Report 14-11
September 2014

Wisconsin Economic Development Corporation

State of Wisconsin

Legislative Audit Bureau

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Joe Chrisman
State Auditor

September 19, 2014

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

Section 13.94(1)(dr), Wis. Stats., requires the Legislative Audit Bureau to biennially conduct a financial audit of the Wisconsin Economic Development Corporation (WEDC) and a program evaluation audit of WEDC's economic development programs. In May 2013, we issued report 13-7, which fulfilled the requirement for a program evaluation audit, partially fulfilled the requirement for a financial audit, and included recommendations to improve WEDC's financial management. In this report (14-11), we complete certain analyses related to WEDC's financial management during fiscal year (FY) 2011-12 and FY 2012-13, and update certain information in report 13-7. Our next comprehensive biennial audit of WEDC and its economic development programs will begin in fall 2014.

In FY 2012-13, WEDC's administrative expenditures totaled $15.1 million, of which $8.3 million was for salaries and fringe benefits. WEDC also incurred $14.7 million in expenditures for grants awarded through its economic development programs, and it disbursed an additional $14.6 million in loans awarded under these programs.

As of June 30, 2013, the outstanding loan balance for which WEDC was responsible totaled $60.5 million. From June 30, 2013, through December 31, 2013, the total potentially uncollectible loan balance decreased by $7.7 million, including $6.6 million because WEDC wrote off loans it turned over to the Department of Administration, amended loan contracts, and forgave loans that had been considered delinquent as of June 30, 2013, because WEDC staff did not complete forgiveness reviews.

We include recommendations to further improve WEDC's financial management, including its efforts to monitor loans. A response from WEDC's chief executive officer follows our report.

Respectfully submitted,

Joe Chrisman
State Auditor

JC/KE/ss

Introduction ■

2011 Wisconsin Act 7 created the Wisconsin Economic Development Corporation (WEDC) as the State's lead economic development organization. WEDC, which is not a state agency, became fully operational in July 2011. It is statutorily required to develop and implement economic programs that provide support, expertise, and financial assistance to firms that are investing and creating jobs in Wisconsin, as well as programs that support new business start-ups and business expansion and growth in the State. WEDC may also develop and implement any other programs related to economic development. Although WEDC is exempt from some statutory requirements that apply to state agencies, it remains subject to certain reporting and oversight provisions, including audits by the Legislative Audit Bureau, and is funded almost entirely with state funds.

Section 13.94(1)(dr), Wis. Stats., requires the Legislative Audit Bureau to biennially conduct a financial audit of WEDC and a program evaluation audit of WEDC's economic development programs. In May 2013, we issued report 13-7, which fulfilled the requirement for a program evaluation audit and partially fulfilled the requirement for a financial audit of WEDC. For example, in report 13-7 we reviewed purchasing card transactions, assessed the process WEDC used to purchase goods and services, and made recommendations to improve WEDC's financial management. However, at the time of our fieldwork for report 13-7, WEDC did not have adequate familiarity with its accounting system, had not established accounting policies and procedures, and had experienced turnover in key financial management positions. Therefore, we included only estimates of WEDC's fiscal year (FY) 2011-12 expenditures in report 13-7.

In this report (report 14-11), we complete certain analyses related to WEDC's financial management and update certain information in report 13-7 by reviewing WEDC's:

- revenues, administrative expenditures, and grant expenditures for both FY 2011-12 and FY 2012-13; and
- efforts to monitor loan repayments and resolve delinquent loans.

When combined, report 14-11 and report 13-7 fulfill our statutory requirement to conduct a financial audit of WEDC.

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Revenues and Expenditures ▪

WEDC is funded primarily by state general purpose revenue (GPR) and segregated revenue. From FY 2011-12 to FY 2012-13, WEDC's administrative expenditures increased 34.0 percent, and its grant expenditures decreased 2.8 percent. We make recommendations to further improve aspects of WEDC's financial management related to its accounting for administrative and grant activities.

Revenues

GPR and segregated revenue accounted for 90.0 percent or more of WEDC's revenue.

As shown in Table 1, WEDC's revenue increased from $57.9 million in FY 2011-12 to $62.5 million in FY 2012-13. This increase is primarily due to an increase in federal revenue from the Wisconsin Housing and Economic Development Authority to administer a federal program intended to support lending to small businesses and manufacturers. GPR and segregated revenue accounted for 97.1 percent of WEDC's FY 2011-12 revenues and 90.0 percent of its FY 2012-13 revenues.

Table 1

WEDC Revenues

	FY 2011-12	Percentage of Total	FY 2012-13	Percentage of Total
General Purpose Revenue	$32,018,000	55.3%	$32,049,100	51.3%
Segregated Revenue[1]	24,189,200	41.8	24,189,200	38.7
Federal Revenue	410,000	0.7	4,139,700	6.6
Loan Interest and Fees	918,200	1.6	886,900	1.4
Other[2]	380,300	0.6	1,203,700	2.0
Total	**$57,915,700**[3]	**100.0%**	**$62,468,600**	**100.0%**

[1] Includes $23.2 million from the State's Economic Development Fund, which is funded by an economic development surcharge on Wisconsin businesses.

[2] Includes bond servicing fees, registration fees for WEDC-sponsored conferences, and trade mission participation fees.

[3] Excludes $46.5 million in financial resources, such as loan receivables, that were transferred to WEDC from the State of Wisconsin to provide initial funding.

Administrative and Grant Expenditures

WEDC incurs administrative expenditures for its economic development programs and operations. WEDC also incurs grant expenditures for costs its grant recipients incur under the terms of the grant agreements.

Administrative expenditures increased from $11.2 million in FY 2011-12 to $15.1 million in FY 2012-13 primarily due to increases in expenditures for staff salaries and fringe benefits and marketing. Grant expenditures decreased from $15.2 million in FY 2011-12 to $14.7 million in FY 2012-13. The amount of grant funds WEDC expends in any year may vary and is related to when costs are incurred by grant recipients. WEDC indicated that 62 grants were awarded in FY 2011-12 and 81 grants were awarded in FY 2012-13.

WEDC's revenues exceeded its expenditures in both FY 2011-12 and FY 2012-13. As a result, WEDC accumulated a surplus of $18.4 million in excess of what WEDC determined was necessary for its operations, programs, and unanticipated contingencies. This accumulated surplus was discussed at a meeting of the Joint Committee on Finance in January 2014, at which time the GPR available to WEDC was reduced for FY 2013-14. We will assess funding of WEDC's FY 2013-14 operations and programs in our next biennial audit.

Administrative Expenditures

From FY 2011-12 to FY 2012-13, staff salaries and fringe benefits increased 24.3 percent primarily due to an increase in the number of employees.

As shown in Table 2, staff salaries and fringe benefits totaled $8.3 million in FY 2012-13. From FY 2011-12 to FY 2012-13, staff salaries and fringe benefits expenditures increased by 24.3 percent. This is primarily due to an increase in WEDC's staffing levels during its first two years of operation. WEDC had 58 employees at the beginning of FY 2011-12 and 99 employees at the end of FY 2012-13. Marketing expenditures, which totaled 10.7 percent of administrative expenditures in FY 2012-13, include payments for video and graphic production, advertising, research, WEDC's website, and printing. Professional services expenditures, which totaled 10.4 percent of administrative expenditures in FY 2012-13, include costs for external services such as payroll processing.

Table 2

Administrative Expenditures

	FY 2011-12	Percentage of Total	FY 2012-13	Percentage of Total
Staff Salaries and Fringe Benefits	$6,660,300	59.2%	$ 8,278,600	55.0%
Marketing	780,100	6.9	1,605,200	10.7
Professional Services	1,281,400	11.4	1,565,000	10.4
Building, Maintenance, and Utilities	765,200	6.8	1,076,100	7.1
Information Technology	648,400	5.8	1,067,200	7.1
Conferences and Professional Development	461,200	4.1	642,600	4.3
Travel	342,100	3.1	414,100	2.7
Recruiting	0	0.0	90,400	0.6
Other	304,100	2.7	321,300	2.1
Total	**$11,242,800**	**100.0%**	**$15,060,500**	**100.0%**

Staff Salaries and Fringe Benefits

Because staff salaries and fringe benefits represented over one-half of WEDC's administrative expenditures, we examined these expenditures in greater detail. We reviewed documentation for ten individuals employed by WEDC between July 1, 2011, and June 30, 2013, and found the salary and fringe benefits expenditures for these ten individuals were supported by information maintained by WEDC's human resources department.

In FY 2012-13, WEDC employees received merit and recognition awards totaling $78,225.

In report 13-7, we noted that WEDC's vice presidents may recommend merit awards for employees who exceed performance expectations and that managers may give employees recognition awards to recognize a special effort or accomplishment. No merit or recognition awards were given to employees in FY 2011-12. Of the $182,000 WEDC budgeted for merit and recognition awards in FY 2012-13, $78,225 was paid to employees.

In FY 2012-13, 24 WEDC employees received merit awards totaling $77,700. Merit awards, which ranged from $1,000 to $5,000 per award, were given to employees across multiple WEDC divisions. In addition, merit awards totaling $7,500 for three employees were approved in FY 2012-13 but were paid in FY 2013-14. We note that the approval of merit awards for these three employees was not documented in accordance with WEDC's procedures.

In addition to merit awards, WEDC managers may give their employees recognition awards of either one or two $25 gift cards. Employees select the desired gift card(s) from a predetermined list of entities. Employees are eligible to receive multiple recognition awards during the year. In December 2012 and January 2013, WEDC staff purchased 87 gift cards totaling $2,175 from six entities. In FY 2012-13, 12 WEDC employees received 21 gift cards, with a total value of $525, as recognition awards. WEDC staff indicated that they performed a review, implemented physical controls, and separated duties related to gift cards in early 2014. We will further review WEDC's procedures related to gift cards in our next biennial audit.

Other Administrative Expenditures

Non-payroll administrative expenditures represented approximately 45.0 percent of WEDC's administrative expenditures in FY 2012-13. We reviewed 223 expenditures recorded during FY 2011-12 and FY 2012-13 and found instances in which the supporting documentation provided by WEDC was not adequate to demonstrate that the expenditures were incurred, were reasonable, and were approved. For example, supporting documentation provided for one expenditure did not demonstrate that it was incurred or reasonable because the amounts charged and dates of service were missing. Supporting documentation provided for another expenditure did not demonstrate that it was incurred, reasonable, or approved because the support provided was not specifically related to the expenditure. We also identified some expenditures that we believe would have been more appropriately recorded in a different account or that were not recorded consistently with similar types of expenditures. For example, $50,000 expended under a grant agreement was instead recorded as a professional services expenditure.

Grant Expenditures

WEDC expended grant funds totaling $15.2 million in FY 2011-12 and $14.7 million in FY 2012-13.

Through its economic development programs, WEDC may award grants to businesses, economic development organizations, and local governments to support economic development projects. WEDC may also award grants to economic development organizations and local governments to support their operational and marketing activities when they serve as strategic partners of WEDC. Strategic partners provide services beyond those available from WEDC, such as technical assistance in applying for grants. As noted, WEDC expended grant funds totaling $15.2 million in FY 2011-12 and $14.7 million in FY 2012-13.

To receive reimbursement, each grant recipient submits documentation to WEDC demonstrating it incurred costs under the terms of the grant agreement. Because grant agreements may allow recipients to complete projects over multiple years, the amount of funds WEDC expends in any year relates to both grants awarded in that year and to grants awarded in prior years.

We reviewed 44 grant expenditures WEDC recorded during FY 2011-12 and FY 2012-13, including several that were part of transactions that reclassified grant expenditures originally recorded in multiple other transactions. While there were initial errors in processing several of the expenditures we reviewed, we found that WEDC staff had subsequently reviewed and corrected them. In May 2014, WEDC also implemented a new loan and grant tracking system, which WEDC staff indicated will allow the expenditure transactions to be uploaded directly into the accounting system and eliminate duplicate data entry. As a result, the use of this new system may decrease the risk that grant expenditures are recorded incorrectly in the accounting system. We will review WEDC's use of the new loan and grant tracking system in our next biennial audit.

Although WEDC had corrected the accounting system for errors in recording grant expenditures, the supporting documentation provided by WEDC for some of the 44 grant expenditures we reviewed was not adequate. For example, for two grant expenditures, the supporting documentation provided did not include disbursement requests that were formally approved by WEDC.

As noted, we identified instances in which the supporting documentation provided by WEDC for administrative and grant expenditures incurred in FY 2011-12 and FY 2012-13 was not adequate and expenditures were not consistently recorded. This may, in part, be explained by turnover in key financial management positions in those years. Subsequently, the current chief financial officer has been employed by WEDC since June 2013, and the current controller has been employed by WEDC since September 2013. In report 13-7, we recommended that WEDC develop policies for several areas of its operations. Among the policies WEDC presented to its board in July 2013 were some policies related to its financial management. We will consider these new policies in our next biennial audit. As WEDC continues its efforts to improve its financial management, it should take steps to ensure adequate supporting documentation is maintained and transactions are appropriately and consistently recorded in the accounting system.

☑ Recommendation

We recommend the Wisconsin Economic Development Corporation:

- *ensure supporting documentation is maintained for its expenditures that demonstrates that each expenditure was incurred, was reasonable, and was approved; and*

- *ensure similar expenditures are consistently recorded in the accounting system in the appropriate account.*

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Loans ▪

Through its economic development programs, WEDC awards loans to businesses and economic development organizations to support economic development projects. We reviewed WEDC's efforts to monitor loan repayments and resolve delinquent loans, and we make recommendations to further improve aspects of WEDC's financial management related to its loan activities.

Types of Loans

WEDC awards both collectible and forgivable loans with interest rates that averaged approximately 2.5 percent annually as of June 30, 2013. A collectible loan is a traditional loan with a loan contract that includes repayment terms, which may not be required to begin for six months or more.

A forgivable loan also has a loan contract that includes repayment terms. A forgivable loan contract includes specific conditions, such as creating or retaining a certain number of jobs. If such conditions in the forgivable loan contract are met by the loan recipient, WEDC may forgive the loan in whole or in part. No repayment is necessary for the amount of the loan that is forgiven, including any related interest.

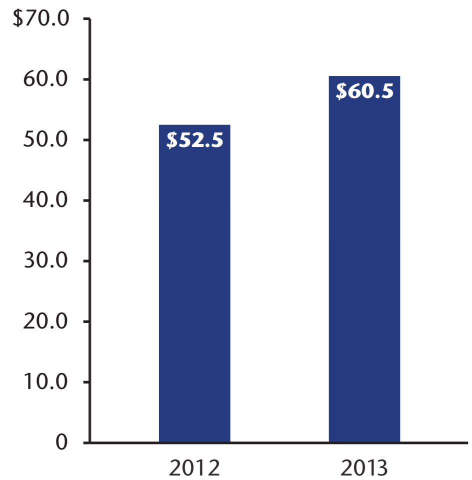
Loan Balances

The overall balance of WEDC's loan portfolio was $60.5 million as of June 30, 2013.

As shown in Figure 1, the overall balance of the loan portfolio for which WEDC was responsible increased from $52.5 million as of June 30, 2012, to $60.5 million as of June 30, 2013, or by 15.3 percent. Of the loan balances for which WEDC was responsible, loans awarded by the former Department of Commerce accounted for 74.6 percent as of June 30, 2012, and 54.3 percent as of June 30, 2013.

Figure 1

Loan Balances as of June 30[1]
(in millions)



[1] Excludes accrued interest and amounts related to loans awarded through the State Energy Program because the Department of Administration is responsible for these loans.

Loan Disbursements

Excluding interest, WEDC received $4.3 million in loan repayments during FY 2012-13.

WEDC typically disburses loan funds after recipients submit documentation showing that they incurred project-related costs consistent with the terms of the loan contracts. As a result, amounts awarded under a loan contract may be disbursed to the recipient over multiple months or years. Therefore, the amount of loan funds disbursed in any year includes both funds from loans awarded in that year and loans awarded in prior years. As shown in Table 3, WEDC disbursed $14.5 million in loan funds in FY 2011-12 and $14.6 million in FY 2012-13. More than half of the disbursements were related to collectible loans. WEDC received loan repayments, excluding interest, of $3.6 million during FY 2011-12 and $4.3 million during FY 2012-13.

Table 3

Loan Disbursements[1]

	FY 2011-12	FY 2012-13
Collectible Loans	$ 8,533,200	$10,249,100
Forgivable Loans	5,960,000	4,394,600
Total	**$14,493,200**	**$14,643,700**

[1] Excludes amounts related to loans awarded through the State Energy Program because the Department of Administration is responsible for these loans.

Loan Monitoring

In its capacity as a lender, WEDC is responsible for collecting loan repayments, monitoring loans not fully repaid, pursuing collection of delinquent loans, and reporting loan portfolio information. WEDC staff stated that, since October 2012, they query the loan and grant tracking system monthly to identify delinquent loans. WEDC staff also indicated that they send notices to recipients of loans for which repayment is 30 days or more past due and consider other actions when loan repayments become 90 days or more past due. As part of its efforts to monitor loans, WEDC staff also compile information on each loan past due, including the current principal balance of these loans.

Loan repayments of nearly $1.7 million were 90 days or more past due as of December 31, 2013, and represented 2.7 percent of the total outstanding loan balance.

Currently, a published goal of WEDC's Division of Credit and Risk is to "maintain a delinquency rate that is acceptable to senior management and WEDC Board of Directors." Delinquency rates may be calculated using more than one methodology. For example, WEDC reported that, as of December 31, 2013, its delinquency rate was 2.7 percent. This rate represents loan repayments that were 90 days or more past due and that totaled nearly $1.7 million, or 2.7 percent, of the total outstanding loan balance of $62.2 million for the loan portfolio, including accrued interest of $2.8 million. WEDC staff indicated this delinquency rate methodology helps WEDC monitor the success of efforts to bring delinquent loans into current repayment status. However, as a measure of risk, this delinquency rate methodology is limited because it does not consider the entire loan balance that is potentially uncollectible for loans with repayments that are 90 days or more past due. For example, this methodology considers only the $16,250 in repayments that were 90 days or more past due as of December 31, 2013, for one specific loan and does not consider that loan's entire $768,800 outstanding loan balance as of December 31, 2013.

The total potentially uncollectible loan balance of $5.5 million as of December 31, 2013, represented 8.8 percent of the total outstanding loan balance.

Another methodology for calculating a delinquency rate is to measure the entire loan balance for loans with repayments 90 days or more past due as a percentage of the total outstanding loan balance for the loan portfolio. For example, for loans with repayments 90 days or more past due, the total potentially uncollectible loan balance of $5.5 million as of December 31, 2013, represented 8.8 percent of the total outstanding loan balance of $62.2 million for the loan portfolio, including accrued interest.

The delinquency rate of 2.7 percent as of December 31, 2013, considers loan repayments that are 90 days or more past due. The delinquency rate of 8.8 percent as of December 31, 2013, considers the maximum potential loss if the loans become uncollectible. Establishing goals for both delinquency rate methodologies and incorporating these goals into its overall approach would further improve WEDC's monitoring of its loans and provide the Legislature with a more comprehensive assessment of WEDC's delinquent loans.

Change in the Potentially Uncollectible Loan Balance

From June 30, 2013, to December 31, 2013, the total potentially uncollectible loan balance decreased by $7.7 million.

In our analyses, we considered the change from June 30, 2013, to December 31, 2013, in the amount of loans with repayments 90 days or more past due. The total potentially uncollectible loan balance for such loans decreased from $13.2 million for 49 loans as of June 30, 2013, to $5.5 million for 30 loans as of December 31, 2013, or by $7.7 million. Of this $7.7 million decrease, $6.6 million was related to:

- $3.2 million in loans with repayments 90 days or more past due that WEDC wrote off because it turned the loans over to the Department of Administration;

- $2.1 million in loans with repayments 90 days or more past due for which WEDC amended the loan contracts to defer repayments; and

- $1.3 million in forgivable loans that WEDC forgave, in whole or in part. Because WEDC staff did not complete forgiveness reviews for these loans prior to the repayment date identified in the loan contract, these loans were considered delinquent as of June 30, 2013, on the loan and grant tracking system.

The decrease in the potentially uncollectible loan balance from June 30, 2013, to December 31, 2013, also related to:

- $346,100 received by WEDC for potentially uncollectible loans, of which $42,600 was to pay off past due amounts for six loans with outstanding balances totaling $1.2 million;

- $1.2 million in outstanding balances for the six loans that became current and are no longer considered delinquent as a result of the $42,600 pay-off of past due amounts; and

- $787,600 for a loan that had been erroneously considered delinquent due to a data entry error.

The decrease in the potentially uncollectible loan balance was partially offset by loans with outstanding balances totaling $1.2 million for which loan repayments first became 90 days or more past due during the period from June 30, 2013, through December 31, 2013.

Loan Write-Offs

From July 1, 2013, through December 31, 2013, WEDC wrote off three loans awarded by the former Department of Commerce. These loans accounted for $3.2 million of the $13.2 million potentially uncollectible loan balance as of June 30, 2013.

WEDC turns over loans that were awarded by the former Department of Commerce, and that WEDC considers uncollectible, to the Department of Administration, which works with the Department of Justice to pursue collection. Because any amounts collected are retained by the Department of Administration, WEDC writes off the loans it turns over to the Department of Administration for resolution. As a result, the write-off of these loans helped to decrease the amount of loans with repayments 90 days or more past due.

For loans it awards, WEDC may use an external collection agency to pursue collection of a loan before determining that the loan is uncollectible. Although amounts collected on such loans are remitted to WEDC, WEDC pays the collection agency for its services. Because FY 2011-12 was the first year that WEDC awarded loans, and because loan repayments are often not contractually required to begin for six months or more, few of the loans awarded by WEDC have become delinquent and been referred for collection.

At the time of our fieldwork, we identified only one $75,000 loan that WEDC had referred to an external collection agency. At that time, WEDC had not yet determined this loan to be uncollectible and was pursuing other options for collection, such as legal action against the loan recipient.

Loan Contract Amendments

From July 1, 2013, through December 31, 2013, WEDC deferred $2.1 million of the $13.2 million potentially uncollectible loan balance by completing loan contract amendments for 11 of the 49 loans with repayments 90 days or more past due as of June 30, 2013. Loan recipients may seek, and WEDC may approve, loan contract amendments for a variety of reasons. The most common loan contract amendments are those that defer the dates on which a loan recipient must make repayments on the loan. If the repayment dates are deferred, WEDC no longer considers the loan to be delinquent. As a result, contract amendments that defer the repayment dates reduce the amount of loans with repayments 90 days or more past due.

Early in FY 2013-14, WEDC developed a policy on amending loan contracts. Under the policy, when a loan recipient requests a loan contract amendment, WEDC staff review the request for completeness, prepare an amendment authorization form, and make a recommendation to WEDC management. After subsequent reviews by WEDC's "underwriter review group" and vice president of credit and risk, loan contract amendments recommended for approval are subject to final approval as follows:

- amendments for loans up to $1.0 million are approved by the chief executive officer;
- amendments for loans greater than $1.0 million and up to $10.0 million are approved by the Award Risk Committee, which consists of the chief executive officer, vice president of credit and risk, chief operating officer, chief financial officer, two WEDC board members, and two non-voting citizen members; and
- amendments for loans greater than $10.0 million are approved by the full WEDC board.

After final approval, the loan contract amendment is provided to the loan recipient for signature. Once the loan contract amendment is signed by the loan recipient, WEDC's loan and grant tracking system is updated to reflect the revised loan contract terms.

Historical information on the number and extent of loan contract amendments was not readily available because of limitations with WEDC's loan and grant tracking system. As noted, WEDC replaced that system in May 2014. We will assess WEDC's use of its new system and the effects on its monitoring of loans during our next biennial audit.

Loan Forgiveness

As noted, while repayment terms are included in the loan contract, a forgivable loan may be forgiven in whole or in part if certain conditions specified in the contract are met. During FY 2011-12 and FY 2012-13, WEDC staff did not perform forgiveness reviews to determine whether loan recipients met the specified conditions and, therefore, did not forgive any loans in whole or in part. WEDC staff stated that forgiveness reviews were not completed and loan forgiveness did not occur because WEDC did not have a policy in place during that time regarding loan forgiveness. When forgiveness reviews are not completed prior to the repayment date identified in the loan contract, the loan and grant tracking system considers the loans to be delinquent if repayments are not received. As of June 30, 2013, four loans were considered delinquent because WEDC staff did not complete forgiveness reviews. Between June 30, 2013, and December 31, 2013, WEDC staff developed a loan forgiveness policy and reviewed and forgave these four loans, in whole or in part, which accounted for $1.3 million of the $13.2 million potentially uncollectible loan balance as of June 30, 2013.

Reconciliation of Loan Activity

Although WEDC uses a separate loan and grant tracking system, loan-related activity is also recorded in its accounting system. However, no reconciliations between WEDC's loan and grant tracking system and accounting system were completed before November 2012. At the time of our fieldwork, WEDC conducted monthly reconciliations but did not have formal written procedures in place for the monthly reconciliation process. Documenting its procedures for completing this reconciliation will help ensure consistency, particularly if different staff need to complete the reconciliation due to turnover or for other reasons.

☑ Recommendation

We recommend the Wisconsin Economic Development Corporation:

- *establish delinquency rate goals that include both loan repayments 90 days or more past due and the entire loan balance for loans with repayments 90 days or more past due as percentages of the total outstanding loan balance for the loan portfolio, and include these goals into its overall approach for monitoring loans;*

- *develop formal written procedures for reconciling the loan and grant tracking system with the accounting system; and*

- *report to the Joint Legislative Audit Committee by January 15, 2015, on the status of its efforts to implement these recommendations.*

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September 17, 2014

Mr. Joe Chrisman, State Auditor
Legislative Audit Bureau
22 E. Mifflin Street, Suite 50
Madison, WI 53703

Dear Mr. Chrisman:

Thank you for the opportunity to respond to the Legislative Audit Bureau's ("LAB") financial audit of Wisconsin Economic Development Corporation ("WEDC") for the periods FY 2011-12 and FY 2012-13, and an update of certain information in report 13-7. We respectfully request that this letter be included with the report.

We appreciate that LAB shares our commitment to ensuring that taxpayer resources are used effectively to encourage economic development and growth in the State of Wisconsin. We welcome recommendations as another tool to improve our internal controls, processes and procedures.

This new audit details the significant progress WEDC has made in strengthening internal controls, processes and procedures, and notes many of the steps taken during the last two years including:

- the adoption of comprehensive financial and systems policies;
- the adoption of an awards administration policy and process that includes tiered award levels requiring management, board committee, and full board approval for major awards;
- the implementation of new award administration software;
- the hiring of key staff, including a VP of Credit and Risk with extensive lending experience and a Chief Financial Officer with experience in both public accounting and government finance administration;
- a major reduction in the number of delinquent loans and the amount of principal at risk; and
- a vigorous compliance program within the legal department.

As an audit of FY12 and FY13, the concerns raised in the audit report all occurred prior to January 1, 2014.

The financial report includes recommendations for improvements to WEDC's financial operations from FY12 and FY13. Consequently, we have already implemented, or are in the process of implementing, additional controls and procedures in all of the areas noted by LAB.

We are pleased to provide LAB, our Board, the Legislature, the public and our other stakeholders with an update on those improvements and our plans for continued improvements related to your recommendations, as follows:

LAB Recommendation 1 – ensure supporting documentation is maintained for its expenditures that demonstrates that each expenditure was incurred, was reasonable, and was approved.

WEDC believes that payments made were for expenditures that were incurred, reasonable and approved. We acknowledge that not all documentation was maintained to demonstrate this as WEDC was still developing office procedures and document storage processes during the time period under audit. In July 2013 WEDC adopted systems policy FIN 102 WEDC Payments, which outlines the responsibility for ensuring that appropriate supporting documentation is provided with all payment requests. We believe this policy, in conjunction with the newly established WEDC processes, addressed this concern. As a supplemental measure, we will add this to our internal monitoring plan for FY15.

LAB Recommendation 2 – ensure similar expenditures are consistently recorded in the accounting system in the appropriate account.

A well designed and well communicated list of account numbers and names used to organize accounting records, called the chart of accounts, is the backbone of any accounting system. Consistent use of the chart of accounts occurs when there is organization-wide understanding of the chart of accounts combined with review of individual transactions both before and after transactions are posted.

We have substantially improved organization-wide knowledge of the chart of accounts through better internal communication during the budget process and more consistent use of account numbers during the year. Additionally, there is regular review of the general ledger by the Controller, Chief Financial Officer, and department/division heads to ensure correct categorization of transactions. WEDC will continue to conduct detailed reviews of account balances during the year to ensure transactions are properly classified. In FY15 WEDC will also develop a *working budget* document for internal staff use to better communicate the account numbers in use and their purposes.

LAB Recommendation 3 – establish delinquency rate goals that include both loan repayments 90 days or more past due and the entire loan balance for loans with repayments 90 days or more past due as percentages of the total outstanding loan balance for the loan portfolio, and include these goals into its overall approach for monitoring loans;

With three years of activity as an organization, WEDC now has the historical information necessary to gauge the benchmarks used for evaluating our loan portfolio risk. WEDC's loan portfolio is much different than the portfolio of a bank and should be evaluated with this in mind. During FY15 staff will review the performance of the portfolio and work with our Board and Awards Administration Committee to identify the portfolio metrics that are the most meaningful for our unique loan portfolio.

LAB Recommendation 4 – develop formal written procedures for reconciling the loan and grant tracking system with the accounting system;

In July 2013, WEDC developed systems policy FIN 105 Financial Controls Policy, which identifies periodic reconciliation of account balances as a primary control to ensure account balances are properly stated. During FY13 and FY14, WEDC reconciled the payments made within the awards management system to the accounting system on a monthly basis. A new awards management system was deployed in FY14. Due to anticipated changes in the procedures because of the deployment, written procedures for the previous system were not developed at that time. WEDC staff will develop a formal accounting procedures manual during FY15. The goal of this manual is to identify and document key financial controls. We will ensure that this reconciliation is specifically included in this manual.

LAB Recommendation 5 – report to the Joint Legislative Audit Committee by January 15, 2015 on the status of efforts to implement these recommendations.

WEDC will provide a report on its implementation of these recommendations outlined to the Joint Legislative Audit Committee by January 15, 2015

We appreciate the diligence and dedication of LAB's staff and find great value in the fact that many of their recommendations have provided validation for the changes and improvements that have occurred during the last year.

With best regards,

Reed E. Hall

Reed E. Hall
CEO & Secretary