

Audit Report

Maryland Economic Development Corporation

January 2016



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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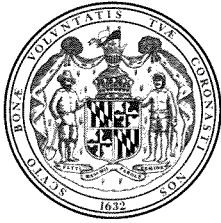
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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
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Warren G. Deschenaux
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Legislative Auditor

January 19, 2016

Senator Guy J. Guzzone, Co-Chair, Joint Audit Committee
Delegate Craig J. Zucker, Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland


Ladies and Gentlemen:

We have conducted a fiscal compliance audit of the Maryland Economic Development Corporation (MEDCO) for the period beginning May 18, 2012 and ending June 30, 2015. MEDCO's purpose is to assist in the expansion, modernization, and retention of existing Maryland businesses and to attract new business to the State.

Our audit did not disclose any findings.

We wish to acknowledge the cooperation extended to us by MEDCO during the course of this audit.

Respectfully submitted,


Thomas J. Barnickel III, CPA
Legislative Auditor

Background Information

Agency Responsibilities and Financial Activity

The Maryland Economic Development Corporation (MEDCO), which functions under the provisions of Title 10, Subtitle 1 of the Economic Development Article of the Annotated Code of Maryland, is constituted as a public instrumentality of the State of Maryland. MEDCO's goal is to assist in the expansion, modernization, and retention of existing Maryland businesses and to attract new businesses to the State. MEDCO also owns and manages certain properties and, upon request, assists local jurisdiction projects, and borrows money and issues bonds for financing this assistance. Since its creation in 1984 through June 30, 2014, MEDCO has undertaken 254 projects.

MEDCO is managed by a 12-member Board of Directors appointed by the Governor. The administrative affairs and technical activities of MEDCO are directed and supervised by an executive director who is appointed by the Board, subject to the approval of the Governor.

According to MEDCO's audited financial statements, as of June 30, 2014 and 2015, MEDCO owned and managed 15 operating facilities and its non-recourse debt totaled \$705 million and \$723 million, respectively. This debt represents obligations related to the operating facilities of MEDCO and is to be retired solely from the operating revenues of the respective facilities. MEDCO is not liable to bondholders and lenders in the event of project/borrower default. The debt consists primarily of revenue bonds issued by MEDCO (which are not obligations of the State of Maryland) and loans from government agencies (for example, the Maryland Department of Commerce).

Based on a review of MEDCO's annual activities report for the fiscal year ending June 30, 2015 and discussions with management personnel, we noted that 2 of its 15 operating facilities were financially troubled. A resort and conference center was classified as a "non-performing" project because its debt service payment was only partially made and certain financial covenants were not met. A student housing project was classified as a "watch" project, in part, because it did not meet its required debt coverage ratio. As a result, MEDCO worked with the parties involved with these projects and engaged management consultants to identify various improvement strategies that are in the process of being implemented.

Organizational Change

Effective October 1, 2015, in accordance with Chapter 141, Laws of Maryland 2015, the principal economic development entities in the State, including MEDCO, were restructured under the newly created Secretary of Commerce. As the Secretary of Commerce already serves on the MEDCO Board of Directors, MEDCO does not anticipate this organizational change having any significant impact on its operations.

Financial Statement Audits

MEDCO engaged an independent accounting firm to audit its financial statements for the fiscal years ended June 30, 2013, 2014, and 2015. In the related audit reports, the firm stated that MEDCO's financial statements present fairly, in all material respects, the financial position of MEDCO and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Status of Finding From Preceding Audit Report

Our audit included a review to determine the status of the finding contained in our preceding audit report dated December 3, 2012. We determined that MEDCO satisfactorily addressed this finding.

Findings and Recommendations

Our audit did not disclose any significant deficiencies in the design or operation of the Maryland Economic Development Corporation's (MEDCO) internal control. Our audit also did not disclose any significant instances of noncompliance with applicable laws, rules, or regulations.

A draft copy of this report was provided to MEDCO. Since there are no recommendations in this report, a written response was not necessary.

Audit Scope, Objectives, and Methodology

We have conducted a fiscal compliance audit of the Maryland Economic Development Corporation (MEDCO) for the period beginning May 18, 2012 and ending June 30, 2015. The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine MEDCO's financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included cash receipts, cash disbursements, and a review of MEDCO projects. We also determined the status of the finding contained in our preceding audit report.

MEDCO engaged an independent accounting firm to audit its financial statements for the fiscal years ended June 30, 2013, 2014, and 2015. In the related audit reports, the firm stated that MEDCO's financial statements present fairly, in all material respects, the financial position of MEDCO and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. We have relied on the work of the independent accounting firm to provide audit coverage pertaining to MEDCO's debt financing and payroll. Our audit procedures in these areas were generally limited, therefore, to obtaining a sufficient basis for that reliance.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, observations of MEDCO's operations, and tests of transactions. Generally, transactions were selected for testing based on auditor judgment, which primarily considers risk. Unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, the results of the tests cannot be used to project those results to the entire population from which the test items were selected. We also performed other auditing procedures that we

considered necessary to achieve our objectives. The reliability of data used in this report for background or informational purposes was not assessed.

MEDCO's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

AUDIT TEAM

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