ (490,279)	\$ 0	\$ (9,702,768)
Capital assets (net)	\$ 8,469,281	\$ (479,876)	\$ 0	\$ 7,989,406

Note 5 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, 2013:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated absences	\$2,358,529	\$762,600	\$939,827	\$2,181,300	\$1,166,600

## 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. MEDC does not make any contributions to the deferred compensation plans for employees in the State Employees' Defined Benefit Retirement Plan.

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 is funded by the State on a pre-funded basis.

For the State Employees' Defined Benefit Retirement Plan, MEDC paid an average 5.39% of its payroll costs for pension charges and retiree postemployment benefits in fiscal year 2012-13. 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 42.15% of its payroll costs toward other postemployment benefits in fiscal year 2012-13 for most State employees.

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.

Note 7

Related Party Transactions

In November 2012, MEDC provided funds to the Michigan Land Bank Fast Track Authority (a discretely presented component unit of the State of Michigan) to acquire the building housing the Michigan Life Science and Innovation Center (MLSIC) in Plymouth. This building has been used as an incubator center by new innovation companies. MEDC provided \$558,000 to pay off the loan MLSIC had against the building and also forgave a \$250,000 loan made to MLSIC in 2008 toward the purchase of this building. The Michigan Land Bank Fast Track Authority holds the title on the property. The MLSIC continues to be an incubator for life science

companies and, therefore, MEDC continues to be involved with the operations of the building. Income generated from the rent pays all expenses related to building repairs, maintenance, and utilities. MEDC collected approximately \$804,000 in rent and used approximately the same amount for building expenses during fiscal year 2012-13.

# GLOSSARY

## Glossary of Abbreviations and Terms

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.
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.



