

State of Michigan

Comprehensive Annual Financial Report



Fiscal Year Ended September 30, 2004
Jennifer M. Granholm, Governor
Prepared by Office of the State Budget

In recognition of its 125th anniversary, we have featured the Michigan State Capitol on the cover and several pages throughout the report.

Construction of the Capitol began in 1872 and was dedicated to the people of Michigan January 1, 1879, for a modest cost of \$1.4 million. In 1992, a three-year project to restore the Capitol to its original glory was successfully completed.

It is one of America's finest examples of Victorian decorative painting. Almost every surface of the inside is hand-painted. The building is a masterpiece of craftsmanship. One of the most spectacular sights in the Capitol is the view of the inner dome from the first floor (photo shown inside).

Today, the Capitol enjoys a well-deserved reputation as one of the nation's most important historic buildings. Every year, over 125,000 individuals, representing every state in the nation and many foreign countries, take guided tours.

This document and other related information may be accessed via the Internet at www.michigan.gov/ofm.

This publication was produced at a cost of \$6,776 for printing or \$7.97 per copy. A total of 850 copies were printed using recycled paper. This report is required by law, Public Act 431 of 1984, as amended.



State of Michigan
Comprehensive Annual Financial Report

Fiscal Year Ended September 30, 2004

JENNIFER M. GRANHOLM
Governor

MARY A. LANNOYE
State Budget Director
Office of the State Budget

MICHAEL J. MOODY, CPA
Director
Office of Financial Management

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Michigan

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STATE OF MICHIGAN

JENNIFER M. GRANHOLM
GOVERNOR

OFFICE OF THE STATE BUDGET
LANSING

MARY A. LANNOYE
DIRECTOR

December 27, 2004

The Honorable Jennifer M. Granholm, Governor
Members of the Legislature
People of the State of Michigan

As required by Article 9, Section 21, of the State Constitution and Section 494, Public Act 431 of 1984, as amended, we are pleased to submit the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)* for the fiscal year ended September 30, 2004.

INTRODUCTION TO THE REPORT

Responsibility: The Office of the State Budget, Office of Financial Management, prepares the SOMCAFR and is responsible for both the accuracy of the data and the completeness and fairness of the presentation, including disclosures. To the best of our knowledge and belief, the information contained in the SOMCAFR is accurate in all material respects and reported in a manner that fairly presents the financial position and results of operations of the State primary government and component units for which it is financially accountable. All disclosures necessary to enable the reader to gain a reasonable understanding of the State's financial affairs have been included.

Adherence to Generally Accepted Accounting Principles: As required by State statute, we have prepared the financial statements contained in the SOMCAFR in accordance with generally accepted accounting principles (GAAP) applicable to state and local governments, as promulgated by the Governmental Accounting Standards Board (GASB). The State also voluntarily follows the recommendations of the Government Finance Officers Association of the United States and Canada (GFOA) for the contents of government financial reports, and participates in the GFOA's review program for the Certificate of Achievement for Excellence in Financial Reporting.

Report: The SOMCAFR is divided into three major sections: introductory, financial, and statistical:

- The introductory section includes this letter, the State's organization chart, and the list of principal officials.
- The financial section includes: the independent auditor's report on the Basic Financial Statements; Management's Discussion and Analysis (MD&A) which provide an introduction, overview, and analysis to the Basic Financial Statements; the Basic Financial Statements, which present the government-wide financial statements and fund

financial statements for governmental funds, proprietary funds, fiduciary funds, and component units, together with footnotes to the Basic Financial Statements; Required Supplementary Information other than MD&A, which presents budgetary comparison schedules and information about infrastructure assets; and the supplemental financial data which includes the combining financial statements and schedules.

- The statistical section includes such items as trend information, information on debt levels, and other selected economic and statistical data.

Internal Control Structure: The Office of the State Budget is responsible for the overall operation of the State's central accounting system and for establishing and maintaining the State's internal control structure. The system of internal control has been designed to provide reasonable rather than absolute assurance that the financial statements are free from material misstatement.

All financial transactions of the State primary government are recorded in the central accounting system, except for the Michigan Unemployment Compensation Funds, Attorney Discipline System, the State Employees' Deferred Compensation Funds, the State Employees' Defined Contribution Retirement Fund, and the Michigan Education Savings Program. Many of the essential control features are decentralized, such as the preparation and entry of expenditure transactions into the central accounting system. Consequently, the Office of the State Budget relies upon the controls in place at the various State departments and agencies.

The Management and Budget Act requires each principal department to appoint an internal auditor and to maintain adequate internal control systems. Each department is also required to periodically report to the Governor on the adequacy of its internal accounting and administrative control systems and, if any material weaknesses exist, to provide corrective action plans and time schedules for addressing such weaknesses. This reporting is required on or before May 1 of each odd numbered year, effective as of the preceding October 1.

The discretely presented component units generally operate outside the State's central accounting system and are responsible for establishing and maintaining their own separate internal control structures.

Independent Auditors: The Office of the Auditor General (OAG) is the principal auditor of the SOMCAFR. The OAG also relies on the opinions of outside public accounting firms, particularly for component unit financial statements (such as the Michigan State Housing Development Authority and 10 of the State's universities), the larger pension and other employee benefit trust funds, and the Unemployment Compensation funds. The purpose of the OAG's audit is to provide reasonable assurance that the Basic Financial Statements for the fiscal year ended September 30, 2004 are free of material misstatements. The OAG concluded that the Basic Financial Statements for the fiscal year ended September 30, 2004 are fairly presented in accordance with GAAP and issued unqualified opinions.

In addition to the annual audit of the SOMCAFR, the OAG also performs periodic financial statement and performance audits of the various State departments, agencies, and institutions of higher education. The Auditor General also has primary responsibility for conducting audits under the federal Single Audit Act of 1984. Pursuant to Michigan Public Act 251 of 1986, these audits are conducted biennially for applicable State departments, agencies and component unit authorities, and result in separately issued audit reports.

Management's Discussion and Analysis (MD&A): GAAP requires that management provide a narrative introduction, overview, and analysis to accompany the Basic Financial Statements in the form of MD&A. This letter of transmittal is intended to complement MD&A and should be read in conjunction with it. The MD&A can be found immediately following the Independent Auditor's Report.

PROFILE OF THE GOVERNMENT

Michigan was admitted to the Union as the 26th state in 1837. The State is governed under the Constitution of 1963, as amended.

Executive Branch: The Executive Branch consists of 19 principal departments. Sixteen principal departments are headed by commissions and/or directors appointed by the elected governor. Two principal departments, Attorney General and State, are headed by elected officials and one, Education, is headed by an elected board.

Judicial Branch: The Judicial Branch consists of the Supreme Court, Court of Appeals, Court of Claims, and the State's circuit, district, probate, and municipal courts. In addition to its judicial duties, the Supreme Court is responsible for the general administrative supervision of all courts in the state. The Supreme Court also establishes rules for practice and procedure in all courts.

Legislative Branch: The Legislative Branch consists of the Senate, House of Representatives, and Office of the Auditor General. The Senate, which consists of 38 elected members, and House of Representatives, which consists of 110 elected members, enact the laws of Michigan. The Office of the Auditor General conducts post financial and performance audits of state government operations

Reporting Entity: The financial reporting entity of the State includes all of the funds of the primary government as

well as component units for which the State's elected officials are financially accountable. The transmittal letter, MD&A, and the financial statements focus on the primary government and its activities. Although information pertaining to the component units is provided, their separately issued financial statements should be read to obtain a complete overview of their financial position.

Budgetary Reporting and Control: For the State primary government operating funds (i.e., the General Fund and annually appropriated special revenue and permanent funds), the State budgets projected revenues and expenditures and calculates fund balance for budgetary purposes in accordance with GAAP. Public Act 431 of 1984, as amended, prohibits the State from budgeting for an ending fund balance deficit in an operating fund. If an actual deficit is incurred, the Constitution and Act 431 require that it be addressed in the subsequent year's budget. If accounting principles change, Act 431 requires the State to also implement such changes in its budgetary process.

Compliance with the final updated budget for the annually budgeted operating funds of the State primary government is demonstrated in the budget and actual comparative schedules and notes in the SOMCAFR. In addition, subsequent to the publication of the SOMCAFR, the State releases "Statewide Authorization Dispositions", a report providing line item appropriation details, the legal level of budgetary control, for the General Fund and budgeted operating funds.

ECONOMIC CONDITIONS AND OUTLOOK

The current U.S. economic recovery is now three years old, having begun in November 2001. Over the past six quarters, real annualized GDP growth has exceeded 3.0 percent each quarter. In five of the past six quarters, consumption growth has been strong and equipment investment has grown at double-digit rates. Light vehicle sales have remained strong throughout the recovery, boosted by record incentives and low financing rates. Supported by historically low interest rates, new and existing home sales have remained strong as well.

However, employment growth lagged the recovery. Employment declined each quarter during the recovery until the fourth quarter of 2003. Employment has grown in each of the past four quarters, but that growth has been uneven. Employment reported tepid growth the last quarter of 2003 and moderate growth in the first quarter of 2004; employment then surged in the second quarter of this year before moderating in the third quarter. Employment recorded a strong increase in October, but employment growth was tepid in November. Continued job growth will be key to sustained economic growth.

Despite recent growth, U.S. payroll employment in November was still about 400,000 jobs below its March 2001 peak. Further, some sectors are still struggling. The manufacturing sector has been particularly hard hit. U.S. manufacturing employment declined for 42 straight months, before reporting solid gains in early 2004. However, in recent months, manufacturing employment has declined slightly. Rapid productivity gains have allowed firms to

reduce payroll employment even as they have continued to increase output.

2004 Michigan Economic Review: Michigan's economy relies heavily on the performance of the manufacturing sector in general and the auto industry specifically. Given extremely weak Big 3 market share along with continued supply rationalization among vehicle suppliers, Michigan's employment performance has been below the national average. Substantial productivity gains in the manufacturing sector and vehicle industry have also contributed to Michigan's sub-par employment performance.

Over the past three years, the annual average for wage and salary employment has fallen. Through October, state employment is down compared to a year ago. From Michigan's employment peak in June 2000 compared to October 2004, Michigan has lost more than 300,000 jobs. By this time after the 1990-1991 recession, Michigan employment had risen nearly 200,000 jobs above its pre-recession peak. Michigan manufacturing employment has declined even more sharply. Since June 2000, Michigan manufacturing employment has fallen by slightly more than 200,000 jobs. However, while both overall and manufacturing employment have trended down since June 2000, the rate of that decline has slowed. Through October, state employment has increased in two of the last three months.

Michigan's annual average unemployment rate for 2003 was 7.3 percent, the highest level since 1992. The most recent monthly unemployment reading in October 2004 was 6.6 percent. The state's unemployment rate is down 1.0 percentage point from a year ago but substantially above its lows, around 3.0 percent, during the expansion of the late 1990s. Wages and salaries grew 0.6 percent year-over-year in the second quarter of 2004. Overall personal income grew 3.1 percent year-over-year in the second quarter.

The Department of Treasury and House and Senate Fiscal Agencies met on December 3, 2004, and reached a consensus for the 2004 and 2005 revenue and economic forecasts. The following summarizes the consensus economic forecast for 2005.

2005 U.S. Consensus Economic Outlook: Conference parties reached agreement on the outlook for several key economic variables. According to the Consensus forecast, real GDP is forecast to grow 3.2 percent in 2005, after growing a projected 4.4 percent in 2004. U.S. light vehicle sales are forecast to continue to be relatively steady with sales expected to be 16.7 million units in 2004 and 16.8 million units in 2005. The import share of those sales is expected to continue to rise, increasing from 19.9 percent in 2003 to 20.1 percent in 2004 and 20.6 percent in 2005. The U.S. unemployment rate is expected to decline from 6.0 percent in 2003 to 5.5 percent in 2004 and 5.4 percent in 2005. Interest rates are projected to rise over the forecast horizon but still remain at historically low levels as the Federal Reserve continues to raise the target federal funds rate at a measured pace. The Treasury bill rate is forecast to rise from 1.4 percent in 2004 to 2.4 percent in 2005. As measured by the consumer price index (CPI), inflation is expected to remain moderate with consumer prices rising a projected 2.6 percent, down slightly from 2.7 percent in 2004.

As businesses gain confidence in the sustainability of the expansion, business investment is expected to remain strong and the labor market is projected to firm up. With a firmer labor market and continued low interest rates, consumption is projected to remain solid. At the same time, higher oil prices, rising interest rates, and an end to the tax cuts will act to slow growth in 2005.

2005 Michigan Consensus Economic Outlook: With continued U.S. economic growth, smaller declines in manufacturing sector employment and improvements in the private non-manufacturing sector, Michigan employment is expected to grow each quarter, with employment gains averaging a modest 8,000 jobs per quarter.

For 2004, employment is estimated to have declined by 49,000 jobs (1.1 percent) – the fourth straight annual Michigan employment decline. With slight growth in 2005, employment is forecast to average 0.3 percent higher than 2004 employment. After falling from 7.3 percent to 6.7 percent in 2004, Michigan's unemployment rate is forecast to rise to 6.9 percent in 2005.

Michigan personal income is projected to rise 4.5 percent in 2005, after increasing an estimated 2.7 percent in 2004. In 2005, wages and salaries income is forecast to grow 3.7 percent after rising slightly (0.7 percent) in 2004. As measured by the Detroit CPI, consumer prices are projected to increase 2.4 percent.

The Department of Treasury and House and Senate Fiscal Agencies will meet again on January 13, 2005, for a Consensus Revenue Estimating Conference. At that conference, the agencies will reach consensus economic and revenue forecasts for 2005 and 2006.

MAJOR INITIATIVES AND FUTURE PROJECTS

Education: Despite tough economic times, the State remains committed to quality education at all age levels. Over \$14.5 billion, or 37 percent, of the State's total FY 2004-2005 budget is devoted to education. This includes funding for early childhood programs, the K-12 system, universities, community colleges, and student financial aid.

As part of its overall goal of improving student achievement, the State continues to place emphasis on learning in the critical preschool years by investing in programs that provide quality early childhood learning, childcare, and parental education. The State has also instituted a program to identify and assist schools that are considered high priority for improvement in academic achievement.

Health and Human Services: Protecting Michigan's most vulnerable citizens is also a high priority. For FY 2004-2005, the two departments primarily responsible for health and human services, the Department of Community Health and Family Independence Agency, account for \$14.1 billion, or 36 percent, of the overall State budget.

While the State administers a variety of health and human services programs, Medicaid is the most extensive, accounting for \$8.6 billion of the FY 2004-2005 budget. These funds allow the State to provide health care services for over 1.3 million low-income citizens.

Economy: State government is committed to growing its economy by sustaining and creating business investment and jobs in Michigan. One of the key initiatives in this area is the Technology Tri-Corridor, which fosters growth in life sciences, advanced automotive technologies, and homeland security industries through funding and resource collaboration, focusing on emerging technology sectors. Financing is available through a competitive proposal process for life sciences, advanced automotive technologies and homeland security companies and researchers.

Other initiatives related to the economy include the Michigan Timely Application and Permit Service (MiTAPS), which provides one-stop shopping for businesses to identify and apply for permits needed to do business in Michigan; the Michigan Broadband Development Authority, which promotes broadband deployment and utilization in Michigan to stimulate economic development and organizational efficiency; and the Cool Cities Pilot Project, aimed at keeping and attracting young, educated, and skilled workers.

Hometown Security: Michigan is now benefiting from the services of 89 additional Michigan State Police Troopers as a result of the recent completion of the 120th Trooper Recruit School. This is the first trooper recruit school held since 2001. With the addition of these troopers, 1,095 troopers are assigned to posts located throughout the state.

Michigan is also in the midst of a variety of efforts to control the growth in the prison population without sacrificing the safety of its citizens. As a result of these efforts, the State has been able to forego the reopening of two closed prisons, saving \$60 million. It also expects to close an additional prison during FY 2004-2005 by shifting prisoners from an older, less cost-efficient facility to a newer, underutilized facility.

Better Government: State government continued to become more efficient during FY 2003-2004 by implementing administrative measures that reduced spending by \$185 million. Most of the savings resulted from ongoing improvements in contracting practices, such as reducing the number of sole source contracts, eliminating contract extensions, and negotiating price reductions. Other examples of savings included continued reductions in the number of cars in the State's fleet, debt restructuring, voluntary

rent reductions for leased facilities, and decreased energy consumption.

The State also streamlined routine human resources, benefits, and payroll functions by opening a centralized service center that provides services and support to State employees in most executive branch departments. Establishment of the centralized service center is expected to save the State \$25 million over the next five years by reducing the number of staff needed in departmental human resources offices.

In order to ensure that Michigan citizens get maximum value for their future tax dollars, the State has modified its budget development process to incorporate a "budgeting for outcomes" approach for the FY 2005-2006 budget year. Budgeting for outcomes differs from the traditional approach by focusing on buying results for citizens rather than cutting or adding to last year's budget. The goal is to get the results citizens need at the price they are willing to pay.

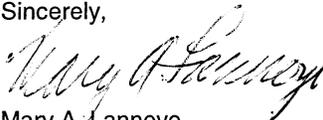
AWARDS AND ACKNOWLEDGEMENTS

Certificate of Achievement: The GFOA awarded a Certificate of Achievement for Excellence in Financial Reporting to the State of Michigan for its SOMCAFR for the year ended September 30, 2003. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report whose content satisfies both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. The State has received a Certificate of Achievement for 17 consecutive years. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

Acknowledgments: The preparation of this report requires the collective efforts of the management and staff of the Accounting and Financial Reporting Division, Office of Financial Management; the chief financial officers, chief accountants, internal auditors and their staffs from all State agencies; and the management and staff of the Office of the Auditor General. We sincerely appreciate the dedicated efforts of all of these individuals that have allowed Michigan to maintain its position as a national leader in quality and efficiency for financial reporting.

Sincerely,



Mary A. Lannoy
State Budget Director



Michael J. Moody, CPA
Director, Office of Financial Management

Certificate of Achievement for Excellence in Financial Reporting

Presented to

State of Michigan

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
September 30, 2003

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



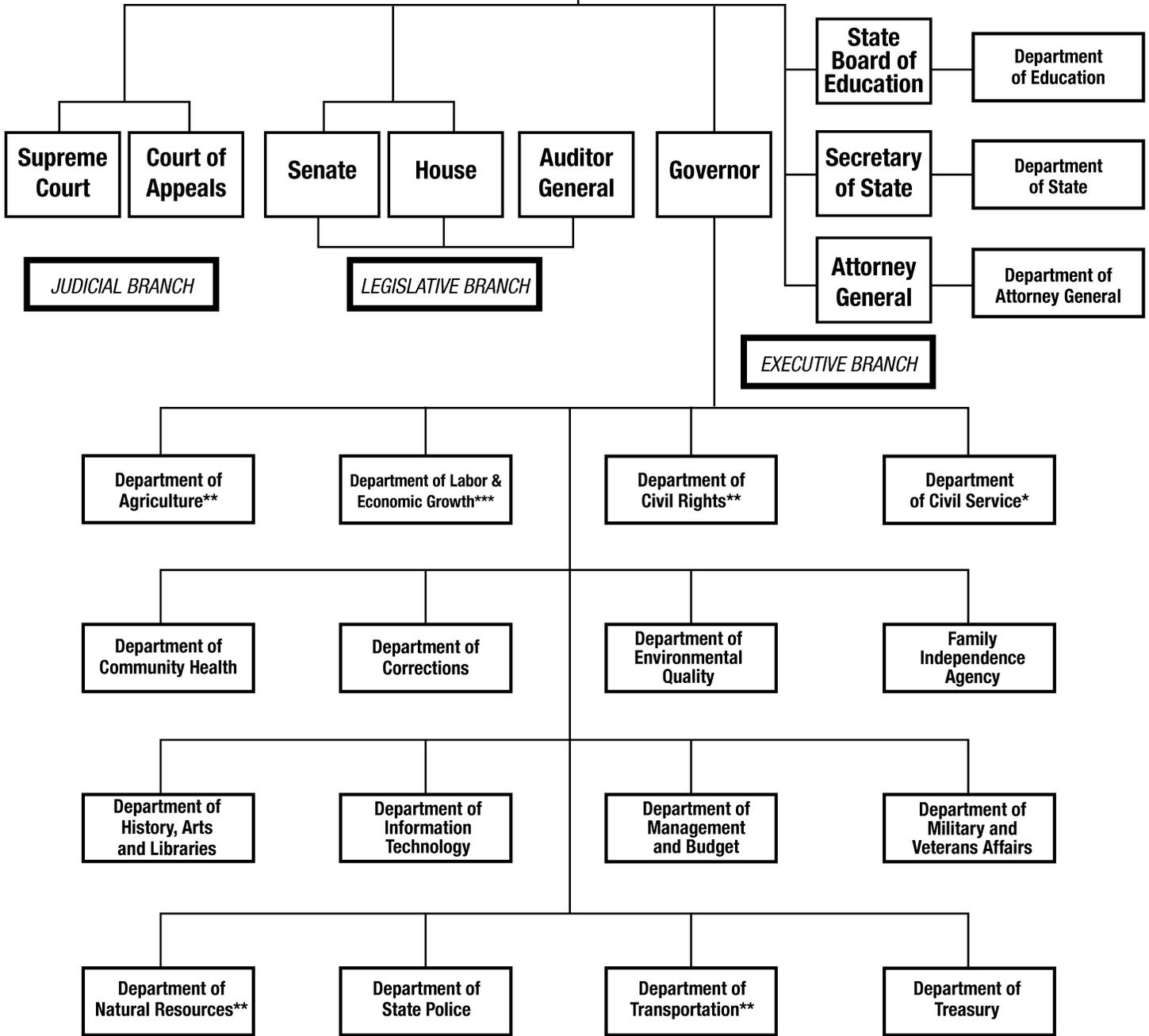
Nancy L. Zielle

President

Jeffrey R. Enos

Executive Director

STATE OF MICHIGAN ORGANIZATIONAL STRUCTURE



* Has Commission appointed by Governor
 ** Has Commission appointed by Governor, confirmed by Senate
 *** Formerly the Department of Career Development and Department of Consumer & Industry Services

STATE OF MICHIGAN
PRINCIPAL STATE OFFICIALS

JUDICIAL BRANCH

Supreme Court Justices
Honorable Maura D. Corrigan, Chief Justice
Honorable Michael F. Cavanagh, Justice
Honorable Marilyn Kelly, Justice
Honorable Stephen J. Markman, Justice
Honorable Clifford W. Taylor, Justice
Honorable Elizabeth A. Weaver, Justice
Honorable Robert P. Young, Jr., Justice

LEGISLATIVE BRANCH

Honorable Kenneth R. Sikkema
Majority Leader of the Senate

Honorable Rick V. Johnson
Speaker of the House of Representatives

Thomas H. McTavish
Legislative Auditor General

EXECUTIVE BRANCH

Honorable Jennifer M. Granholm, Governor

Honorable John D. Cherry Jr., Lt. Governor

Honorable Mike Cox, Attorney General

Honorable Terri Lynn Land, Secretary of State

State Board of Education
Kathleen N. Straus, President
John C. Austin
Elizabeth W. Bauer
Carolyn L. Curtin
Marianne Yared McGuire
Herbert S. Moyer
Reginald M. Turner
Eileen L. Weiser
Honorable Jennifer M. Granholm (Ex Officio)
Thomas D. Watkins, Jr.
Superintendent of Public Instruction

Michigan Commission of Agriculture
William Pridgeon, Chair
James E. Byrum
Douglas E. Darling
Ann Jousma-Miller
James E. Maitland
Dan Wyant, Director, Department of Agriculture

Civil Rights Commission
Gary Torgow, Chair
Mohammed Abdrabboh
Mark Bernstein
Albert Calille
Tarun K. Sharma
Valerie P. Simmons
Margaret M. Van Houten
Linda V. Parker, Director, Department of Civil Rights

Civil Service Commission
Susan Grimes Munsell, Chair
F. Thomas Lewand
Sherry L. McMillan
James P. Pitz
James D. Farrell, Director, Department of Civil Service

Janet Olszewski, Director
Department of Community Health

David C. Hollister, Director
Department of Labor and Economic Growth

Patricia L. Caruso, Director
Department of Corrections

Steven E. Chester, Director
Department of Environmental Quality

Marianne Udow, Director
Family Independence Agency

William Anderson, Director
Department of History, Arts and Libraries

Teresa M. Takai, Director
Department of Information Technology

Mitch Irwin, Director
Department of Management and Budget

Mary A. Lannoye, State Budget Director
Office of the State Budget

Major General Thomas G. Cutler, Director
Department of Military and Veterans Affairs

Natural Resources Commission

Keith J. Charters, Chair
Mary C. Brown
Bob Garner
Gerald R. Hall Jr.
John M. Madigan
Franklin C. Wheatlake
Vacant

Rebecca A. Humphries, Director
Department of Natural Resources

Col. Tadarial J. Sturdivant, Director
Department of State Police

Transportation Commission
Ted B. Wahby, Chair
Linda Miller Atkinson
Betty Jean Awrey
Robert Bender
Vincent Brennan
John W. Garside
Gloria J. Jeff, Director
Department of Transportation

Jay B. Rising, State Treasurer



Senate Chamber from Entry



House of Representatives Chamber



II FINANCIAL SECTION

INDEPENDENT AUDITOR'S REPORT MANAGEMENT'S DISCUSSION AND ANALYSIS BASIC FINANCIAL STATEMENTS



STATE OF MICHIGAN
 OFFICE OF THE AUDITOR GENERAL
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 LANSING, MICHIGAN 48913
 (517) 334-8050
 FAX (517) 334-8079

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

Independent Auditor's Report

The Honorable Jennifer M. Granholm, Governor
 Members of the Legislature

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Michigan, principally as of and for the year ended September 30, 2004, which collectively comprise the State's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the State's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the State Lottery Fund, Michigan Unemployment Compensation Funds, Michigan Employment Security Act - Administration Fund, State Building Authority - Debt Service Fund, State Building Authority - Capital Projects Fund, Attorney Discipline System, State Sponsored Group Insurance Fund, State Employees' Deferred Compensation Funds, State Police Retirement Fund, State Employees' Retirement Fund, Public School Employees' Retirement Fund, Judges' Retirement Fund, State Employees' Defined Contribution Retirement Fund, Michigan Education Savings Program, Michigan State Housing Development Authority, Michigan Municipal Bond Authority, Mackinac Bridge Authority, Mackinac Island State Park Commission, Michigan Higher Education Assistance Authority, Michigan Higher Education Facilities Authority, Michigan Higher Education Student Loan Authority, Michigan State Hospital Finance Authority, State Bar of Michigan, Central Michigan University, Western Michigan University, Eastern Michigan University, Ferris State University, Grand Valley State University, Lake Superior State University, Michigan Technological University, Northern Michigan University, Oakland University, and Saginaw Valley State University. Those financial statements reflect total assets and revenues or additions of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information as follows:

<u>Opinion Unit</u>	<u>Percent of Total Assets</u>	<u>Percent of Total Revenues/Additions</u>
Governmental Activities	2.0%	1.5%
Business-Type Activities	98.3%	85.0%
Aggregate Discretely Presented Component Units	92.2%	94.6%
State Lottery Fund	100.0%	100.0%
Michigan Unemployment Compensation Funds	100.0%	100.0%
Aggregate Remaining Fund Information	92.5%	64.3%

Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for these component units and funds, are based solely upon the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the



STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL

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

The Honorable Jennifer M. Granholm, Governor
Members of the Legislature
Page 2

accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Michigan, as of September 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 4 to the basic financial statements, the State of Michigan adopted Governmental Accounting Standards Board Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, and Governmental Accounting Standards Board Technical Bulletin No. 2004-1, *Tobacco Settlement Recognition and Financial Reporting Entity Issues*.

The management's discussion and analysis on pages 5 through 12, budgetary comparison schedules and corresponding notes on pages 86 through 89, and information about infrastructure assets reported using the modified approach on pages 90 and 91 are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We and the other auditors have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State of Michigan's basic financial statements. The combining and individual fund statements and schedules - non-major funds listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. These statements and schedules have been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, in our opinion, based on our audit and the reports of other auditors, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections listed in the table of contents have not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Sincerely,

Thomas H. McTavish, C.P.A.
Auditor General
December 27, 2004



MANAGEMENT'S DISCUSSION AND ANALYSIS

The following is a discussion and analysis of the State of Michigan's (the State's) financial performance, providing an overview of the activities for the fiscal year ended September 30, 2004. Please read it in conjunction with the transmittal letter at the front of this report and with the State's financial statements, which follow this section.

HIGHLIGHTS

Government-wide:

- At September 30, 2004, the State's assets exceeded its liabilities by \$17.2 billion.
- The State's unrestricted net assets were (\$954.8) million as of the close of the year. A positive balance in unrestricted net assets represents excess assets available to meet ongoing obligations. A negative balance means that it would be necessary to convert restricted assets to unrestricted assets if all ongoing obligations were immediately due and payable.
- The State's total net assets decreased by \$1.0 billion (5.7 percent) during fiscal year 2003-2004.

Fund Level:

- As of the close of the fiscal year, the State's governmental funds reported combined ending fund balances of \$3.3 billion. Of this amount, \$495.5 million is *unreserved fund balance* and, therefore, available to fund general-purpose expenditures of the respective funds in future years. The remaining \$2.8 billion is reserved for specific purposes, such as education and transportation.
- The State's three major governmental funds, the General Fund, Counter-Cyclical Budget and Economic Stabilization Fund, and the School Aid Fund, all closed the fiscal year with positive fund balances, totaling a combined \$1.3 billion. In the General Fund and School Aid Fund, the entire fund balance, \$1.2 billion and \$74.1 million, respectively, is reserved for specific purposes. In the Counter-Cyclical Budget and Economic Stabilization Fund, the entire fund balance of \$81.3 million is unreserved.
- The State's proprietary funds reported net assets at year-end of \$1.3 billion. This represents a decrease of \$602.8 million (31.8 percent) compared to the prior year-end.

Long-term Debt:

- The State's total long-term debt (bonds and notes payable) as of September 30, 2004 was \$6.2 billion. This is an increase of \$255.1 million since the last fiscal year-end. The increase represents the net difference between new issuances, payments, and refundings of outstanding debt.

More detailed information regarding the government-wide, fund level, and long-term debt activities can be found beginning on page 7.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is an introduction to the State's basic financial statements, which comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.

Government-wide Statements (Reporting the State as a Whole)

The Statement of Net Assets and the Statement of Activities are two financial statements that report information about the State, as a whole, and about its activities that should help answer this question: How has the State's financial position, as a whole, changed as a result of this year's activities? These statements include all non-fiduciary assets and liabilities using the accrual basis of accounting. The current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The Statement of Net Assets (pages 14 and 15) presents all of the State's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases and decreases in net assets measure whether the State's financial position is improving or not.

The Statement of Activities (pages 16 and 17) presents information showing how the State's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying events giving rise to the change occur, regardless of the timing of related cash flows. Therefore, revenues and expenses are reported in these statements for some items that will only result in cash flows in future fiscal periods (e.g. uncollected taxes and earned but unused vacation leave).

Both statements report three activities:

- *Governmental Activities* – Most of the State's basic services are reported under this category. Taxes and intergovernmental revenues generally fund these services. The Legislature, the Judiciary, and the general operations of the Executive departments fall within the governmental activities.
- *Business-type Activities* – The State charges fees to customers to help it cover all or most of the cost of certain services it provides. Lottery tickets, liquor purchases, and the State's unemployment compensation services are examples of business-type activities.
- *Discretely Presented Component Units* – Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. The State has 14 authorities and 10 universities that are reported as discretely presented component units of the State.

This report includes two schedules (pages 21 and 23) that reconcile the amounts reported on the governmental fund financial statements (modified accrual accounting) with governmental activities (accrual accounting) on the appropriate government-wide statements. The following summarizes the impact of transitioning from modified accrual to accrual accounting:

- Capital assets used in governmental activities are not reported on governmental fund statements.
- Certain tax revenues that are earned, but not available, are reported as governmental activities, but are reported as deferred revenue on the governmental fund statements.
- Other long-term assets that are not available to pay for current period expenditures are deferred in governmental fund statements, but not deferred on the government-wide statements.
- Internal service funds are reported as governmental activities, but reported as proprietary funds in the fund financial statements.
- Certain pension trust funds have been funded in excess of their annual required contribution. These assets are recorded only in the government-wide statements.
- Deferred issue costs are capitalized and amortized as governmental activities, but reported as expenditures in the governmental fund statements.
- Unless due and payable, long-term liabilities, such as capital lease obligations, compensated absences, litigation, bonds and notes payable, and others only appear as liabilities in the government-wide statements.
- Capital outlay spending results in capital assets on the government-wide statements, but are reported as expenditures on the governmental fund statements.
- Bond and note proceeds result in liabilities on the government-wide statements, but are recorded as other financing sources on the governmental fund statements.
- Certain other outflows represent either increases or decreases in liabilities on the government-wide statements, but are reported as expenditures on the governmental fund statements.

The Notes to the Basic Financial Statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes can be found beginning on page 41 of this report.

Fund Financial Statements (Reporting the State's Major Funds)

The fund financial statements begin on page 20 and provide detailed information about the major individual funds. A fund is a fiscal and accounting entity with a self-balancing set of accounts that the State uses to keep track of specific sources of funding and spending for a particular purpose. In addition to the major funds, page 96 begins the individual fund data for the non-major funds. The State's funds are divided into three categories – governmental, proprietary, and fiduciary – and use different accounting approaches.

- *Governmental funds* -- Most of the State's basic services are reported in the governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for future spending. The governmental fund financial statements provide a detailed short-term view of the State's general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial

resources that can be spent in the near future to finance the State's programs. These funds are reported using *modified accrual* accounting, which measures cash and all other financial assets that can readily be converted to cash. Governmental funds include the General Fund and special revenue, capital project, debt service, and permanent funds.

- *Proprietary funds* -- When the State charges customers for the services it provides, whether to outside customers or to other agencies within the State, these services are generally reported in proprietary funds. Proprietary funds (enterprise and internal service) utilize accrual accounting, the same method used by private sector businesses. Enterprise funds report activities that provide supplies and services to the general public. An example is the State Lottery Fund. Internal service funds report activities that provide supplies and services for the State's other programs and activities - such as the State's Vehicle and Travel Services. Internal service funds are reported as governmental activities on the government-wide statements.
- *Fiduciary funds* -- The State acts as a trustee or fiduciary for its employee pension plans. It is also responsible for other assets that, because of a trust arrangement, can be used only for the trust beneficiaries. The State's fiduciary activities are reported in separate Statements of Fiduciary Net Assets and Changes in Fiduciary Net Assets beginning on page 32. These funds, which include pension (and other employee benefit), private-purpose, and agency funds, are reported using accrual accounting. The government-wide statements exclude fiduciary fund activities and balances because these assets are restricted in purpose and do not represent discretionary assets of the State to finance its operations.

Additional Required Supplementary Information

Following the basic financial statements is additional Required Supplementary Information that further explains and supports the information in the financial statements. The Required Supplementary Information includes budgetary comparison schedules reconciling the statutory and generally accepted accounting principles (GAAP) fund balances at fiscal year-end, and condition and maintenance data regarding certain portions of the State's infrastructure.

Other Supplementary Information

Other supplementary information includes combining financial statements for non-major governmental, proprietary, and fiduciary funds, and non-major discretely presented component units. These funds are added together, by fund type, and presented in single columns in the basic financial statements, but are not reported individually, as with major funds, on the governmental fund financial statements.

FINANCIAL ANALYSIS OF THE GOVERNMENT AS A WHOLE

The State's combined net assets decreased \$1.0 billion (5.7 percent) over the course of this fiscal year's operations. The net assets of the governmental activities decreased \$437.7 million (2.7 percent) and business-type activities had a decrease of \$600.5 million (or 33.9 percent).

	Changes in Net Assets For Fiscal Year Ending September 30 (In Millions)					
	Governmental Activities		Business-type Activities		Total Primary Government	
	2004	2003 *	2004	2003 *	2004	2003*
Current and other non-current assets	\$ 9,601.8	\$ 9,368.1	\$2,189.2	\$2,860.3	\$11,791.0	\$12,228.4
Capital assets	18,694.8	18,669.0	.6	.6	18,695.4	18,669.6
Total assets	<u>28,296.6</u>	<u>28,037.1</u>	<u>2,189.8</u>	<u>2,860.9</u>	<u>30,486.4</u>	<u>30,898.0</u>
Current liabilities	4,359.5	4,042.1	543.2	551.9	4,902.7	4,594.0
Long-term liabilities	7,941.5	7,561.8	475.6	537.4	8,417.1	8,099.1
Total liabilities	<u>12,301.1</u>	<u>11,603.9</u>	<u>1,018.8</u>	<u>1,089.3</u>	<u>13,319.9</u>	<u>12,693.2</u>
Net assets:						
Invested in capital assets, net of related debt	14,962.9	14,996.9	.6	.6	14,963.5	14,997.5
Restricted	1,993.3	1,886.3	1,164.5	1,765.7	3,157.9	3,652.0
Unrestricted	(960.7)	(450.0)	5.9	5.3	(954.8)	(444.7)
Total net assets	<u>\$15,995.6</u>	<u>\$16,433.3</u>	<u>\$1,171.0</u>	<u>\$1,771.5</u>	<u>\$17,166.6</u>	<u>\$18,204.8</u>

* The prior year columns have been restated to reflect the implementation of GASB Technical Bulletin 2004-1 and the addition of the Attorney Discipline System.

Michigan

- The largest component, \$15.0 billion, of the State's net assets reflects its investment in capital assets (e.g. land, buildings, equipment, infrastructure, and others), less any related debt outstanding that was needed to acquire or construct the assets. Restricted net assets are the next largest component, comprising \$3.2 billion. These represent resources that are subject to external restrictions, constitutional provisions, or enabling legislation on how they can be used. The State's unrestricted net assets were (\$954.8) million as of the close of the year. A positive balance in unrestricted net assets represents excess assets available to meet ongoing obligations. A negative balance means that it would be necessary to convert restricted assets to unrestricted assets if all ongoing obligations were immediately due and payable.

The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the State's net assets changed during the fiscal year:

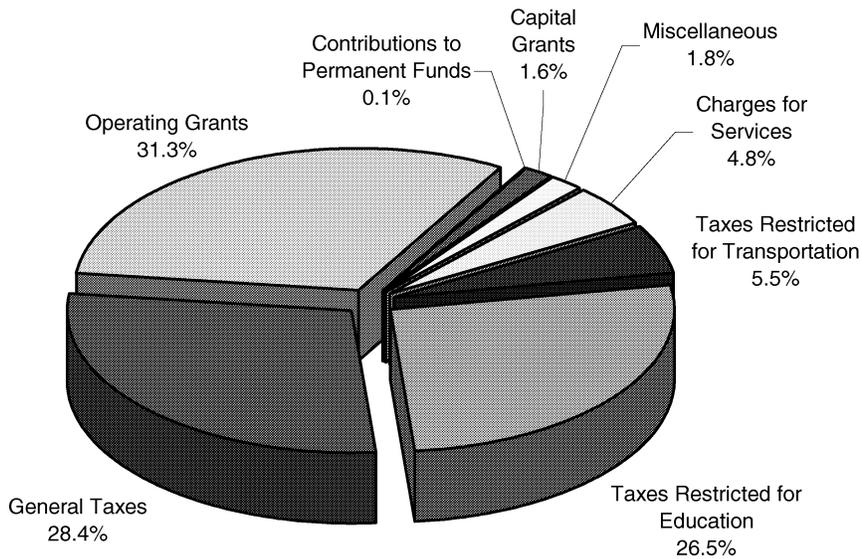
Changes in Net Assets For Fiscal Year Ending September 30 (In Millions)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2004	2003	2004	2003	2004	2003
Revenues						
Program revenues						
Charges for services	\$ 1,801.4	\$ 1,782.9	\$4,500.6	\$4,039.8	\$6,302.0	\$5,822.7
Operating grants	11,783.5	11,290.7	76.8	135.1	11,860.2	11,425.8
Capital grants	618.4	546.7	-	-	618.4	546.7
General revenues						
General taxes	10,672.9	10,133.7	12.0	11.3	10,684.9	10,145.0
Taxes restricted for educational purposes	9,958.3	10,098.3	-	-	9,958.3	10,098.3
Taxes restricted for transportation purposes	2,077.0	2,021.1	-	-	2,077.0	2,021.1
Unrestricted investment and interest earnings	9.7	14.1	1.2	1.1	11.0	15.2
Miscellaneous	677.8	813.6	-	-	677.8	813.6
Total revenues	<u>37,599.1</u>	<u>36,701.1</u>	<u>4,590.6</u>	<u>4,187.4</u>	<u>42,189.7</u>	<u>40,888.5</u>
Expenses						
General government	1,748.6	1,714.8	-	-	1,748.6	1,714.8
Education	14,418.9	14,840.0	-	-	14,418.9	14,840.0
Family independence services	3,985.9	3,891.7	-	-	3,985.9	3,891.7
Public safety and corrections	2,256.4	2,159.5	-	-	2,256.4	2,159.5
Conservation, environment, recreation, and agriculture	674.4	612.6	-	-	674.4	612.6
Labor, commerce, and regulatory	920.1	901.6	-	-	920.1	901.6
Health services	9,605.2	9,362.9	-	-	9,605.2	9,362.9
Transportation	3,104.8	2,792.8	-	-	3,104.8	2,792.8
Tax expenditures	702.7	707.8	-	-	702.7	707.8
Intergovernmental - revenue sharing	1,305.1	1,451.4	-	-	1,305.1	1,451.4
Interest on long-term debt	247.0	281.4	-	-	247.0	281.4
Liquor Purchase Revolving Fund	-	-	544.7	515.2	544.7	515.2
State Lottery Fund	-	-	1,391.4	1,152.8	1,391.4	1,152.8
Attorney Discipline System	-	-	4.1	-	4.1	-
Michigan Unemployment Compensation Funds	-	-	2,349.4	2,473.8	2,349.4	2,473.8
Total expenses	<u>38,969.1</u>	<u>38,716.4</u>	<u>4,289.5</u>	<u>4,141.8</u>	<u>43,258.6</u>	<u>42,858.2</u>
Excess (deficiency) Before Contributions and Transfers	(1,370.0)	(2,015.3)	301.1	45.5	(1,068.9)	(1,969.8)
Contributions to permanent fund principal	30.8	31.9	-	-	30.8	31.9
Transfers	901.6	843.8	(901.6)	(843.8)	-	-
Increase (decrease) in net assets	<u>(437.7)</u>	<u>(1,139.6)</u>	<u>(600.5)</u>	<u>(798.2)</u>	<u>(1,038.2)</u>	<u>(1,937.8)</u>
Net assets – beginning restated	16,433.3	17,572.9	1,771.5	2,569.8	18,204.8	20,142.6
Net assets – ending	<u>\$15,995.6</u>	<u>\$16,433.3</u>	<u>\$1,171.0</u>	<u>\$1,771.5</u>	<u>\$17,166.6</u>	<u>\$18,204.8</u>

Governmental Activities:

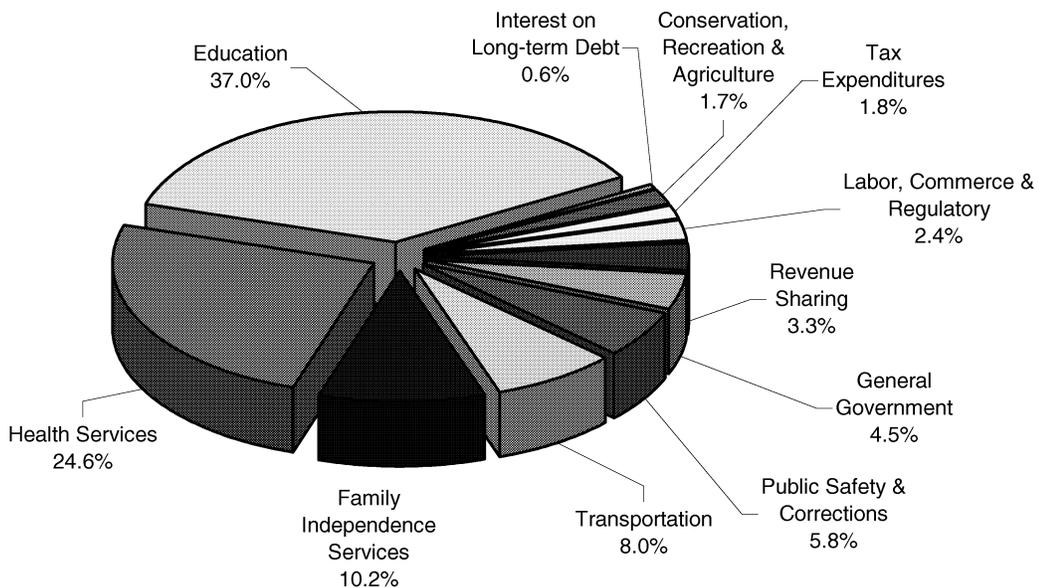
The following chart depicts revenues of the governmental activities for the fiscal year:

**Revenues - Governmental Activities for
Fiscal Year Ending September 30, 2004**
(\$37.6 billion)



The following chart depicts expenses of the governmental activities for the fiscal year:

**Expenses - Governmental Activities for
Fiscal Year Ending September 30, 2004**
(\$39.0 billion)



Business-type Activities

The business-type activities' net assets decreased by \$600.5 million (33.9 percent) during the fiscal year. Factors contributing to these results included:

- The increase in unemployment in the State resulted in the Michigan Unemployment Compensation Funds finishing the fiscal year with a decrease in net assets of \$573.1 million (34.5 percent) to \$1.1 billion.
- The State Lottery Fund's net assets decreased by \$28.1 million (26.7 percent), which resulted from a decrease in the market value of investments that Lottery holds to fund future payments due for lottery prizes.

FINANCIAL ANALYSIS OF THE STATE'S FUNDS

As the State completed the year, its governmental funds reported fund balances of \$3.3 billion. Of this total amount, \$495.5 million constitutes unreserved fund balance, which is available for appropriation for the general purposes of the funds. The Budget Stabilization Fund (\$81.3 million) and the transportation-related funds (\$337.1 million) comprise a significant portion of the unreserved fund balance. The remainder of fund balance is reserved and is not available for new spending because it has already been dedicated for various commitments, such as capital outlay projects.

General Fund

The General Fund is the chief operating fund of the State. At the end of fiscal year 2003-2004, the General Fund unreserved fund balance was transferred to the Budget Stabilization Fund and reserved fund balance was \$1.2 billion. Total fund balance diminished during the fiscal year by \$140.9 million (10.8 percent), primarily because transfers to other funds increased by \$120.8 million.

General Fund Budgetary Highlights:

During fiscal year 2004, the State was again faced with difficult budget challenges resulting in significant expenditure reductions. In December 2003, Executive Order 2003-23 was issued authorizing expenditure reductions of \$200.9 million and transfers of unexpended balances and excess revenues from restricted revenue sources totaling \$147.9 million to be used as general fund, general purpose revenues. In addition, the executive order reduced work project and capital outlay project carry-forward authorization from prior years by \$31.0 million.

In addition to the executive order spending reductions, the original budget was amended by various supplemental appropriations and appropriation reductions. The following summarizes the differences between the original and final budget amounts:

- General purpose tax revenues of \$7.9 billion were \$101.4 million less than the original estimate of \$8.0 billion.
- Restricted revenue inflows of \$13.6 billion were \$312.9 million more than the estimated \$13.3 billion.
- The Merit Award Trust Fund made transfers to the General Fund totaling \$63.0 million as part of the Executive Order 2003-23.
- The General Fund transferred \$81.3 million to the Budget Stabilization Fund at the end of the year.

Differences between the final budget and actual spending result from spending authority lapses of \$122.7 million and restricted revenue authorized but not spent of \$8.9 million.

The Department of Community Health finished the year with a net overexpenditure of \$38.2 million and the Family Independence Agency had line-item overexpenditures of \$1.1 million. All other agencies finished the year with lapses.

In December 2004, the consensus revenue agreement indicated that the General Fund revenues are expected to decline in the next fiscal year. Another consensus revenue conference will be held in January 2005. Corresponding reductions in spending and other measures will help ensure that the fund balance remains positive if revenues decline as expected.

School Aid Fund

Fund balance at September 30, 2004, totaled \$74.1 million, a decrease of \$41.1 million (35.7 percent) from the prior year. Revenues and transfers to the fund totaled \$12.3 billion. Expenditures to school districts and other costs decreased by \$43.5 million from the previous year and totaled \$12.3 billion. During the year, the School Aid budget was adjusted by prorating school aid payments. The school aid payments were reduced by \$131.1 million.

Counter-cyclical Budget and Economic Stabilization Fund

Fund balance increased by \$81.3 from the previous year as a result of the transfer from the General Fund.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets: At the end of the fiscal year 2003-2004, the State had invested \$18.7 billion, net of accumulated depreciation, in a broad range of capital assets (see the table below). Depreciation charges for this fiscal year totaled \$182.6 million.

Capital Assets as of September 30
(Net of Depreciation, In Millions)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2004	2003	2004	2003	2004	2003
Land	\$ 3,117.0	\$ 3,103.1	\$ -	\$ -	\$ 3,117.0	\$ 3,103.1
Land improvement	86.5	75.7	-	-	86.5	75.7
Buildings and improvements	2,047.4	2,088.2	-	-	2,047.4	2,088.2
Equipment	144.5	163.9	.6	.6	145.0	164.4
Infrastructure	11,964.6	11,831.3	-	-	11,964.6	11,831.3
Other	19.8	18.9	-	-	19.8	18.9
Subtotal	17,379.8	17,281.0	.6	.6	17,380.4	17,281.6
Construction in progress	1,315.0	1,388.0	-	-	1,315.0	1,388.0
Total	\$18,694.8	\$18,669.0	\$.6	\$.6	\$18,695.4	\$18,669.6

The most significant impact on capital assets during the year resulted from the road and bridge construction and repair projects.

As allowed by GASB Statement No. 34, the State has adopted an alternative process for recording depreciation expense on selected infrastructure assets. Under this alternative method, referred to as the modified approach, the State expenses certain maintenance and preservation costs and does not report depreciation expense. Assets accounted for under the modified approach include the State's network of public transportation roads and bridges, including ancillary assets, such as guard rails, signs, lighting, culverts, fencing, and the like. The State is responsible for maintaining approximately 27,534 lane miles of roads and 4,724 bridges (spans in excess of 20 feet).

The State has consistently improved the assessed condition of roads over the past five years. The State's goal is to have no more than 30% of roads in "poor" or "very poor" condition. The most recent condition assessment, completed for calendar year 2003, indicated that 20.0% of roads were considered poor or very poor.

The State's bridges have assessed conditions that are better than the established benchmarks. The most recent assessment (2003) indicated that the condition of the bridges had improved from the condition reported for 2002.

The State's fiscal year 2004-2005 capital outlay appropriations have not been enacted except for the rent payments made to the State Building Authority totaling \$250.8 million. Unspent capital outlay authorizations of \$463.0 million that existed at September 30, 2004, are available in fiscal year 2005. More detailed information about the State's capital assets is presented in Note 9 to the financial statements.

Long-term Debt: The State, along with the State Building Authority (SBA), a blended component unit of the State, are empowered by law to authorize, issue, and sell debt obligations. General obligation bonds, issued by the State, are backed by the full faith and credit of the State. The State also issues revenue dedicated bonded debt, whose payment for principal and interest comes solely out of funds that receive legally restricted revenues. The State is not legally obligated for the debt issued by SBA. SBA's bonds generate revenue to finance the construction of facilities used by the State and universities. Revenues derived from leases on the facilities fund the debt service requirements. More detailed information regarding the State's long-term obligations is presented in Notes 12 and 14 to the financial statements.

Michigan

Outstanding Bonded Debt as of September 30 (In Millions)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2004	2003	2004	2003	2004	2003
General obligation bonds (backed by the State)	\$1,527.5	\$1,413.4	\$ -	\$ -	\$1,527.5	\$1,413.4
Revenue bonds and notes (backed by specific tax and fee revenues)	3,987.7	3,919.6	-	-	3,987.7	3,919.6
Total	\$5,515.2	\$5,333.0	\$ -	\$ -	\$5,515.2	\$5,333.0

During fiscal year 2003-2004 the State issued general obligation debt totaling \$302.8 million, including \$64.5 million for conservation and recreation projects (the Clean Michigan Initiative) and \$238.3 million to provide funds for loans to school districts.

Bond Ratings

The State's general obligations are rated AA+ by Standard & Poors and Aa1 by Moody's.

Limitations on Debt

The State Constitution authorizes general obligation long-term borrowing, with approval of the Legislature and a majority of the voters, and general obligation short-term notes, of which the principal may not exceed 15% of undedicated revenues received in the preceding year. In fiscal year 2003-2004 the State issued and repaid short-term borrowing totaling \$1.3 billion.

ECONOMIC CONDITION AND OUTLOOK

Michigan's economy relies heavily on the performance of the manufacturing sector in general and the auto industry specifically. Given extremely weak manufacturing employment performance, declining vehicle production, continued declines in Big 3 market share along with continued supply rationalization among vehicle suppliers, Michigan's employment performance has been below the national average. Substantial productivity gains in the manufacturing sector and vehicle industry have also contributed to Michigan's sub-par employment performance.

Through October, state employment is down compared to a year ago. From Michigan's employment peak in June 2000 compared to October 2004, Michigan has lost more than 300,000 jobs. By this time after the 1990-1991 recession, Michigan employment had risen nearly 200,000 jobs above its pre-recession peak. Michigan manufacturing employment has declined even more sharply. Since June 2000, Michigan manufacturing employment has fallen by slightly more than 200,000 jobs.

However, with continued U.S. economic growth, smaller declines in manufacturing sector employment and improvements in the private non-manufacturing sector, Michigan employment is expected to grow each quarter, with employment gains averaging a modest 8,000 jobs per quarter. For 2004, employment is estimated to have declined by 49,000 jobs (1.1 percent) – the fourth straight annual Michigan employment decline. With slight growth in 2005, employment is forecast to average 0.3 percent higher than 2004 employment. After falling from 7.3 percent to 6.7 percent in 2004, Michigan's unemployment rate is forecast to rise to 6.9 percent in 2005.

Michigan personal income is projected to rise 4.5 percent in 2005, after increasing an estimated 2.7 percent in 2004. In 2005, wages and salaries income is forecast to grow 3.7 percent after rising slightly (0.7 percent) in 2004. As measured by the Detroit CPI, consumer prices are projected to increase 2.4 percent.

CONTACTING THE STATE'S OFFICE OF FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the State's finances and to demonstrate the State's accountability for the money it receives. Additional copies of this report and other financial information can be obtained by visiting the Office of Financial Management website at www.michigan.gov/ofm. You can also contact the office by phone at (517) 373-3029.

The State's component units issue their own separately issued audited financial statements. These statements may be obtained by directly contacting the component unit. To obtain their phone numbers, you may contact the Office of Financial Management at (517) 373-3029.



BASIC FINANCIAL STATEMENTS

Michigan

STATEMENT OF NET ASSETS

SEPTEMBER 30, 2004

(In Thousands)

	PRIMARY GOVERNMENT			COMPONENT UNITS
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTALS	
ASSETS				
Current Assets:				
Cash	\$ 13,323	\$ 5,245	\$ 18,568	\$ 670,035
Equity in common cash (Note 5)	1,554,396	71,357	1,625,754	75,128
Taxes, interest, and penalties receivable (Note 6)	4,444,613	-	4,444,613	-
Internal balances	27,937	(27,937)	-	-
Amounts due from component units	3,963	730	4,693	239
Amounts due from primary government	-	-	-	178,713
Amounts due from federal government	898,175	1,682	899,857	28,919
Amounts due from local units	204,408	39,288	243,696	907,370
Inventories	42,247	7,251	49,498	15,660
Investments (Note 8)	439,512	1,029,597	1,469,108	1,027,279
Securities lending collateral (Note 8)	21,775	301,950	323,724	-
Other current assets	558,314	249,946	808,260	392,407
Total Current Assets	<u>8,208,662</u>	<u>1,679,109</u>	<u>9,887,771</u>	<u>3,295,749</u>
Restricted Assets:				
Cash and cash equivalents	-	-	-	17,281
Investments	-	-	-	380,354
Mortgages and loans receivable	-	-	-	45,365
Taxes, interest, and penalties receivable (Note 6)	271,994	-	271,994	-
Amounts due from federal government	2,201	-	2,201	-
Amounts due from local units	666,998	-	666,998	2,324,057
Mortgages and loans receivable	-	-	-	3,023,054
Investments (Note 8)	380,908	496,824	877,732	3,107,403
Capital Assets (Note 9):				
Land and other non-depreciable assets	3,153,972	-	3,153,972	95,757
Buildings, equipment, and other depreciable assets	4,593,772	4,834	4,598,606	4,071,388
Less accumulated depreciation	(2,067,291)	(4,268)	(2,071,559)	(1,505,094)
Infrastructure	11,699,350	-	11,699,350	102,621
Construction in progress	1,315,044	-	1,315,044	174,559
Total capital assets	<u>18,694,846</u>	<u>566</u>	<u>18,695,412</u>	<u>2,939,231</u>
Interest in joint ventures (Note 7)	31,473	-	31,473	-
Other noncurrent assets	39,542	13,300	52,842	301,236
Total Assets	<u>\$ 28,296,625</u>	<u>\$ 2,189,799</u>	<u>\$ 30,486,424</u>	<u>\$ 15,433,731</u>
LIABILITIES				
Current Liabilities:				
Warrants outstanding	\$ 179,255	\$ 8,434	\$ 187,690	\$ 1,116
Obligations under security lending	21,775	301,950	323,724	-
Accounts payable and other liabilities	2,335,801	231,645	2,567,445	267,732
Income tax refunds payable (Note 15)	717,518	-	717,518	-
Amounts due to component units	2,013	-	2,013	-
Amounts due to primary government	-	-	-	5,141
Bonds and notes payable (Notes 12 and 13)	648,935	-	648,935	1,083,309
Interest payable	111,977	-	111,977	108,789
Deferred revenue	110,746	813	111,559	71,212
Current portion of other long-term obligations (Note 14)	231,519	368	231,887	101,114
Total Current Liabilities	<u>4,359,539</u>	<u>543,209</u>	<u>4,902,748</u>	<u>1,638,413</u>
Prize awards payable (Note 14)	-	430,228	430,228	-
Deferred revenue	21,533	-	21,533	3,284
Bonds and notes payable (Notes 12 and 13)	6,042,970	-	6,042,970	7,001,277
Noncurrent portion of other long-term obligations (Note 14)	1,877,030	45,346	1,922,376	1,520,085
Total Liabilities	<u>\$ 12,301,071</u>	<u>\$ 1,018,784</u>	<u>\$ 13,319,855</u>	<u>\$ 10,163,060</u>

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

Michigan

	PRIMARY GOVERNMENT			COMPONENT UNITS
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTALS	
NET ASSETS				
Invested in capital assets, net of related debt	\$ 14,962,902	\$ 566	\$ 14,963,468	\$ 1,903,120
Restricted For:				
Education	-	-	-	198,565
Construction and debt service	48,707	-	48,707	299,060
Public safety and corrections	17,532	-	17,532	-
Conservation, environment, recreation, and agriculture	323,327	-	323,327	-
Health and family services	20,264	-	20,264	-
Transportation	770,056	-	770,056	-
Unemployment compensation	-	1,087,442	1,087,442	-
Other purposes	245,632	77,098	322,729	1,519,310
Funds Held as Permanent Investments:				
Expendable	93,658	-	93,658	26,942
Nonexpendable	474,158	-	474,158	193,723
Unrestricted	(960,684)	5,910	(954,774)	1,129,952
Total Net Assets	\$ 15,995,554	\$ 1,171,016	\$ 17,166,569	\$ 5,270,672

Michigan

STATEMENT OF ACTIVITIES

FISCAL YEAR ENDED SEPTEMBER 30, 2004

(In Thousands)

<u>Functions/Programs</u>	PROGRAM REVENUES			
	EXPENSES	CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS
Primary Government:				
Governmental Activities:				
General government	\$ 1,748,598	\$ 826,573	\$ 202,168	\$ 27,526
Education	14,418,940	5,277	1,325,584	-
Family independence services	3,985,861	58,170	2,777,417	-
Public safety and corrections	2,256,393	154,440	130,466	-
Conservation, environment, recreation, and agriculture	674,387	254,861	121,972	330
Labor, commerce, and regulatory	920,056	247,857	514,973	-
Health services	9,605,216	57,071	6,312,530	-
Transportation	3,104,841	197,125	398,362	590,590
Tax expenditures (Note 15)	702,700	-	-	-
Intergovernmental-revenue sharing	1,305,146	-	-	-
Interest on long-term debt	246,992	-	-	-
Total governmental activities	<u>38,969,130</u>	<u>1,801,373</u>	<u>11,783,472</u>	<u>618,445</u>
Business-type Activities:				
Liquor Purchase Revolving Fund	544,683	675,747	-	-
State Lottery Fund	1,391,385	2,002,688	18,694	-
Attorney Discipline System	4,056	4,593	-	-
Michigan Unemployment Compensation Funds	2,349,400	1,817,576	58,068	-
Total business-type activities	<u>4,289,524</u>	<u>4,500,604</u>	<u>76,762</u>	<u>-</u>
Total primary government	<u>\$ 43,258,653</u>	<u>\$ 6,301,978</u>	<u>\$ 11,860,234</u>	<u>\$ 618,445</u>
Component Units:				
Authorities:				
Michigan Education Trust	\$ 67,688	\$ 237	\$ 37,167	\$ -
Michigan State Housing Development Authority	481,956	169,942	348,447	-
Michigan Municipal Bond Authority	143,218	103,059	151,203	-
Non-Major	433,252	115,133	217,708	-
State Universities:				
Central Michigan University	293,418	183,985	30,827	2,623
Western Michigan University	436,423	259,272	70,215	1,397
Non-Major	1,262,415	723,963	161,835	65,557
Total component units	<u>\$ 3,118,369</u>	<u>\$ 1,555,592</u>	<u>\$ 1,017,402</u>	<u>\$ 69,577</u>

General Revenues:	
Taxes:	
General:	
Sales and use	
Personal income	
Single business	
Other	
Restricted For Educational Purposes:	
Sales and use	
Personal income	
Education, property, and real estate transfers	
Other	
Restricted For Transportation Purposes:	
Sales and use	
Gasoline and diesel fuel	
Motor vehicle weight	
Other	
Unrestricted investment and interest earnings	
Miscellaneous	
Contributions to permanent fund principal	
Payments from State of Michigan	
Transfers	
Total general and other revenue, payments, and transfers	
Change in net assets	
Net assets-beginning-restated	
Net assets-ending	

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

Michigan

NET (EXPENSE) REVENUES AND
CHANGES IN NET ASSETS

PRIMARY GOVERNMENT			
GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTALS	COMPONENT UNITS
\$ (692,332)	\$ -	\$ (692,332)	\$ -
(13,088,079)	-	(13,088,079)	-
(1,150,274)	-	(1,150,274)	-
(1,971,487)	-	(1,971,487)	-
(297,224)	-	(297,224)	-
(157,227)	-	(157,227)	-
(3,235,615)	-	(3,235,615)	-
(1,918,764)	-	(1,918,764)	-
(702,700)	-	(702,700)	-
(1,305,146)	-	(1,305,146)	-
(246,992)	-	(246,992)	-
<u>(24,765,839)</u>	<u>-</u>	<u>(24,765,839)</u>	<u>-</u>
-	131,064	131,064	-
-	629,997	629,997	-
-	537	537	-
<u>-</u>	<u>(473,756)</u>	<u>(473,756)</u>	<u>-</u>
<u>-</u>	<u>287,843</u>	<u>287,843</u>	<u>-</u>
<u>(24,765,839)</u>	<u>287,843</u>	<u>(24,477,996)</u>	<u>-</u>
-	-	-	(30,284)
-	-	-	36,433
-	-	-	111,045
-	-	-	(100,411)
-	-	-	(75,982)
-	-	-	(105,539)
-	-	-	(311,060)
-	-	-	(475,798)
2,565,865	-	2,565,865	-
4,693,512	-	4,693,512	-
1,773,325	-	1,773,325	-
1,640,244	11,989	1,652,233	-
5,143,414	-	5,143,414	-
1,896,860	-	1,896,860	-
2,142,706	-	2,142,706	-
775,297	-	775,297	-
64,960	-	64,960	-
1,070,488	-	1,070,488	-
933,822	-	933,822	-
7,721	-	7,721	-
9,728	1,225	10,953	62,131
677,848	-	677,848	57,962
30,759	-	30,759	-
-	-	-	667,806
901,580	(901,580)	-	-
<u>24,328,129</u>	<u>(888,366)</u>	<u>23,439,763</u>	<u>787,898</u>
(437,710)	(600,524)	(1,038,233)	312,100
16,433,263	1,771,539	18,204,803	4,958,572
<u>\$ 15,995,554</u>	<u>\$ 1,171,016</u>	<u>\$ 17,166,569</u>	<u>\$ 5,270,672</u>



GOVERNMENTAL FUND FINANCIAL STATEMENTS



Major Funds

GENERAL FUND

This fund is the State's operating fund. It accounts for the financial resources and transactions not accounted for in other funds.

COUNTER - CYCLICAL BUDGET AND ECONOMIC STABILIZATION FUND

This fund, commonly referred to as the "Budget Stabilization Fund" or "Rainy Day Fund," was created by P.A. 76 of 1977 to assist in stabilizing revenue and employment during periods of economic recession and high unemployment. In general, transfers are made into this fund from the General Fund during improving economic times and funds flow from this fund to the General Fund in times of declining economy. Additional information regarding the fund is provided in Note 3.

SCHOOL AID FUND

An amendment to the 1908 State Constitution created this fund in 1955. The 1963 State Constitution provided for the fund's continued existence. Its purpose is to aid in the support of the public schools and the intermediate school districts of the State. School aid payments to school districts are based on a statutory formula. Public Act 158 of 2003, effective October 1, 2003, created the school aid stabilization fund as a separate account within the School Aid Fund. Pursuant to this act, any remaining unreserved fund balance in the School Aid Fund at year-end is transferred to this account.

The fund receives State revenues restricted to local school programs, including: the constitutionally dedicated sixty percent of the collections of sales tax imposed at a rate of 4% and all of the collections of sales tax imposed at the additional rate of 2%; State Lottery Fund earnings; a percentage of the adjusted gross receipts from casino gaming; the real estate transfer tax; and portions of the personal income, cigarette, liquor, and industrial and commercial facilities taxes. A constitutional amendment approved by voters in 1994 made structural changes in the method of financing local school districts. The amendment authorized the levy of a statewide property tax, which is deposited in the School Aid Fund. Appropriated transfers are also made from the General Fund.

Non-Major Funds

Non-major governmental funds are presented, by fund type, beginning on page 96.

Michigan

BALANCE SHEET
GOVERNMENTAL FUNDS
 SEPTEMBER 30, 2004
 (In Thousands)

	GENERAL FUND	COUNTER - CYCLICAL BUDGET AND ECONOMIC STABILIZATION FUND	SCHOOL AID FUND	NON-MAJOR FUNDS	TOTALS
ASSETS					
Current Assets:					
Cash	\$ 7,541	\$ -	\$ -	\$ 5,691	\$ 13,232
Equity in common cash (Note 5)	-	-	-	1,279,959	1,279,959
Taxes, interest, and penalties receivable (Note 6)	2,498,042	-	1,820,188	126,383	4,444,613
Amounts due from other funds (Note 17)	1,551,776	81,258	9,883	961,147	2,604,063
Amounts due from component units	819	-	-	2,991	3,811
Amounts due from federal agencies	671,540	-	59,335	167,299	898,175
Amounts due from local units	61,530	-	80,564	62,315	204,408
Inventories	21,276	-	-	6,067	27,344
Investments (Note 8)	-	-	-	439,512	439,512
Securities lending collateral	-	-	-	21,775	21,775
Other current assets	298,132	-	466	238,123	536,722
Total Current Assets	5,110,656	81,258	1,970,435	3,311,264	10,473,613
Taxes, interest, and penalties receivable (Note 6)	226,440	-	44,143	1,411	271,994
Advances to other funds (Note 17)	6,768	-	-	21,689	28,457
Amounts due from federal agencies	2,201	-	-	-	2,201
Amounts due from local units	619,604	-	1,125	46,270	666,998
Investments (Note 8)	-	-	-	380,908	380,908
Other noncurrent assets	2,337	-	-	6,985	9,323
Total Assets	\$ 5,968,006	\$ 81,258	\$ 2,015,703	\$ 3,768,527	\$ 11,833,494
LIABILITIES AND FUND BALANCES					
Current Liabilities:					
Warrants outstanding	\$ 113,279	\$ -	\$ 1,228	\$ 61,159	\$ 175,666
Obligations under security lending	-	-	-	21,775	21,775
Accounts payable and other liabilities (Note 22)	1,388,343	-	147,952	715,012	2,251,307
Income tax refunds payable (Note 15)	717,518	-	-	-	717,518
Amounts due to other funds (Note 17)	926,041	-	1,466,496	214,735	2,607,272
Amounts due to component units	1,893	-	-	120	2,013
Bonds and notes payable	-	-	-	449,170	449,170
Interest payable	-	-	-	367	367
Deferred revenue	1,331,132	-	281,814	259,509	1,872,455
Total Current Liabilities	4,478,206	-	1,897,490	1,721,847	8,097,543
Long-Term Liabilities:					
Advances from other funds (Note 17)	-	-	-	21,689	21,689
Deferred revenue	319,981	-	44,143	19,294	383,418
Total Liabilities	4,798,187	-	1,941,634	1,762,830	8,502,650
Fund Balances:					
Reserved fund balance (Note 21)	1,169,819	-	74,070	1,591,479	2,835,368
Unreserved fund balance reported in:					
Special revenue funds	-	81,258	-	456,659	537,917
Debt service funds	-	-	-	365,841	365,841
Capital projects funds	-	-	-	(451,060)	(451,060)
Permanent funds	-	-	-	42,778	42,778
Total Fund Balances	1,169,819	81,258	74,070	2,005,697	3,330,844
Total Liabilities and Fund Balances	\$ 5,968,006	\$ 81,258	\$ 2,015,703	\$ 3,768,527	\$ 11,833,494

**RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET ASSETS**

SEPTEMBER 30, 2004

(In Thousands)

Total fund balances for governmental funds \$ 3,330,844

Amounts reported for governmental activities in the Statement of Net Assets
are different because:

Capital assets used in governmental activities are not financial resources
and therefore are not reported in the funds. (Note 9)

Land and other non-depreciable assets	3,153,972	
Buildings, equipment, and other depreciable assets	4,151,380	
Infrastructure	11,699,350	
Construction in progress	1,315,044	
Interest in joint ventures	31,473	
Accumulated depreciation	<u>(1,727,154)</u>	18,624,065

Certain tax revenues are earned but not available and therefore are not
reported in the funds. 1,831,784

Other long-term assets are not available to pay for current period
expenditures and therefore are deferred in the funds. 298,604

Internal service funds are used by management to charge the costs of
certain activities, such as insurance and telecommunications, to
individual funds. The assets and liabilities of the internal service funds
are included in governmental activities in the Statement of Net Assets. 121,620

Certain pension trust funds have been funded in excess of the annual
required contributions, creating a year-end asset. This asset is not a
current available resource and is not reported in the funds. (Note 10) 1,861

Deferred issue costs are reported as current expenditures in the funds.
However, deferred issue costs are amortized over the life of the bonds
and are included in the governmental activities in the Statement of Net
Assets. 28,301

Long-term liabilities are not due and payable in the current period and
therefore are not reported in the funds. (Note 14)

Capital lease obligations	(403,433)	
Compensated absences	(468,034)	
Workers' compensation	(106,492)	
Litigation	(588,388)	
Net pension obligations	(316,133)	
Other long-term liabilities	<u>(4,699)</u>	(1,887,180)

Long-term bonded debt is not due and payable in the current period and
therefore is not reported in the funds. Unamortized premiums, loss on
refundings, and interest payable are not reported in the funds. However,
these amounts are included in the Statement of Net Assets. This is the
net effect of these balances on the statement. (Note 12)

Bonds and notes payable	(6,115,206)	
Unamortized premiums	(225,279)	
Less deferred loss amount on refundings	97,750	
Accrued interest payable	<u>(111,610)</u>	<u>(6,354,345)</u>

Net assets of governmental activities \$ 15,995,554

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

Michigan

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS**

FISCAL YEAR ENDED SEPTEMBER 30, 2004

(In Thousands)

	GENERAL	COUNTER - CYCLICAL BUDGET AND ECONOMIC STABILIZATION FUND	SCHOOL AID FUND	NON-MAJOR FUNDS	TOTALS
REVENUES					
Taxes	\$ 10,689,854	\$ -	\$ 9,970,459	\$ 2,139,616	\$ 22,799,928
From federal agencies	9,258,903	-	1,256,727	1,064,589	11,580,220
From local agencies	109,553	-	-	130,262	239,815
From services	147,683	-	-	457	148,140
From licenses and permits	378,983	-	-	176,875	555,858
Special Medicaid reimbursements	704,551	-	-	-	704,551
Miscellaneous	545,483	-	11,122	648,762	1,205,367
Total Revenues	21,835,010	-	11,238,308	4,160,560	37,233,878
EXPENDITURES					
Current:					
General government	1,012,314	-	-	105,345	1,117,659
Education	1,905,826	-	12,298,895	240,463	14,445,184
Family independence services	3,932,471	-	-	2,699	3,935,170
Public safety and corrections	2,118,888	-	-	2,695	2,121,584
Conservation, environment, recreation, and agriculture	329,962	-	-	256,134	586,096
Labor, commerce, and regulatory	713,456	-	-	189,448	902,903
Health services	9,577,909	-	-	98,360	9,676,268
Transportation	-	-	-	2,212,371	2,212,371
Tax expenditures (Note 15)	702,700	-	-	-	702,700
Capital outlay	42,053	-	-	1,058,052	1,100,106
Intergovernmental-revenue sharing	1,305,146	-	-	-	1,305,146
Debt service:					
Bond principal retirement	-	-	-	729,557	729,557
Bond interest and fiscal charges	-	-	-	241,194	241,194
Capital lease payments	50,123	-	-	717	50,840
Total Expenditures	21,690,848	-	12,298,895	5,137,036	39,126,778
Excess of Revenues over (under) Expenditures	144,162	-	(1,060,587)	(976,475)	(1,892,901)
OTHER FINANCING SOURCES (USES)					
Bonds and notes issued	-	-	-	520,676	520,676
Premium on bond issuance	-	-	-	55,940	55,940
Refunding bonds issued	-	-	-	660,249	660,249
Payment to refunded bond escrow agent	-	-	-	(247,256)	(247,256)
Capital lease acquisitions	19,661	-	-	-	19,661
Proceeds from sale of capital assets	4,609	-	-	12,627	17,236
Transfers from other funds (Note 19)	512,905	81,258	1,022,683	1,678,094	3,294,939
Transfers to other funds (Note 19)	(822,275)	-	(3,167)	(1,566,652)	(2,392,095)
Total Other Financing Sources (Uses)	(285,101)	81,258	1,019,516	1,113,677	1,929,350
Excess of Revenues and Other Sources over (under) Expenditures and Other Uses	(140,939)	81,258	(41,071)	137,202	36,449
Fund Balances - Beginning of fiscal year restated	1,310,758	-	115,141	1,868,496	3,294,395
Fund Balances - End of fiscal year	\$ 1,169,819	\$ 81,258	\$ 74,070	\$ 2,005,697	\$ 3,330,844

Michigan

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES**
FISCAL YEAR ENDED SEPTEMBER 30, 2004
(In Thousands)

Net change in fund balance - total governmental funds \$ 36,449

Governmental funds report capital outlay as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.
(Note 9)

Land and other non-depreciable assets	26,814	
Buildings, equipment, and other depreciable assets	108,064	
Infrastructure additions	135,660	
Construction in progress	(72,949)	
Gain on sale of capital assets	8,191	
Accumulated depreciation	<u>(133,407)</u>	72,372

Certain revenues that were reported as resources in the funds but were earned in prior fiscal years are not reported in the Statement of Activities. 6,944

Increase in equity interest in joint ventures (Note 7) 75

Tax revenues that were reported as resources in the funds but were earned in prior fiscal years are not reported in the Statement of Activities. (79,876)

Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds. The net revenue (expense) of the internal service funds is reported with governmental activities. (3,290)

Bond proceeds provide current financial resources to governmental funds by issuing debt which increases long-term bonded debt in the Statement of Net Assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term bonded debt in the Statement of Net Assets. This is the amount proceeds exceed repayments. (Note 12)

Bond proceeds and premiums received	(1,236,865)	
Repayment of bond principal	729,557	
Payment to refunded bond escrow agent	247,256	
Accrued interest and amortization	(4,199)	
Deferred issue costs	7,330	
Other	<u>(9,971)</u>	(266,893)

Certain expenditures are reported in the funds. However, they either increase or decrease long-term liabilities reported on the Statement of Net Assets and have been eliminated from the Statement of Activities.
(Note 14)

Net pension obligation	(161,708)	
Capital lease payments	21,561	
Compensated absences payments	(87,299)	
Litigation settlements and payments	27,590	
Workers' compensation	(1,012)	
Other	<u>(2,623)</u>	<u>(203,492)</u>

Change in net assets of governmental activities \$ (437,710)

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



PROPRIETARY FUND FINANCIAL STATEMENTS



Major Funds

STATE LOTTERY FUND

Public Act 239 of 1972 established the State Lottery Fund and created a Bureau of State Lottery under authority of Article 5, Section 4, of the State Constitution. This authority expired on August 1, 1974, at which time the Bureau became an organizational entity in the Department of Management and Budget. The Bureau was transferred to the Department of Treasury during fiscal year 1990-91. Net income of the fund related to lottery operations is transferred to the School Aid Fund and the fund's net income related to bingo and charity games regulation is transferred to the General Fund. The remaining net assets balance represents the unrealized cumulative gain or loss on investments, as required by GASB Statement No. 31.

Revenues and related expenses are recognized in the period during which the related drawings are held. Deferred prize awards are recorded as expenses and liabilities at their discounted present value. The State Treasurer invests funds equivalent to the discounted value of the installment payments and the Lottery Fund is credited with the interest earnings.

MICHIGAN UNEMPLOYMENT COMPENSATION FUNDS

The columns for the Michigan Unemployment Compensation Funds reflect the activity of two funds administered by the Bureau of Worker's and Unemployment Compensation within the Department of Labor and Economic Growth: the Michigan Unemployment Compensation Fund and the Michigan Employment Security Act Contingent Fund. The Michigan Unemployment Compensation Fund receives contributions from employers and provides for the payment of benefits to eligible unemployed workers. The fund also makes payments under certain federally funded programs. Administrative costs of the fund are accounted for in the Michigan Employment Security Act - Administration Fund, a special revenue fund.

The Michigan Employment Security Act Contingent Fund was created by P.A. 535 of 1982 to receive a special temporary unemployment tax surcharge, known as the solvency tax. The fund also receives interest and penalty charges on late contributions. Public Act 224 of 1989 restricts use of solvency taxes for payment of interest on the Michigan Unemployment Compensation borrowings from the federal government.

A portion of the asset "Amounts due from other funds" and the liability "Amounts due to other funds" represent receivables and payables between the Michigan Unemployment Compensation Fund and the Michigan Employment Security Act Contingent Fund.

Non-Major Funds

Individual fund statements for the Enterprise Funds, whose combined totals are presented on this statement, begin on page 160.

Individual fund statements for the Internal Service Funds, whose combined totals are presented on this statement, begin on page 164.

Michigan

**STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
SEPTEMBER 30, 2004
(In Thousands)**

	BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	MAJOR			TOTALS	
	STATE LOTTERY FUND	MICHIGAN UNEMPLOYMENT COMPENSATION FUNDS	NON-MAJOR		
ASSETS					
Current Assets:					
Cash	\$ 2	\$ 4,049	\$ 1,194	\$ 5,245	\$ 91
Equity in common cash (Note 5)	6,736	4,557	60,064	71,357	274,437
Amounts due from other funds (Note 17)	-	4,959	-	4,959	31,180
Amounts due from component units	-	730	-	730	152
Amounts due from federal agencies	-	1,682	-	1,682	-
Amounts due from local units	-	39,288	-	39,288	-
Inventories	3,750	-	3,501	7,251	14,904
Investments (Note 8)	103,862	924,572	1,163	1,029,597	-
Securities lending collateral	301,950	-	-	301,950	-
Other current assets	55,346	187,173	7,427	249,946	20,293
Total Current Assets	471,645	1,167,010	73,349	1,712,005	341,057
Investments (Note 8)	496,824	-	-	496,824	-
Capital Assets (Note 9):					
Buildings and equipment	4,112	-	722	4,834	442,392
Allowance for depreciation	(3,599)	-	(669)	(4,268)	(340,138)
Total capital assets	513	-	53	566	102,254
Other noncurrent assets	-	13,300	-	13,300	-
Total Assets	\$ 968,982	\$ 1,180,310	\$ 73,403	\$ 2,222,695	\$ 443,311
LIABILITIES					
Current Liabilities:					
Warrants outstanding	\$ 1,757	\$ -	\$ 6,677	\$ 8,434	\$ 3,589
Accounts payable and other liabilities (Note 22)	145,984	26,893	58,694	231,571	69,809
Amounts due to other funds (Note 17)	9,978	22,915	77	32,970	13,419
Deferred revenue	-	118	695	813	6,737
Obligations under security lending (Note 8)	301,950	-	-	301,950	-
Current portion of other long-term obligations (Note 14)	172	-	196	368	96,461
Total Current Liabilities	459,841	49,926	66,339	576,105	190,016
Long-Term Liabilities:					
Advances from other funds (Note 17)	-	-	-	-	6,768
Prize awards payable	430,228	-	-	430,228	-
Noncurrent portion of other long-term obligations (Note 14)	1,816	42,942	588	45,346	124,907
Total Liabilities	891,885	92,868	66,927	1,051,679	321,691
NET ASSETS					
Invested in capital assets, net of related debt	\$ 513	\$ -	\$ 53	\$ 566	\$ 82,667
Restricted For:					
Unemployment compensation	-	1,087,442	-	1,087,442	-
Other purposes	77,098	-	-	77,098	3,361
Unrestricted	(513)	-	6,423	5,910	35,591
Total Net Assets	\$ 77,098	\$ 1,087,442	\$ 6,476	\$ 1,171,016	\$ 121,620

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

Michigan

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS

PROPRIETARY FUNDS

FISCAL YEAR ENDED SEPTEMBER 30, 2004

(In Thousands)

	BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	MAJOR			TOTALS	
	STATE LOTTERY FUND	MICHIGAN UNEMPLOYMENT COMPENSATION FUNDS	NON-MAJOR		
OPERATING REVENUES					
Operating revenues	\$ 2,002,688	\$ 1,817,576	\$ 680,340	\$ 4,500,604	\$ 1,569,067
Total Operating Revenues	<u>2,002,688</u>	<u>1,817,576</u>	<u>680,340</u>	<u>4,500,604</u>	<u>1,569,067</u>
OPERATING EXPENSES					
Salaries, wages, and other administrative	240,615	-	54,181	294,796	521,761
Interest expense	1	-	-	1	18
Depreciation	149	-	24	173	48,966
Purchases for resale	-	-	493,271	493,271	43,058
Purchases for prison industries	-	-	-	-	14,204
Lottery prize awards	1,107,050	-	-	1,107,050	-
Premiums and claims	-	-	1	1	894,837
Unemployment benefits	-	1,980,227	-	1,980,227	-
Other operating expenses	-	369,173	1,262	370,435	51,099
Total Operating Expenses	<u>1,347,815</u>	<u>2,349,400</u>	<u>548,739</u>	<u>4,245,953</u>	<u>1,573,943</u>
Operating Income (Loss)	<u>654,874</u>	<u>(531,824)</u>	<u>131,601</u>	<u>254,651</u>	<u>(4,876)</u>
NONOPERATING REVENUES (EXPENSES)					
Specific tax on spirits	-	-	11,989	11,989	-
Interest revenue	960	-	1,177	2,137	3,025
Investment revenue (expense) - net	17,734	58,068	48	75,850	-
Other nonoperating revenues	-	-	-	-	630
Amortization of prize award obligation discount	(39,223)	-	-	(39,223)	-
Interest expense	(4,347)	-	-	(4,347)	(1,214)
Other nonoperating expense	-	-	-	-	(791)
Total Nonoperating Revenues (Expenses)	<u>(24,876)</u>	<u>58,068</u>	<u>13,214</u>	<u>46,406</u>	<u>1,651</u>
Income (Loss) Before Capital Contributions and Transfers	<u>629,997</u>	<u>(473,756)</u>	<u>144,815</u>	<u>301,057</u>	<u>(3,226)</u>
CAPITAL CONTRIBUTIONS AND TRANSFERS					
Capital contributions from other funds	-	-	-	-	1,125
Transfers To:					
School Aid Fund	(644,883)	-	-	(644,883)	-
Other funds	(13,193)	(99,325)	(144,180)	(256,698)	(1,190)
Total transfers to other funds	<u>(658,076)</u>	<u>(99,325)</u>	<u>(144,180)</u>	<u>(901,580)</u>	<u>(1,190)</u>
Total Capital Contributions and Transfers In (Out)	<u>(658,076)</u>	<u>(99,325)</u>	<u>(144,180)</u>	<u>(901,580)</u>	<u>(64)</u>
Change in net assets	<u>(28,079)</u>	<u>(573,080)</u>	<u>636</u>	<u>(600,524)</u>	<u>(3,290)</u>
Total net assets - Beginning of fiscal year	<u>105,176</u>	<u>1,660,522</u>	<u>5,841</u>	<u>1,771,539</u>	<u>124,910</u>
Total net assets - End of fiscal year	<u>\$ 77,098</u>	<u>\$ 1,087,442</u>	<u>\$ 6,476</u>	<u>\$ 1,171,016</u>	<u>\$ 121,620</u>

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

Michigan

STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
 FISCAL YEAR ENDED SEPTEMBER 30, 2004
 (In Thousands)

	BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	MAJOR			TOTALS	
	STATE LOTTERY FUND	MICHIGAN UNEMPLOYMENT COMPENSATION FUNDS	NON-MAJOR		
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from federal and local agencies	\$ -	\$ 381,108	\$ -	\$ 381,108	\$ -
Receipts from customers	2,008,218	1,395,780	675,747	4,079,745	1,552,322
Membership dues	-	-	4,791	4,791	-
Payments to employees	(10,978)	-	(13,347)	(24,324)	(158,873)
Payments to suppliers	(46,409)	-	(524,124)	(570,533)	(678,130)
Payments to prize winners	(1,205,945)	-	-	(1,205,945)	-
Payments for commissions to retailers	(182,305)	-	-	(182,305)	-
Claims paid	-	(2,360,586)	-	(2,360,586)	(681,027)
Other receipts	-	2,100	167	2,267	311
Other payments	-	-	(5,127)	(5,127)	(8,784)
Net cash provided (used) by operating activities	<u>\$ 562,581</u>	<u>\$ (581,598)</u>	<u>\$ 138,107</u>	<u>\$ 119,089</u>	<u>\$ 25,819</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES					
Loans or loan repayments from other funds	\$ -	\$ -	\$ -	\$ -	\$ 31,987
Loans or loan repayments to other funds	-	-	-	-	(31,695)
Specific tax on spirits	-	-	11,989	11,989	-
Transfers to other funds	(673,241)	(105,977)	(144,180)	(923,398)	(1,190)
Other receipts	-	-	-	-	9
Net cash provided (used) by noncapital financing activities	<u>\$ (673,241)</u>	<u>\$ (105,977)</u>	<u>\$ (132,191)</u>	<u>\$ (911,409)</u>	<u>\$ (888)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Acquisition and construction of capital assets	\$ (82)	\$ -	\$ -	\$ (82)	\$ (19,514)
Interest paid	-	-	-	-	(292)
Capital lease payments (including imputed interest expense)	-	-	-	-	(17,037)
Proceeds from sale of capital assets	-	-	-	-	180
Net cash provided (used) by capital and related financing activities	<u>\$ (82)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (82)</u>	<u>\$ (36,664)</u>
CASH FLOWS FROM INVESTING ACTIVITIES					
Proceeds from sale and maturities of investment securities	\$ 108,890	\$ 620,901	\$ (26)	\$ 729,765	\$ -
Interest and dividends on investments	960	58,068	1,177	60,205	3,025
Income from securities lending activities	4,723	-	-	4,723	-
Expenses from securities lending activities	(4,347)	-	-	(4,347)	-
Net cash provided (used) by investing activities	<u>\$ 110,226</u>	<u>\$ 678,969</u>	<u>\$ 1,151</u>	<u>\$ 790,346</u>	<u>\$ 3,025</u>
Net cash provided (used) - all activities	\$ (516)	\$ (8,606)	\$ 7,067	\$ (2,056)	\$ (8,708)
Cash and cash equivalents at beginning of year	<u>5,498</u>	<u>17,212</u>	<u>47,514</u>	<u>70,223</u>	<u>279,647</u>
Cash and cash equivalents at end of year	<u><u>\$ 4,981</u></u>	<u><u>\$ 8,606</u></u>	<u><u>\$ 54,580</u></u>	<u><u>\$ 68,168</u></u>	<u><u>\$ 270,939</u></u>

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

Michigan

BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS

	MAJOR			TOTALS	GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	STATE LOTTERY FUND	MICHIGAN UNEMPLOYMENT COMPENSATION FUNDS	NON-MAJOR		
RECONCILIATION OF CASH AND CASH EQUIVALENTS					
Per Statement of Net Assets Classifications:					
Cash	\$ 2	\$ 4,049	\$ 1,194	\$ 5,244	\$ 91
Equity in common cash	6,736	4,557	60,064	71,357	274,437
Warrants outstanding	(1,757)	-	(6,677)	(8,434)	(3,589)
Cash and cash equivalents at end of year	<u>\$ 4,981</u>	<u>\$ 8,606</u>	<u>\$ 54,580</u>	<u>\$ 68,168</u>	<u>\$ 270,939</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES					
Operating income (loss)	\$ 654,874	\$ (531,824)	\$ 131,601	\$ 254,651	\$ (4,876)
Adjustments to Reconcile Operating Income to Net Cash Provided (Used)					
by Operating Activities:					
Depreciation expense	149	-	24	173	48,966
Amortization of prize award obligation discount	(39,223)	-	-	(39,223)	-
Other reconciling items	131	-	-	131	-
Net Changes in Assets and Liabilities:					
Inventories	(1,619)	-	161	(1,458)	2,346
Other assets (net)	12,940	(38,849)	(3,506)	(29,415)	(12,603)
Accounts payable and other liabilities	2,378	(10,911)	9,462	929	(8,014)
Prize awards payable	(67,050)	-	-	(67,050)	-
Deferred revenue	-	(14)	365	351	-
Net cash provided (used) by operating activities	<u>\$ 562,581</u>	<u>\$ (581,598)</u>	<u>\$ 138,107</u>	<u>\$ 119,089</u>	<u>\$ 25,819</u>
SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES					
Capital contributions	\$ -	\$ -	\$ -	\$ -	\$ 1,125
Cost of capital assets acquisitions financed by capital leases	-	-	-	-	10,576
Capital lease liabilities entered into during the year	-	-	-	-	(10,576)
Increase (decrease) in fair value of investments	(28,079)	-	-	(28,079)	-
Transfers to other funds (accrual)	(9,883)	(19,750)	-	(29,633)	-
Gain (loss) on disposal of capital assets	-	-	-	-	(339)
Total noncash investing, capital, and financing activities	<u>\$ (37,962)</u>	<u>\$ (19,750)</u>	<u>\$ -</u>	<u>\$ (57,712)</u>	<u>\$ 786</u>



FIDUCIARY FUND FINANCIAL STATEMENTS



Individual fund financial statements begin on the following pages:
Pension (and Other Employee Benefit) Trust Funds, page 172
Private Purpose Trust Funds, page 178
Agency Funds, page 181

Michigan

STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
 SEPTEMBER 30, 2004
 (In Thousands)

	<u>PENSION (AND OTHER EMPLOYEE BENEFIT) TRUST FUNDS</u>	<u>PRIVATE PURPOSE TRUST FUNDS</u>	<u>AGENCY FUNDS</u>
ASSETS			
Cash	\$ 592	\$ 960	\$ 79,707
Equity in common cash (Note 5)	208,426	69,386	4,095
Receivables:			
From participants	136,342	-	-
From employers	546,220	-	-
Interest and dividends	179	143	-
Due from other funds (Note 17)	14,902	-	-
Sale of investments	184	1,160	-
Investments at Fair Value (Note 8):			
Short term investments	1,549,154	-	15,070
Bonds, notes, mortgages, and preferred stock	8,177,244	11,734	44,606
Common stock	22,947,573	86	-
Real estate	3,259,600	-	-
Alternative investments	6,169,744	-	-
International investments	4,969,425	-	-
Mutual funds	1,677,805	623,053	-
Pooled investment funds	1,756,243	-	-
Money market funds	63,081	-	-
Guaranteed funding agreements	-	120,804	-
Securities lending collateral (Note 8)	2,808,598	1	-
Other current assets	-	6,973	6,029
Other noncurrent assets	-	-	372,614
Total assets	\$ 54,285,311	\$ 834,300	\$ 522,122
LIABILITIES			
Warrants outstanding	\$ 10,098	\$ 1,891	\$ 154
Accounts payable and other liabilities	70,735	7,240	100,448
Amounts due to other funds (Note 17)	26	-	1,298
Obligations under security lending	2,808,598	1	-
Other long-term liabilities	-	-	420,222
Total liabilities	\$ 2,889,457	\$ 9,133	\$ 522,122
NET ASSETS			
Net assets held in trust for pension, postemployment health-care, other employee benefits, and other purposes	<u>\$ 51,395,854</u>	<u>\$ 825,168</u>	
Reconciliation of Net Assets Held in Trust:			
Pension benefits (Note 10)	\$ 47,687,660	\$ -	
Postemployment health-care benefits	527,391	-	
Other employee benefits (Note 16)	3,180,803	-	
Other purposes	-	825,168	
Total net assets held in trust for benefits and other purposes	\$ 51,395,854	\$ 825,168	

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

Michigan

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

FIDUCIARY FUNDS

FISCAL YEAR ENDED SEPTEMBER 30, 2004

(In Thousands)

	PENSION (AND OTHER EMPLOYEE BENEFIT) TRUST FUNDS	PRIVATE PURPOSE TRUST FUNDS
	<u> </u>	<u> </u>
ADDITIONS		
Contributions:		
From participants	\$ 732,441	\$ 260,920
From employers	1,887,056	-
From clients	-	37,860
From gifts, bequests, and endowments	-	983
From other plans	5,055	-
Investment Income:		
Net appreciation (depreciation) in fair value of investments	4,701,940	31,039
Interest, dividends, and other	1,093,914	25,145
Securities lending income	30,206	18
Less Investment Expense:		
Investment activity expense	79,120	2,714
Securities lending expense	26,887	17
Net investment income (loss)	<u>5,720,053</u>	<u>53,472</u>
Escheated property	-	22,622
Miscellaneous income	<u>2,480</u>	<u>1,664</u>
 Total Additions	 <u>8,347,086</u>	 <u>377,520</u>
DEDUCTIONS		
Benefits paid to participants or beneficiaries	3,431,197	22,277
Medical, dental, and life insurance for retirants	1,003,803	-
Refunds and transfers to other systems	31,818	-
Amounts distributed to clients, claimants, or third parties	-	73,668
Administrative expense	82,263	6,785
Transfers to other funds	<u>74</u>	<u>-</u>
 Total Deductions	 <u>4,549,155</u>	 <u>102,731</u>
 Net increase (decrease)	 3,797,931	 274,789
 Net assets - Beginning of fiscal year	 <u>47,597,924</u>	 <u>550,378</u>
 Net assets - End of fiscal year (Note 10)	 <u>\$ 51,395,854</u>	 <u>\$ 825,168</u>
Reconciliation of Net Increase in Assets:		
Net increase (decrease) in assets held in trust for pension benefits	\$ 3,564,783	\$ -
Net increase (decrease) in assets held in trust for postemployment benefits	31,416	-
Net increase (decrease) in assets held in trust for other employee benefits	201,732	-
Net increase (decrease) in assets held in trust for other purposes	<u>-</u>	<u>274,789</u>
 Total net increase (decrease)	 <u>\$ 3,797,931</u>	 <u>\$ 274,789</u>

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



COMPONENT UNIT FINANCIAL STATEMENTS



Major Funds

MICHIGAN EDUCATION TRUST

The Michigan Education Trust (MET) operates a prepaid tuition program. A purchaser enters into a contract with MET which provides that in return for a specified actuarially determined payment, MET will provide a Michigan child's undergraduate tuition at any Michigan public university or community college. The amount the purchaser is required to pay is based on several factors, among them are tuition costs, the child's age and grade in school, anticipated investment earnings, tuition rate increases, and the type of contract purchased.

Public Act 316 of 1986 created MET. MET is governed by a nine-member board that consists of the State Treasurer and eight other individuals appointed by the Governor with the advice and consent of the Senate. Although MET is administratively located within the Michigan Department of Treasury, the Act provides its assets are not to be considered assets of the State and are not to be loaned or otherwise transferred or used by the State for any purpose other than the purposes specified in the Act. The Act and contracts also specifically provide that the State is not liable if MET becomes actuarially unsound. In that event, the contracts provide for refunds to participants.

MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY

Public Act 346 of 1966, as amended, created the Michigan State Housing Development Authority (MSHDA) to issue notes and bonds to finance housing for sale or rental to families with low or moderate incomes and to finance home improvements. MSHDA is also the administrator of various "Section 8" housing programs in Michigan for the U.S. Department of Housing and Urban Development. The Governor appoints MSHDA's board members.

MICHIGAN MUNICIPAL BOND AUTHORITY

Public Act 227 of 1985, as amended, created the Michigan Municipal Bond Authority (MMBA) to assist local units of government in reducing their financing costs for public improvements, deficit reduction, and various other municipal purposes. MMBA pools the borrowing needs of various units and issues limited obligation debt; the proceeds of which are used to purchase local unit obligations or to make loans to local units.

MMBA is governed by a board of trustees consisting of the State Treasurer, two appointees of the Governor, and five state residents appointed by the Governor, with the advice and consent of the Senate.

MMBA and the Department of Environmental Quality serve as co-administrators of a special State Revolving Fund, which is reported as part of MMBA. The State Revolving Fund assists governmental units in financing water quality projects. Federal government and State matching provides financing for this activity along with investment interest earnings and/or other available funds. MMBA's separately issued financial reports provide a separate accounting of this fund's activities.

CENTRAL MICHIGAN UNIVERSITY AND WESTERN MICHIGAN UNIVERSITY

Central Michigan University and Western Michigan University are the two major universities of the ten universities included in this report. They are legally separate entities whose governing boards are appointed by the Governor and for which the State is therefore, defined as legally accountable. Excluded from this report are three other universities (University of Michigan, Michigan State University and Wayne State University) whose board members are elected by the voters and, therefore, considered separate special purpose governments.

Non-Major Funds

The non-major component unit - authorities are presented beginning on page 186.

The non-major component unit - State universities are presented beginning on page 192.

STATEMENT OF NET ASSETS
COMPONENT UNITS
 SEPTEMBER 30, 2004
 (In Thousands)

	AUTHORITIES			
	MICHIGAN EDUCATION TRUST	MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY	MICHIGAN MUNICIPAL BOND AUTHORITY	NON-MAJOR
ASSETS				
Current Assets:				
Cash	\$ 189,538	\$ 162,199	\$ 75	\$ 78,631
Equity in common cash (Note 5)	-	-	229	74,899
Amounts due from component units	-	-	-	-
Amounts due from primary government	1,355	-	570	1,263
Amounts due from federal government	-	-	-	14,036
Amounts due from local units	-	-	907,126	-
Inventories	-	-	-	727
Investments (Note 8)	-	101,600	560,919	323,278
Other current assets	18,176	40,639	40,436	195,347
Total Current Assets	209,069	304,438	1,509,353	688,181
Restricted Assets:				
Cash and cash equivalents	-	-	-	6,407
Investments	-	-	-	10,539
Mortgages and loans receivable	-	-	-	-
Amounts due from local units	-	-	2,324,057	-
Mortgages and loans receivable	-	1,766,448	-	1,224,512
Investments (Note 8)	721,677	576,497	1,032,666	394,772
Capital Assets:				
Land and other non-depreciable assets	-	-	-	843
Buildings, equipment, and other depreciable assets	-	15,098	-	46,592
Less accumulated depreciation	-	(2,056)	-	(18,702)
Infrastructure	-	-	-	102,621
Construction in progress	-	-	-	-
Total capital assets	-	13,042	-	131,355
Other noncurrent assets	41,836	47,430	151,300	16,882
Total Assets	\$ 972,583	\$ 2,707,854	\$ 5,017,377	\$ 2,472,648
LIABILITIES				
Current Liabilities:				
Warrants outstanding	\$ -	\$ -	\$ -	\$ 1,116
Accounts payable and other liabilities	5	33,182	6,132	28,004
Amounts due to primary government	-	-	525	1,945
Bonds and notes payable (Note 13)	-	148,780	862,056	40,626
Interest payable	-	8,588	74,935	8,246
Deferred revenue	-	-	10,942	2,838
Current portion of other long-term obligations	86,004	-	-	4,235
Total Current Liabilities	86,008	190,551	954,589	87,009
Deferred revenue	-	-	-	-
Bonds and notes payable (Note 13)	-	1,533,730	2,564,958	1,854,898
Noncurrent portion of other long-term obligations	881,662	430,839	65,088	66,140
Total Liabilities	\$ 967,670	\$ 2,155,120	\$ 3,584,635	\$ 2,008,047
NET ASSETS				
Invested in capital assets, net of related debt	\$ -	\$ -	\$ -	\$ 126,200
Restricted For:				
Education	-	-	-	-
Construction and debt service	-	261,272	-	10,371
Other purposes	4,913	-	1,422,475	29,677
Funds Held as Permanent Investments:				
Expendable	-	-	-	-
Nonexpendable	-	-	-	-
Unrestricted	-	291,462	10,267	298,353
Total Net Assets	\$ 4,913	\$ 552,734	\$ 1,432,742	\$ 464,601

STATE UNIVERSITIES

CENTRAL MICHIGAN UNIVERSITY	WESTERN MICHIGAN UNIVERSITY	NON-MAJOR	TOTALS
\$ 31,594	\$ 16,571	\$ 191,428	\$ 670,035
-	-	-	75,128
-	-	239	239
43,264	21,643	110,618	178,713
717	2,857	11,310	28,919
-	16	228	907,370
3,321	4,495	7,117	15,660
-	11,234	30,248	1,027,279
16,081	15,820	65,908	392,407
<u>94,977</u>	<u>72,636</u>	<u>417,096</u>	<u>3,295,749</u>
2,612	-	8,262	17,281
52,977	138,041	178,797	380,354
7,252	-	38,112	45,365
-	-	-	2,324,057
-	8,706	23,388	3,023,054
70,996	67,092	243,703	3,107,403
9,922	14,912	70,080	95,757
504,253	845,587	2,659,859	4,071,388
(209,060)	(286,161)	(989,116)	(1,505,094)
-	-	-	102,621
11,878	41,081	121,600	174,559
<u>316,993</u>	<u>615,419</u>	<u>1,862,423</u>	<u>2,939,231</u>
-	16,621	27,167	301,236
<u>\$ 545,807</u>	<u>\$ 918,514</u>	<u>\$ 2,798,948</u>	<u>\$ 15,433,731</u>
\$ -	\$ -	\$ -	\$ 1,116
42,886	34,067	123,456	267,732
646	105	1,920	5,141
6,610	6,520	18,718	1,083,309
981	11,724	4,316	108,789
9,368	9,887	38,178	71,212
-	524	10,352	101,114
<u>60,491</u>	<u>62,827</u>	<u>196,939</u>	<u>1,638,413</u>
-	-	3,284	3,284
125,030	257,425	665,236	7,001,277
15,014	23,166	38,176	1,520,085
<u>\$ 200,535</u>	<u>\$ 343,418</u>	<u>\$ 903,635</u>	<u>\$ 10,163,060</u>
\$ 187,253	\$ 314,666	\$ 1,275,001	\$ 1,903,120
42,928	10,184	145,453	198,565
5,977	8,478	12,963	299,060
-	43,547	18,699	1,519,310
-	-	26,942	26,942
-	47,960	145,763	193,723
109,114	150,262	270,493	1,129,952
<u>\$ 345,273</u>	<u>\$ 575,097</u>	<u>\$ 1,895,313</u>	<u>\$ 5,270,672</u>

Michigan

STATEMENT OF ACTIVITIES

COMPONENT UNITS

FISCAL YEAR ENDED SEPTEMBER 30, 2004

(In Thousands)

<u>FUNCTIONS/PROGRAMS</u>	<u>EXPENSES</u>	<u>PROGRAM REVENUES</u>			<u>NET (EXPENSE) REVENUE</u>
		<u>CHARGES FOR SERVICES</u>	<u>OPERATING GRANTS/ CONTRIBUTIONS</u>	<u>CAPITAL GRANTS/ CONTRIBUTIONS</u>	
Authorities:					
Michigan Education Trust	\$ 67,688	\$ 237	\$ 37,167	\$ -	\$ (30,284)
Michigan State Housing Development Authority	481,956	169,942	348,447	-	36,433
Michigan Municipal Bond Authority	143,218	103,059	151,203	-	111,045
Non-Major	433,252	115,133	217,708	-	(100,411)
State Universities:					
Central Michigan University	293,418	183,985	30,827	2,623	(75,982)
Western Michigan University	436,423	259,272	70,215	1,397	(105,539)
Non-Major	1,262,415	723,963	161,835	65,557	(311,060)
Total	<u>\$ 3,118,369</u>	<u>\$ 1,555,592</u>	<u>\$ 1,017,402</u>	<u>\$ 69,577</u>	<u>\$ (475,798)</u>

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

Michigan

<u>GENERAL REVENUES</u>						
<u>INTEREST AND INVESTMENT EARNINGS (LOSS)</u>	<u>PAYMENTS FROM STATE OF MICHIGAN</u>	<u>OTHER</u>	<u>SPECIAL ITEMS</u>	<u>CHANGE IN NET ASSETS</u>	<u>NET ASSETS BEGINNING OF YEAR RESTATED</u>	<u>NET ASSETS END OF YEAR</u>
\$ -	\$ -	\$ -	\$ -	\$ (30,284)	\$ 35,196	\$ 4,913
15,567	-	-	-	52,000	500,734	552,734
-	-	-	-	111,045	1,321,697	1,432,742
7,486	47,987	5,850	-	(39,089)	503,690	464,601
12,719	90,013	215	-	26,965	318,308	345,273
6,224	135,590	35,361	-	71,636	503,460	575,097
20,135	394,216	16,536	-	119,827	1,775,487	1,895,313
<u>\$ 62,131</u>	<u>\$ 667,806</u>	<u>\$ 57,962</u>	<u>\$ -</u>	<u>\$ 312,100</u>	<u>\$ 4,958,572</u>	<u>\$ 5,270,672</u>