

Audit Report

---

**Maryland Technology Development Corporation**

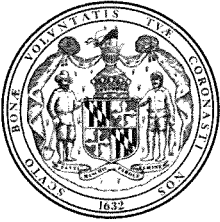
October 2012

---



**OFFICE OF LEGISLATIVE AUDITS**  
DEPARTMENT OF LEGISLATIVE SERVICES  
MARYLAND GENERAL ASSEMBLY

- 
- This report and any related follow-up correspondence are available to the public through the Office of Legislative Audits at 301 West Preston Street, Room 1202, Baltimore, Maryland 21201. The Office may be contacted by telephone at 410-946-5900, 301-970-5900, or 1-877-486-9964.
  - Electronic copies of our audit reports can be viewed or downloaded from our website at <http://www.ola.state.md.us>.
  - Alternate formats may be requested through the Maryland Relay Service at 1-800-735-2258.
  - The Department of Legislative Services – Office of the Executive Director, 90 State Circle, Annapolis, Maryland 21401 can also assist you in obtaining copies of our reports and related correspondence. The Department may be contacted by telephone at 410- 946-5400 or 301-970-5400.
-



Karl S. Aro  
Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES  
OFFICE OF LEGISLATIVE AUDITS  
MARYLAND GENERAL ASSEMBLY

Bruce A. Myers, CPA  
Legislative Auditor

October 11, 2012

Senator James C. Rosapepe, Co-Chair, Joint Audit Committee  
Delegate Guy J. Guzzone, Co-Chair, Joint Audit Committee  
Members of Joint Audit Committee  
Annapolis, Maryland

Ladies and Gentlemen:

We have audited the Maryland Technology Development Corporation (TEDCO) for the period beginning July 1, 2009 and ending May 21, 2012. TEDCO provides certain financial assistance to early-stage technology businesses, funds development and patenting of new technologies at research universities, and promotes State-funded stem cell research and cures through grants and loans to private and public entities in the State.

Our audit disclosed that TEDCO lacked adequate grant monitoring procedures to ensure that stem cell grant expenditures were spent in accordance with the grant agreements. Additionally, TEDCO did not adequately monitor the potential repayment of certain technology development grant funds used to develop profitable new technologies by the grantees, as provided for in the related agreements.

TEDCO's response to this audit is included as an Appendix A to this report. Auditor comments related to TEDCO's response can be found in Appendix B. We wish to acknowledge the cooperation extended to us during the course of this audit by TEDCO.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Thomas J. Barnickel III".

Thomas J. Barnickel III, CPA  
Acting Legislative Auditor



## **Background Information**

### **Agency Responsibilities**

The Maryland Technology Development Corporation (TEDCO) was created by the Maryland General Assembly in 1998 as a public instrumentality of the State to help commercialize the results and products of scientific research and development conducted by higher education institutions and private sector organizations, as well as to promote entrepreneurship and the creation of jobs in technology-related industry. In doing so, TEDCO aims to create and sustain business throughout all regions of the State. TEDCO is governed by a 15-member Board of Directors, including the Secretary of the Department of Business and Economic Development. The remaining 14 members are appointed to the Board by the Governor with the advice and consent of the Maryland Senate.

To achieve its goals, TEDCO provides certain financial assistance to early-stage technology businesses, and funds development and patenting of new technologies at research universities. TEDCO also develops relationships with federal research facilities in the State and helps companies pursue research funds from federal and other sources.

The Maryland Stem Cell Research Commission (MSCRC) was established by law in 2006 as an independent entity within TEDCO to provide oversight for the Maryland Stem Cell Research Fund (MSCRF). The MSCRC is governed by a 15 member Board of Directors, including the Attorney General. The remaining 14 members are appointed by the Governor, the General Assembly, the University System of Maryland, and Johns Hopkins University. The MSCRF was established to promote State-funded stem cell research and cures through grants and loans to public and private entities in the State.

According to its records, TEDCO's fiscal year 2011 expenses primarily funded through State general funds were \$16.8 million, including \$979,000 in administrative expenses.

### **Financial Statements**

In accordance with the Economic Development Article, Title 10-414 of the Annotated Code of Maryland, TEDCO engaged an independent certified public accounting firm to audit its financial statements for fiscal years 2010 and 2011. In the related audit reports, the firm stated that the financial statements presented fairly, in all material respects, the financial position of TEDCO as of the related

fiscal year, and the changes in its net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

## **Status of Finding From Preceding Audit Report**

Our audit included a review to determine the status of the three findings contained in our preceding audit report dated February 3, 2010. We determined that TEDCO satisfactorily addressed two of these findings. The remaining finding is repeated in this report.

## **Findings and Recommendations**

### **Grant Monitoring**

#### **Finding 1**

**TEDCO lacked adequate monitoring procedures and controls over stem cell research and technology development grants.**

#### **Analysis**

TEDCO lacked adequate monitoring procedures and controls over stem cell research and technology development grants. Specifically, our audit disclosed the following conditions:

- TEDCO did not verify that stem cell research grant funds, for which fiscal year 2011 reported awards totaled \$11.2 million, were spent as intended by the grant agreements. Although stem cell research grantees provided required expenditure reports on a regular basis, which were reviewed by TEDCO, the review process did not include an independent verification of the accuracy of the reports to supporting documentation. Consequently, TEDCO lacked adequate assurance regarding the propriety of the grant expenditures, which consisted primarily of payroll costs.
- TEDCO did not ensure that all required grantee reports of revenue related to projects funded by technology development grants were received. Generally, the technology development grant agreements included a five-year grant repayment provision, entitling TEDCO to three percent of the grantee's quarterly revenues from activities related to the respective research or development. Our test of 10 technology development grants totaling \$775,000 that were subject to repayment during our audit period disclosed that, for 9 grants totaling \$675,000, the grantees had not submitted all the

required revenue reports. For example, as of June 30, 2012, two grantees had not submitted any reports for the four-year period such reports were required. Without these reports, TEDCO lacked adequate assurance that all project revenue due was received. According to TEDCO records, in fiscal year 2011, technology development grants awarded totaled \$2.4 million and the balance of grants awarded and subject to the five-year repayment provision as of March 23, 2012 was approximately \$6 million (relating to approximately 90 grantees).

The grant agreements authorize TEDCO to inspect, audit and examine grantee records as a means to verify grant-related activity.

Similar conditions related to grant expenditure monitoring were commented upon in our preceding audit report. In its response to that report, TEDCO agreed to obtain source documentation from grantees on a test basis to determine if funds were spent in accordance with related agreements and take appropriate action to ensure all required expenditure reports were submitted by grantees. Although TEDCO did take steps to enhance certain processes, such as the review of technology development grant expenditures, such reviews were not instituted for stem cell grant expenditures.

#### **Recommendation 1**

##### **We recommend that TEDCO**

- a. take appropriate action to verify stem cell grantee expenditures (such as, obtaining supporting documentation or through audits of grantee records) (repeat); and**
- b. obtain the aforementioned revenue reports and ensure that, in the future, all grantees submit required revenue reports.**

## **Audit Scope, Objectives, and Methodology**

We have audited the Maryland Technology Development Corporation (TEDCO) for the period beginning July 1, 2009 and ending May 21, 2012. The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine TEDCO's financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations. We also determined the status of the findings contained in our preceding audit report.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. The areas addressed by the audit included grants, disbursements, and payroll. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of TEDCO's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

Our audit did not include an evaluation of internal controls for federal financial assistance programs and an assessment of TEDCO's compliance with federal laws and regulations pertaining to those programs because the State of Maryland engages an independent accounting firm to annually audit such programs administered by State agencies, including TEDCO.

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

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

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

This report includes a condition that we consider to be a significant deficiency in the design or operation of internal control that could adversely affect the TEDCO's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our audit

did not disclose any significant instances of noncompliance with applicable laws, rules, or regulations. Another less significant finding was communicated to TEDCO that did not warrant inclusion in this report.

TEDCO's response, to our findings and recommendations, is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise TEDCO regarding the results of our review of its response.



October 4, 2012

Mr. Thomas J. Barnickel III, CPA  
Acting Legislative Auditor  
Department of Legislative Services  
301 West Preston Street  
Room 1202  
Baltimore, Maryland 21201

Dear Mr. Barnickel:

Thank you for the opportunity to respond to the draft audit of the Maryland Technology Development Corporation (TEDCO) for the period beginning July 1, 2009 and ending May 21, 2012. I offer the following responses to the findings:

**Finding 1**

- a) TEDCO respectfully disagrees with the classification of “repeat” of this Finding as it relates to the Stem Cell program. In our response to a similar Finding during our last DLS audit in 2009, TEDCO stated that we did not have the existing staff capacity to audit each of our grantees. However, in order to address this Finding, we stated that we would obtain source documentation from our awardees on a test basis and review such to determine that grant funds were spent in accordance with the grant agreements.<sup>1</sup>

As we considered this approach, we determined that it would be better to obtain a written statement of expenses from each grantee rather than rely on a report from the Principal Investigator (scientific researcher). With internal grantee auditing controls and a clear incentive to comply with TEDCO grants, we felt that this approach would be sufficient. Moreover, obtaining such reports allowed us to verify the expenses of **ALL** grants rather than just a sampling, an outcome we thought would be welcomed by the DLS auditors.

To this end, TEDCO created the Financial Status Report (attachment 1)<sup>2</sup> that is received as part of each grantee’s annual progress report. This report reflects both the budget that was approved in each stem cell grant agreement and the total expenditures for each line item of the approved budget during that reporting year. This Financial Status Report is required to be signed by an authorized official of the grantee’s Finance Office instead of the Principal Investigator, thereby assuring a third-party review.

<sup>1,2</sup> See Appendix B for related auditor comment.



These grants are typically disbursed over a period of two to three years, and any subsequent grant payments are not made without the submission of an approved Financial Status Report.

Further assurances that grant funds are used for their approved purposes can be found in the grant agreements themselves. Representations, Warranties and Covenants Section 3.01(i) defines the Project Budget, while Section 3.02 (b) limits the use of grant proceeds to "Eligible Project Costs", defined to mean those costs incurred for the research project in question in accordance with the Project Budget approved by TEDCO. Having these reports signed by an authorized official of the grantee's Finance Office instead of the Principal Investigator was an additional step we took towards assuring the receipt of accurate expenditure data.

TEDCO feels strongly that we have taken the additional steps we stated in the 2009 audit response to implement adequate procedures, controls and accountability of our stem cell grants, and that the funds provided are being spent in accordance with the approved budget in such agreements. The Financial Status Report, signed by an authorized official of the grantee's Finance Office and reinforced by the grant agreements' provisions, provides assurance that these funds are being spent in accordance with the approved budget as provided in the grant agreement.

During the exit conference meeting with our DLS audit team, we explained our rationale for implementing the additional steps we took regarding obtaining source documentation. While there was recognition that we did implement additional steps to address this Finding, we now understand the degree and type of source documentation that is being sought by the auditors. Therefore, we will begin to obtain, on a test basis, documentation that will satisfy the concern raised in this Finding.

- b) TEDCO agrees with this part of the Finding and has begun to implement a new process for obtaining revenue reports from our grantees.

If you have any questions, please contact me 410-715-4163.

Sincerely,

A handwritten signature in black ink, appearing to read "Robert A. Rosenbaum", with a long horizontal line extending to the right.

Robert A. Rosenbaum  
President and Executive Director

Cc: Jack Lewin III, Chair, Board of Directors, TEDCO  
Margaret Conn Himelfarb, Chair, Maryland Stem Cell Research Commission

## **APPENDIX B**

### **Auditor's Comments on Agency Response**

<sup>1</sup>In its response, TEDCO indicated that it disagreed with the classification of the Finding as a repeat. As noted in the Finding, in response to our preceding audit report, TEDCO had agreed to obtain source documentation from grantees on a test basis to determine if funds were spent in accordance with the related grant agreements. Since this verification method was not employed and other approaches did not sufficiently ensure the accuracy of the reported expenditures, we considered the Finding to be a repeat.

<sup>2</sup>The attachment referenced in TEDCO's response was not included in the report.

AUDIT TEAM

**William R. Smith, CPA**  
Audit Manager

**W. Thomas Sides**  
Senior Auditor

**Nathan H. Suffin**  
Staff Auditor