STATE OF CONNECTICUT

AUDITORS' REPORT
OFFICE OF THE STATE COMPTROLLER
STATE FINANCIAL OPERATIONS
FOR THE FISCAL YEAR ENDED
JUNE 30, 2012

AUDITORS OF PUBLIC ACCOUNTS

JOHN C. GERAGOSIAN ❖ ROBERT M. WARD

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STATE OF CONNECTICUT

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June 25, 2013

INTRODUCTION

We have examined the records of the Comptroller of the State of Connecticut as they pertain to the central accounting of state financial operations, on a budgetary basis of accounting, for the fiscal year ended June 30, 2012. The audit certification on the Comptroller's civil list financial statements, the audited civil list financial statements themselves, and the related auditors' report on compliance and internal control over civil list financial reporting are included in a separate report entitled *Annual Report of the State Comptroller – Budgetary Basis*, for the fiscal year ended June 30, 2012. Throughout this report, we will refer to various financial statements and schedules contained in this annual report, which is hereinafter referred to as the Comptroller's 2012 Annual Report.

We have also examined the records of the Comptroller of the State of Connecticut as they pertain to the State of Connecticut's financial position and results of operations on the basis of generally accepted accounting principles. The audit certification on the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, the aggregate remaining fund information and the respective budgetary comparison for the General Fund and the Special Transportation Fund, and the respective changes in financial position and cash flows, where applicable, of the State of Connecticut, which collectively comprise the state's basic financial statements are included in a separate report entitled *Comprehensive Annual Financial Report* (CAFR) as of and for the year ended June 30, 2012.

This report consists of the Comments and Recommendations, which follow. This report contains an explanation of the difference between the two reports and includes certain findings pertaining to those reports and with the internal controls and procedures applied to the state's financial reporting.

COMMENTS

OFFICERS:

Since January 5, 2011 Kevin Lembo and Martha Carlson have served as State Comptroller and Deputy Comptroller, respectively.

BUDGETARY BASIS REPORT:

The Comptroller's 2012 Annual Report covers the financial operations of the 2011-2012 fiscal year under a biennial budget adopted by the 2011 General Assembly, as revised by the 2012 General Assembly, including the financial accounting for the budget plans of the General Fund and Special Transportation Fund, as it applies to the 2011-2012 audit period.

The financial position as of June 30, 2012, and the 2011-2012 cash transactions of all state civil list funds, accounted for centrally in the records of both the Office of the State Comptroller and State Treasurer, are shown in Exhibit A and Schedule A-1, respectively, of the Comptroller's 2012 Annual Report. The financial position of the General Fund at June 30, 2012, together with a summary of operations for the year then ended, are shown in Exhibit B and Schedule B-1, respectively, of the Comptroller's 2012 Annual Report. Corresponding statements for the Special Transportation Fund are shown in Schedules C-2 and C-3, respectively, of the Comptroller's 2012 Annual Report. A summary of state bonds and notes outstanding as of June 30, 2011, the changes thereto, and the authorizations for future borrowings are shown in Schedules E-3, E-4, and E-5 of the Comptroller's 2012 Annual Report.

The Comptroller prepares the financial statements of the state's civil list funds on a modified cash basis of accounting, consistent with the prior year. The accounting basis used by the State of Connecticut was adopted by the Comptroller under the authority granted by Article Fourth, Section 24, of the Constitution of the State of Connecticut and with the recognition of legislative authorizations. The modified cash basis of accounting permits an accrual of revenues at fiscal year end, which includes the collections in July of Indian gaming payments and certain taxes levied as of June 30th, and requires that expenditures be recorded in the year in which disbursements are made, provided recognition is given to continuing appropriations.

Those taxes for which July collections are accrued include sales and use taxes, corporation taxes, gross earnings taxes on utility and petroleum companies, real estate conveyance taxes and taxes on alcoholic beverages, cigarettes, gasoline and special motor fuels. As provided by various subsections of Section 3-114 of the General Statutes, these taxes are accrued if received by the commissioner of the Department of Revenue Services not later than five business days following the last day of July.

Under the modified cash basis of accounting used by the Comptroller, restricted revenues of the General and Special Transportation Funds are recognized when earned through the expenditure of grant funds, rather than when received or awarded. Receivables reported by the Comptroller include federal and other grants receivable recorded in connection with federally supported programs or capital projects for which federal or other outside participation is available; loans and notes receivable from local governments, nonprofit corporations, businesses or individuals; and the accounts receivable of the University of Connecticut Health Center. Such receivables have been reported by the Comptroller as assets of the funds financing the projects or programs involved and are fully reserved on the balance sheet, except within the Grants and Restricted Accounts Fund and the Transportation Grants and Restricted Accounts Fund where the federal and other grants receivable are the source of financing for restricted appropriations established for the purposes of the grants involved. These restricted revenues are recognized by the Comptroller when earned through the expenditure of grant funds, rather than when received or awarded. In addition, interest income of the Special Transportation Fund is accrued at fiscal year end pursuant to the terms of a Special Tax Obligations Bond Indenture dated September 15, 1984.

In maintaining state accounting records and in preparing financial statements, the Comptroller, consistent with prior years, was guided by the aforementioned requirements and authorizations of state fiscal statutes as regards the method of accounting and fund classification. For this reason, therefore, the financial statements contained in the *Annual Report of the State Comptroller - Budgetary Basis* are not, nor are they intended to be, in accordance with generally accepted accounting principles (GAAP). In order for the Comptroller to follow such principles, among other things, expenditures would have to be recorded on an accrual rather than cash basis, all non-civil list funds and component units of the state would have to be included in the financial statements, all agencies' assets and contingent and long term liabilities would have to be recognized, and appropriate footnote disclosures would have to be made in the financial statements.

The use of the modified cash basis of accounting for the budgetary basis report has inherent weaknesses in that all financial activity for the fiscal year is not being accounted for within that fiscal year. Under the modified cash basis of accounting, revenues are not being recognized when they are measurable and available for use in the fiscal period, and expenditures are not being recognized as soon as they create a demand on current financial resources (when the liability is incurred). This results in reported financial performance being based on the timing of cash inflows or outflows. The timing of these transactions is set by statute or management.

In March 2005, the American Institute of Certified Public Accountants issued an interpretation of its professional auditing standards affecting those governments that prepare financial statements using the cash, or modified cash basis of accounting, rather than reporting their financial activity in accordance with GAAP. As a result, those statements must conform to the applicable disclosure requirements of GAAP in order to avoid receiving an adverse audit opinion. This would require management to prepare and incorporate a management discussion and analysis, notes to the financial statements, and disclosure of infrastructure assets into the budgetary basis report. Because the Office of the State Comptroller has not done such, we have been required to render such an opinion on the *Annual Report of the State Comptroller - Budgetary Basis* for the fiscal year ending June 30, 2012.

The bond indenture for the special tax obligation bonds for transportation infrastructure purposes requires the Special Transportation Fund to be audited by a firm of independent public accountants of recognized standing. Such audit shall be completed within 120 days after the close of each fiscal year. Our audit of the budgetary basis report relies upon the work of other auditors for the Special Transportation Fund and the Transportation Special Tax Obligations Fund. The work performed by other auditors was not completed in time to meet the December 31, 2012 deadline of the budgetary basis report. As a result, our audit opinion included a scope limitation in respect to the financial statements of the Special Transportation Fund and the Transportation Special Tax Obligations Fund. The audit of the Special Transportation Fund and the Transportation Special Tax Obligations Fund was completed February 27, 2013.

COMPREHENSIVE ANNUAL FINANCIAL REPORT:

In order to comply with GAAP, the Office of the State Comptroller has issued a separate *Comprehensive Annual Financial Report* showing the State of Connecticut's financial position and results of operations in accordance with GAAP requirements. It has done so since the fiscal year ended June 30, 1988. This report, however, was always issued in addition to the *Annual Report of the Office of the State Comptroller - Budgetary Basis*, which presents the state's financial operations as budgeted by the General Assembly. Because differing accounting bases are followed in preparing the two reports, substantial variances can occur in the presentation of the state's financial position as well as its operations. The CAFR uses the modified accrual basis of accounting for all governmental activities, and the full accrual basis for business type activities. Under the modified accrual basis, revenues are recognized when they are both measurable and available to finance expenditures of the fiscal period. Expenditures for each agency are recognized in the period in which a transaction creates a demand on current financial resources, as compared to when cash is disbursed in the modified cash basis.

As explained above, the Office of the State Comptroller is required by statute to follow a practice of recording the accrual of certain revenues, notably income and corporation tax payments, without a corresponding accrual of expenditures in the General Fund. This accounting practice resulted in the accrual of more than $328,800,000 in revenues, which under a cash basis system of accounting would be recorded in the 2012-2013 fiscal year. If there had been a similar accrual of expenditures as required by GAAP, there would have been added to General Fund liabilities salaries and fringe benefits payable and accounts payable that are estimated to be as high as $1,500,100,000 over the modified cash basis of accounting during the first year only of any conversion to GAAP budgeting by the state.

As also explained above, grant receivables are recorded as revenues when earned through the expenditure of grant funds. If there had been a similar accrual of grant receivables and accounts receivable as required by GAAP, these expenditure accruals would be offset by additional revenue and receivable accruals totaling $682,900,000 under GAAP. The net result of these effects is an estimated deficit in the Unreserved Fund Balance of the General Fund (GAAP Basis) totaling $1,146,000,000 as of June 30, 2012. This is compared to an estimated deficit totaling $1,748,900,000 as of June 30, 2011. A schedule illustrating these differences, with a comparison to the previous fiscal year, is presented below:

Nearest Thousand Dollars	June 30, 2011	June 30, 2012
Unreserved Fund Balance (Deficit) -		
Modified Cash Basis	$ 0	$ 0
Adjustments to GAAP Basis:		
Additional Assets:		
Reduction of Income Tax Accrual	(525,300,000)	(328,100,000)
Eliminate Corporation Tax Accrual	(5,400,000)	(4,400,000)
Additional Taxes Receivable	4,200,000	3,700,000
Net Accounts Receivable	307,900,000	299,900,000
Federal and Other Grants Receivable	542,100,000	364,000,000
Due From Other Funds	19,600,000	19,000,000

Total Additional Assets	$ 343,100,000	$ 354,100,000
Additional Liabilities:		
Salaries and Fringe Benefits Payable	(245,900,000)	(114,600,000)
Accounts Payable - Dept. of Social Services	(711,900,000)	(588,800,000)
Accounts Payable - All Other	(844,100,000)	(543,700,000)
Payable to the Federal Government	(186,900,000)	(176,600,000)
Due to Other Funds	(103,200,000)	(76,400,000)
Total Additional Liabilities	$(2,092,000,000)	$(1,500,100,000)
Unreserved Fund Balance (Deficit) - GAAP Basis	$(1,748,900,000)	$(1,146,000,000)

As reported in the *Comprehensive Annual Financial Report*, on a government-wide basis which takes into account all non-fiduciary state assets and liabilities (all funds, in addition to the General Fund), the deficit for the 2011-2012 fiscal year totaled $10,555,813,000. This is compared to a deficit of $9,856,474,000 for the 2010-2011 fiscal year. The $699,339,000 increase in the deficit was primarily caused by a decrease of $857,990,000 in cash, deposits with the federal government and investments, and by an increase of $1,023,789,000 in the state's long term liabilities, which include the issuance of debt and pension and other post retirement liabilities. These increases were offset by a $361,868,000 increase in receivables, a $170,314,000 increase in the value of capital assets, a $278,256,000 decrease in accounts payable and a $336,493,000 decrease in the liability for escheated property.

A schedule presenting the deficit on a government-wide basis, from the CAFR Statement of Net Assets - Total Net Assets, for the past ten fiscal years is presented below:

Fiscal Year Ended, June 30, 2003	$(1,471,912,000)
Fiscal Year Ended, June 30, 2004	$(1,780,341,000)
Fiscal Year Ended, June 30, 2005	$(1,392,024,000)
Fiscal Year Ended, June 30, 2006	$ (784,864,000)
Fiscal Year Ended, June 30, 2007	$ (242,540,000)
Fiscal Year Ended, June 30, 2008	$(2,203,449,000)
Fiscal Year Ended, June 30, 2009	$(5,065,237,000)
Fiscal Year Ended, June 30, 2010	$(9,388,402,000)
Fiscal Year Ended, June 30, 2011	$(9,856,474,000)
Fiscal Year Ended, June 30, 2012	$(10,555,813,000)

The significant increase in the deficit since the fiscal year ended June 30, 2007 was primarily the result of an increase in noncurrent liabilities. Total noncurrent liabilities as reported on the CAFR Statement of Net Assets increased from $19,178,345,000 as of June 30, 2007, to $28,850,918,000 as of June 30, 2012. Changes in government accounting standards required the posting of the state's post-employment health care liability, which totaled $5,755,731,000, as of June 30, 2012. In addition, total bonds and notes outstanding increased from $13,720,990,000 as of June 30, 2007 to $18,708,725,000 as of June 30, 2012.

Implementation of GAAP Basis Budgeting:

A major impediment to the widespread use and acceptance of the State's *Comprehensive Annual Financial Report* was the failure of the legislative budget plan to be prepared and enacted in accordance with GAAP. In that way, the CAFR will present, in a unified format, both the budgetary and actual financial operations of the State of Connecticut with the budget plan reflecting most of the various receivable, payable and accrual activity noted above. As we have explained in previous reports, a succession of attempts were made to accomplish this end since the 1993 General Assembly passed Public Act 93-402, codified as Section 3-115b of the General Statutes. Public Act 93-402 called for the implementation of generally accepted accounting principles for the fiscal year commencing July 1, 2005. Statutory deadlines to implement GAAP were extended from July 1, 1995 to July 1, 2009 by a succession of public acts passed by the General Assembly. The statutory deadline for implementation was eliminated by the passage of Public Act 08-111, which eliminated the requirements to implement GAAP and to amortize the accrued and unpaid expenses and liabilities by a certain date and allowed more incremental implementation. Most recently, Section 3-115b of the General Statutes was revised by the passage of Public Act 11-48, during the 2011 Session of the General Assembly.

As a result of Public Act 11-48, the state is implementing GAAP based budgeting as follows:

1. Beginning with the biennial budget for the 2013-2014 and 2014-2015 fiscal years, the Governor must propose, and the General Assembly enact, a state budget that must exclude as revenues the estimated unappropriated prior year surplus, and include as expenditures, the amount necessary to extinguish any unreserved negative balance in any budgeted fund as reported by the prior year CAFR.

2. The opening combined balance sheet for all budgeted funds for the 2013-2014 fiscal year shall be based on GAAP as of July 1, 2013, which will include a charge on the opening combined balance sheet of the accrued and unpaid expenses and liabilities of the initial year of GAAP budgeting.

3. At the close of the 2013-2014 fiscal year and thereafter, if there is a shortfall of revenue relative to expenses, a negative unreserved balance in the balance sheet would result, illustrating a budget deficit. In addition, it requires the following year’s budget sum of anticipated revenue plus the unreserved fund balance, as determined by the audited financial statements, to be equal to or greater than appropriation requirements for that fiscal year; if they do not, a budget deficit would be identified for that following year, and if large enough require the Governor to submit a deficit mitigation plan.

4. Beginning with the 2013-2014 fiscal year, the state is required to begin to amortize the accumulated GAAP deficit over a period of 15 years. Any unappropriated General Fund surplus at the end of any fiscal year must be applied to the annual increment of the accumulated GAAP deficit prior to allocating it for any other purpose. It is estimated that the annual amount required from general fund appropriations to amortize the accumulated deficit will be $79,800,000.

The Core-CT System, Other State Accounting Systems and GAAP Basis Budgeting:

Our previous audit noted certain technical issues and complications in the Core-CT system (the states automated financial system) that needed to be resolved prior to the July 1, 2013 implementation of GAAP based budgeting. Our current audit has reviewed the progress made toward resolving these issues. The Office of Policy and Management and the Office of the State Comptroller have determined the necessary changes to Core-CT processes to accrue receivables and payables and provide for budgetary control and reporting on a GAAP basis. The method adopted is a compromise between the needs of the Office of Policy and Management and the State Comptroller and was designed to minimally disrupt Core-CT operations and avoids requiring the ledgers for both old and new fiscal years to be open at the same time.

The method adopted utilizes the current procedures in Core-CT and will accrue receivables when billings or accounts receivable journal entries are posted. It will accrue expenditures when payment vouchers, payrolls, or general ledger journal entries are posted according to the receipt date, and accrue the salary and fringe benefits payable, including the accumulated liability for sick and vacation leave benefits at the close of the fiscal year. We note that the method described above does not provide monthly reporting on a GAAP basis, and the statutory requirements applicable when a deficit is projected will continue to rely on budgetary basis accounting. To provide GAAP reporting compliant with the requirements of the Government Accounting Standards Board, and to produce the annual CAFR, the manual entry of miscellaneous accounting information not available on the Core-CT system is still required.

The method adopted will provide financial statements available by September 30th of each year that reflect most of the GAAP basis receivables and payables. As required by Public Act 11-48, the State Comptroller will issue unaudited annual financial statements by September 30th for all budgeted funds, on a GAAP basis. These will include a statement of all appropriations and expenditures for the fiscal year itemized by each appropriation account of each budgeted agency; a statement of state revenues classified as far as practicable as to budgeted agencies, sources and funds during such year; a statement setting forth the total tax receipts of the state during such year; and a balance sheet as of the close of the fiscal year.

Public Act 11-48 also defined the budget as an estimate of proposed expenditures for a given period or purpose and the means of financing them, determined for the fiscal year ending June 30, 2014, and each fiscal year thereafter on the basis of generally accepted accounting principles, as administered by the Governmental Accounting Standards Board. We note that the method adopted for GAAP reporting does not carry forward accruals from one fiscal year to the following fiscal year on the Core-CT system. This is a compromise method adopted to avoid significant operational changes in Core-CT processes. As a result, budgets are not being controlled on a GAAP basis, and monthly reporting on the Core-CT system is not on a GAAP basis. As we noted in our previous report, state agencies make benefit or provider payments from agency checking accounts that are not directly reflected in the Core-CT system. The Medicaid program at the Department of Social Services is a particular illustration of the weakness of this method, due to the timing and the significant dollar amounts of its bimonthly billings. As a result, significant receivables and payables can accrue at month or year end that are not promptly reported on the Core-CT system.

FUND FINANCIAL DATA – BUDGETARY BASIS

The State of Connecticut uses fund accounting that places all related assets, liabilities and residual equity within a single self-balancing set of accounts to ensure and demonstrate fiscal accountability and legal compliance. The following is a summary of activity for the state's major funds and fund groups, on the budgetary basis, for the 2011-2012 fiscal year:

GENERAL FUND:

The General Fund is the chief operating fund of the state. It is used to account for all financial resources that are not required to be accounted for in other funds and which are spent for those services normally provided by the state.

The financial position of the General Fund, on a budgetary basis at June 30, 2012, together with a summary of operations recorded for the year then ended, are shown in Exhibit B and Schedule B-1, respectively, of the Comptroller's 2012 Annual Report.

General Fund operations were conducted under a biennial budget plan, which estimated revenues and provided for expenditures of the 2011-2012 and 2012-2013 fiscal years. Public Act 11-06 included revenue estimates and appropriations for the 2011-2012 and 2012-2013 fiscal years. The act incorporated significant changes from prior year budgets with an estimated $1.5 billion increase in revenues and reductions in current services estimated spending that included an estimated $1.0 billion for each year in state employee union concessions.

Revenue enhancements included increasing the number of brackets for the personal income tax and increasing the maximum rate to 6.7 percent. The sales tax was increased to 6.35 percent, with numerous exemptions eliminated. A surcharge of 20 percent was imposed on the corporation tax, and there were increases in taxes on cigarettes and alcoholic beverages.

The budget was passed on May 3, 2011 by the General Assembly and, as noted, included $1.0 billion in state employee union concessions that were not specified. At the time the budget was passed, collective bargaining negotiations were underway. Following the outcome of collective bargaining negotiations on May 13, 2011, the budget plan was amended by Public Act 11-61, passed on June 7, 2011, to adjust for the approved concessions, which estimated at $700 million, fell short of the 1.0 billion target.

Following the failure of unionized state employees to approve the agreement resulting from those negotiations and entering the start of the 2011-2012 fiscal year with a budget out of balance, the General Assembly met in special session on June 30, 2011 and passed Public Act 11-1 of the June Special Session, which revised appropriations, granted the Governor temporary expanded rescission authority, required the preparation of spending reduction plans, and made other measures to balance the budget. Public Act 11-1 provided that many of these changes were to be repealed if the unions approved an agreement. These provisions were not implemented, however, as a second agreement was approved by union membership on August 22, 2011, and was deemed approved by the General Assembly as of that date, in accordance with the provisions of subsection 12 of Public Act 11-1, which provided that if the General Assembly does not call itself into special session in accordance with that subsection, such agreement shall be deemed approved by the General Assembly,

Under budget procedures customarily in effect, the estimates of revenues and the budgeted appropriations, taken in conjunction with whatever surplus or deficit was carried over from the preceding fiscal period, after consideration of any statutorily required transfers, give rise to an anticipated surplus or deficit projected through the end of the fiscal year. The original budget plan for the 2011-2012 fiscal year as reported by the Comptroller may be expressed as follows:

Estimated Revenues, 2011-2012, as Revised by the Committee on Finance, Revenue and Bonding		$18,788,600,000
Budgeted Appropriations, 2011-2012	$19,485,646,329	
Estimated Lapsing Appropriations	(777,911,579)	
Net Appropriations		18,707,734,750
Anticipated Surplus (Deficit), June 30, 2012		**$ 80,865,250**

Changes were made in the 2011-2012 budget by Public Act 11-1 passed in the October 20, 2011 Special Session of the General Assembly, and by Public Act 12-104, passed during the 2012 Session of the General Assembly. These changes consisted of an estimated $8.5 million loss in revenues from modifications to tax credits and deficiency transfers with no net impact on total appropriations.

The actual results of the operations of the 2011-2012 fiscal year are presented in Schedule B-1 of the Comptroller’s 2012 Annual Report. We have previously described the differences between the resulting financial operations by accounting on the budgetary basis as compared to the GAAP basis. An analysis of budgeted General Fund accounts follows:

Actual Budgeted Revenues, 2011-2012		$18,561,633,086
Appropriations, 2011-2012	$19,692,664,582	
Add/(Deduct)		
Appropriations Lapsed	(780,679,843)	
Net Appropriations		18,911,984,739
Balance		(350,351,653)
Prior Year Budgeted Appropriations Continued to 2011-2012 Fiscal Year		200,985,128
Miscellaneous Adjustments		5,849,845
Surplus (Deficit)		(143,516,680)
Release of Reserved Fund Balance		143,516,680
Unappropriated Surplus, June 30, 2012, per Schedule B-1		**$ 0**

The variances between the actual results of operations and the original budget plan may be explained as follows:

1. Actual revenues were some $226,967,000 less than originally estimated. This was primarily from a shortfall in personal income taxes of $239,780,000; in addition, tax refunds were $85,171,000 greater than budgeted. Other shortfalls in revenues occurred in cigarette and tobacco taxes at $22,795,000, and in taxes on public service corporations at $18,303,000. In other revenues, Indian gaming payments received were $30,855,000 less than budgeted and refunds of payments were $47,076,000 greater than budgeted. The decrease in revenues was partly offset by certain tax revenues that were above the original estimates: sales and use at $41,116,000, inheritance and estate at $33,700,000, oil companies at $52,967,000 and real estate conveyance at $17,231,000. In addition, there were other revenues above the original estimates: transfers from special revenue at $25,357,000, and $28,965,000 in miscellaneous revenues.
2. Appropriations showed an increase of approximately $207,018,000 from the budget plan reported by the Comptroller. The increase was primarily from some $6,033,000 in appropriation adjustments, and $200,985,128 in prior year appropriations carried forward to the succeeding fiscal year.
3. Lapsed appropriations were some $2,768,000 greater than estimated, the result of an effort to reduce general state expenditures.

A statement of changes in the unappropriated surplus account of the General Fund for the fiscal year ended June 30, 2012, is presented in Schedule B-1 of the Comptroller's 2012 Annual Report. It should be noted that Section 4-30a of the General Statutes provides that the unappropriated surplus that remains in the General Fund at the end of the fiscal year, after any amounts required by law to be transferred for other purposes have been deducted, shall be deposited to the Budget Reserve Fund, provided that the amount so transferred shall not cause the balance in such fund to exceed ten percent of the net General Fund appropriations for the fiscal year in progress.

In accordance with Section 28 of Public Act 12-104, $222,393,607 of the reserve fund balance from June 30, 2011 was transferred to the Budget Reserve Fund in June 2012. Public Act 12-104 amended previous legislation that required a surplus to be applied toward the repayment of the 2009 economic recovery notes. Subsequent to the close of the 2011-2012 fiscal year, $143,516,680 was transferred from the Budget Reserve Fund to the General Fund to eliminate the deficit. At the close of the fiscal year ended June 30, 2012, the balance in the Budget Reserve Fund totaled $93,454,180.

Section 46 of Public Act 11-48 requires the State Comptroller, if an unappropriated surplus exists in the General Fund after the close of the fiscal year, to establish a reserve of $75 million and $50 million, for the fiscal years ended June 30, 2012 and 2013, respectively, to be applied to any net increase in the unreserved negative fund balance if necessary to ensure that those budgets will remain balanced on a GAAP basis when year-end GAAP adjustments are made, before allocating the balance as otherwise required. However, due to the lack of any General Fund surplus at the close of the 2011-2012 fiscal year, the $75 million reserve was not established.

General Fund Revenues:

Realized budgeted revenues in the General Fund for the 2011-2012 fiscal year totaled $18,561,633,086, as shown in Schedule B-1 of the Comptroller's 2012 Annual Report. This represented an increase in revenues of $854,178,759 or 4.8 percent as compared to the realized budgeted revenue total reported by the Comptroller for the preceding 2010-2011 fiscal year.

The budgeted revenue categories that showed the greatest change during the fiscal year under audit were as follows:

	Nearest Thousand Dollars
Taxes:	
Personal Income	$ 1,064,389,000
Sales and Use	476,886,000
Corporations	(77,951,000)
Electric Generation	69,533,000
Inheritance and Estate	(45,874,000)
Oil Companies	(23,096,000)
All Others (net)	440,133,000
Refunds of Taxes - Increase	(149,117,000)
Total Increase (Decrease) in Taxes	1,754,903,000
Other Revenues and Sources:	
Licenses, Permits and Fees	32,972,000
Rents, Fines and Escheats	(156,807,000)
Sales of Commodities and Services	87,919,000
Investment Income	34,977,000
Refunds of Payments - Increase	(83,502,000)
Federal Grants	(628,014,000)
Statutory Transfers to/from Other Funds - Net	(207,218,000)
All Others (net)	18,949,000
Total Increase (Decrease) in Other Revenues and Sources	(900,724,000)
Total Increases (Decreases)	**$ 854,179,000**

The increases in income and sales and use taxes were attributed to statutory changes in tax rates that were enacted by Public Act 11-06 of the 2011 General Assembly. The decrease in federal grants was primarily from the decline in federal American Recovery and Reinvestment Act funds. Offsetting the increase of tax revenues was a reduction in monies escheated to the state, and a reduction in the amount of monies transferred from the Budget Reserve Fund to the General Fund.

General Fund Expenditures:

Total budgeted expenditures of the General Fund for the 2011-2012 fiscal year amounted to $18,781,633,905, as shown in Schedule B-1 of the Comptroller's 2012 Annual Report. This latter amount represented an increase of some $936,509,690 or 5.2 percent over the total budgeted expenditures reported by the Comptroller for the preceding 2010-2011 fiscal year. General Fund expenditures classified by current expenses, fixed charges and capital outlay are detailed on Schedule I of the Comptroller's 2012 Annual Report. A summary of the areas of significant changes in expenditures from budgeted accounts of the General Fund follows:

	Nearest Thousand Dollars
Personal Services:	
University of Connecticut	$ 193,690,000
University of Connecticut Health Center	107,953,000
Board of Regents of Higher Education	286,550,000
All Other -	40,140,000
Other Current Expenses:	
University of Connecticut	(219,438,000)
University of Connecticut Health Center	(118,661,000)
Board of Regents of Higher Education	(310,206,000)
State Employees Retirement Contributions	89,310,000
State Employees Health Service Cost	27,719,000
Retired State Employees Health Service Cost	58,164,000
Refunds of Escheated Property	(51,947,000)
All Other - Primarily Contractual Services and Commodities	13,371,000
Fixed Charges:	
Teachers' Retirement Board - Retirement Contributions	175,653,000
Teachers' Retirement Board - Health Service Cost	35,259,000
Debt Service	165,176,000
State Aid Grants:	
Office of Policy and Management - Manufacturing Tax Exemption	(47,896,000)
Social Services - Medicaid	248,422,000
Social Services - Disproportionate Share Hospitals	216,762,000
All Other Fixed Charges	27,497,000
Capital Outlay	(1,004,000)
Total Net Increase	**$ 936,510,000**

There were significant year-to-year changes in higher education expenses due to the reclassification of other current expenses to personal services costs. In addition, there was an increase in personal services costs due to an additional payroll disbursement, which occurs every ten years. Adjusted for these changes, personal services costs declined in comparison to the previous fiscal year. Increased costs for certain state aid grants at the Department of Social Services accounted for a significant part of the increase. This was the result of provider taxes imposed on hospitals and nursing homes that had the effect of increasing federal reimbursements. In addition, there was a significant increase in retirement contributions for state employees and teachers and in payments for debt service.

SPECIAL TRANSPORTATION FUND:

The Special Transportation Fund operates in accordance with the provisions of Title 13b, Chapter 243, Part I, of the General Statutes. The Special Transportation Fund was established in 1984 as part of a continuous program of planning, construction and improvement of the state's transportation infrastructure. Such infrastructure includes the state's highways and bridges, the state's share of the local bridge program, mass transportation and transit facilities, waterway and aeronautic facilities other than Bradley International Airport, and maintenance garages and administrative facilities of the Department of Transportation.

The Special Transportation Fund is used for the purpose of budgeting and accounting for all transportation-related taxes, fees and revenues that are used to secure the payment of debt service on Transportation Infrastructure bonds, which are issued in accordance with the provisions of Chapter 243, Part II, of the General Statutes as special tax obligation bonds. After providing for such debt service, the balance of the resources is available for the payment of debt service on other transportation-related bonds issued by the state, and for the funding of appropriations for the Department of Transportation and the Department of Motor Vehicles.

Revenues credited to the Special Transportation Fund are, among other items, certain motor fuel taxes, portions of the oil companies tax and the sales tax on motor vehicles, motor vehicle receipts for licenses, registrations and titles, fees for safety marker plates, motor vehicle-related fines and penalties, transportation-related federal aid, late fees for the emissions inspection of motor vehicles, and revenues from the sale of information by the Department of Motor Vehicles.

The financial position of the Special Transportation Fund as of June 30, 2012, excluding those resources held by the trustee under the Indenture of Trust for the Transportation Infrastructure special tax obligation bonds, on a budgetary basis, is presented in Schedule C-2 of the Comptroller's 2012 Annual Report. A statement of the changes in unappropriated surplus of the fund for the fiscal year then ended is shown in Schedule C-3. It should be noted that cash and investments totaling $703,288,870, which are being held by the trustee, are reported on Exhibit A of the Comptroller's 2012 Annual Report under Debt Service Funds.

Special Transportation Fund operations, like the General Fund, were conducted under a biennial budget plan, Public Act 11-06, the budget act for the Special Transportation Fund enacted by the 2011 General Assembly, and included revenue estimates and appropriations for the 2011-2012 and 2012-2013 fiscal years.

Under budget procedures customarily in effect, the estimates of revenues and the budgeted appropriations, taken in conjunction with whatever surplus or deficit was carried over from the preceding fiscal period give rise to an anticipated surplus or deficit projected through the end of the fiscal year.

The budget plan for the 2011-2012 fiscal year, as reported by the Comptroller may be expressed as follows:

Estimated Revenues, 2011-2012, as Revised by the Committee on Finance, Revenue and Bonding		$1,262,500,000
Budgeted Appropriations, 2011-2012	$1,356,022,262	
Estimated Lapsing Appropriations	(53,536,000)	
Net Appropriations		1,302,486,262
Anticipated Surplus, June 30, 2012		**$ (39,986,262)**

The actual results of the operations of the 2011-2012 fiscal year are presented in Schedule C-3 of the Comptroller's 2012 Annual Report. An analysis of the Special Transportation Fund surplus follows:

Actual Budgeted Revenues, 2011-2012		$1,232,920,590
Appropriations, 2011-2012	$1,356,022,262	
Add/(Deduct)		
Appropriations Lapsed	(120,999,125)	
Net Appropriations		1,235,023,137
Balance		(2,102,547)
Unappropriated Surplus, July 1, 2011		107,365,132
Prior Year Budgeted Appropriations Continued to 2011-2012 Fiscal Year		40,553,674
Miscellaneous Adjustments		199
Unappropriated Surplus, June 30, 2012, per Schedule C-3		**$ 145,816,458**

The variances between the actual results of operations and the original budget plan may be explained as follows:

1. Actual revenues were some $29,579,000 less than anticipated. This was primarily the result of decreases of $14,506,000 in motor fuels taxes, $10,292,000 in interest income, and $7,826,000 in licenses, permits and fees. The decreases were partly offset by an increase of $5,018,000 in sales tax collections.
2. Lapsed appropriations were some $67,463,000 greater than estimated, primarily from reduced debt service costs.

Special Transportation Fund Revenues:

Realized budgeted revenues in the 2011-2012 fiscal year for the Special Transportation Fund totaled $1,232,920,590, as shown in Schedule C-3 of the Comptroller's 2012 Annual Report. This represented an increase of some $65,712,947 over the budgeted revenue total reported by the Comptroller for the preceding 2010-2011 fiscal year. Budgeted revenue categories that showed the greatest change during the fiscal year under audit were as follows:

	Nearest Thousand Dollars
Taxes:	
Motor Fuels Tax	$ 9,269,000
Oil Companies Tax	61,600,000
Other Revenues:	
Motor Vehicle Receipts	13,302,000
Transfers from Other Funds	(26,000,000)
All Other Taxes and Other Revenue	5,542,000
Total Net Increase (Decrease)	**$ 63,713,000**

The above increase was primarily attributable to an increase in the collection of oil company taxes and transfers from other funds. It was offset by decreases in collections for motor fuels tax.

Special Transportation Fund Expenditures:

Total budgeted expenditures of the Special Transportation Fund for the 2011-2012 fiscal year amounted to $1,193,408,074, as shown in Schedule C-5 of the Comptroller's 2012 Annual Report. This represented an increase of some $26,778,341 from the total budgeted expenditures reported by the Comptroller for the preceding 2010-2011 fiscal year. A summary of the areas of significant changes in expenditures from budgeted accounts of the Special Transportation Fund follows:

	Nearest Thousand Dollars
Department of Transportation:	
Personal Services	(21,280,000)
Other Expenses	(8,209,000)
Rail Operations	10,604,000
Highway and Bridge Renewal	(14,307,000)
Pay as You Go Transportation Projects	20,413,000
Town Aid Road Grants	30,000,000
Office of the State Comptroller:	
State Employees Retirement Contributions	7,610,000
All Other (net)	1,947,000
Total Net Increase (Decrease)	**$26,778,000**

The above increase in expenditures was primarily attributable to increases in rail operations, and road projects at the Department of Transportation as well as state employees' retirement contributions.

SPECIAL REVENUE FUNDS:

This category of funds was established to group those funds accounting for the expenditure of revenues that have been restricted to specific programs. Included in this category is the Special Transportation Fund. However, because of the size and importance of this fund, it has been incorporated into this report under a separate heading preceding this section.

The financial position of the combined Special Revenue Funds at June 30, 2012, on a budgetary basis, together with the cash transactions for the fiscal year ended on that date, are shown in Exhibit C and Schedule C-1, respectively, of the Comptroller's 2012 Annual Report. As of June 30, 2012, there were 47 active funds within this category, with the Special Transportation Fund by far being the largest. Of these 47 funds, the following nine funds operate under legislatively enacted budget plans:

- Special Transportation Fund
- Banking Fund
- Insurance Fund
- Consumer Counsel and Public Utility Control Fund
- Workers' Compensation Administration Fund
- Mashantucket Pequot and Mohegan Fund
- Soldiers', Sailors' and Marines' Fund
- Regional Market Operation Fund
- Criminal Injuries Compensation Fund

Grants and Restricted Accounts Fund:

The Grants and Restricted Accounts Fund was established to account for certain federal and other revenues associated with activities of the General Fund, primarily federal grant assistance.

Receipts and transfers amounting to $2,077,308,745 for the 2011-2012 fiscal year were credited to the fund, as shown on Schedule C-1 of the Comptroller's 2012 Annual Report. These represented federal and other grant receipts, restricted and not available for general use. As mentioned previously in this report, such restricted revenue is recognized by the Comptroller when earned through the expenditure of grant funds, rather than when received or awarded. Receipts and transfers increased by some $107,081,849, as compared to the total reported by the Comptroller in the preceding 2010-2011 fiscal year.

Disbursements of federal and other grants from the Grants and Restricted Accounts Fund for the 2011-2012 fiscal year amounted to $2,096,456,294, as shown in Schedule C-1 of the Comptroller's 2012 Annual Report. This represented a decrease of some $14,750,291 over the total reported by the Comptroller for the preceding 2010-2011 fiscal year.

Transportation Grants and Restricted Accounts Fund:

The Transportation Grants and Restricted Accounts Fund was established to account for certain restricted federal and other revenues associated with activities of the Special Transportation Fund, primarily federal grant assistance related to highway and transit projects.

Receipts and transfers amounting to $751,541,329 for the 2011-2012 fiscal year were credited to the Transportation Grants and Restricted Accounts Fund, as shown on Schedule C-1 of the Comptroller's 2012 Annual Report. This represented a decrease of some $53,352,443 over the total reported by the Comptroller for the preceding 2010-2011 fiscal year. For the purpose of construction of any highway or bridge, the Office of the State Comptroller is authorized under the provisions of Section 13a-166 of the General Statutes to record as a receivable that portion of a federal grant apportionment for the financing of the federal share of highway projects approved by the Federal Highway Administration, and such amounts are deemed to be appropriated for said purposes.

Disbursements of federal and other grants from the Transportation Grants and Restricted Accounts Fund for the 2011-2012 fiscal year amounted to $821,780,873, as shown in Schedule C-1 of the Comptroller's 2012 Annual Report. This represented an increase of some $46,035,444 over the total reported by the Comptroller for the preceding 2010-2011 fiscal year.

Additional comments concerning the operations of individual special revenue funds will be found in audit reports covering the various state agencies administering or using such funds.

DEBT SERVICE FUNDS:

This category of funds was established to account for the accumulation of resources for, and payment of, principal and interest on certain state issued bonds and notes. While, as a rule, the bulk of general obligation bonds of the state are liquidated from General Fund and Special Transportation Fund appropriations, most so-called self-liquidating general obligation bond issues are retired by payment from these funds.

The financial position of the combined Debt Service Funds at June 30, 2012, together with the cash transactions for the fiscal year ended on that date, on a budgetary basis, are shown in Exhibit D and Schedule D-1, respectively, of the Comptroller's 2012 Annual Report. As of June 30, 2012, there were six authorized funds within the Debt Service Funds category. The largest debt service fund, entitled Transportation Special Tax Obligations is used to account for cash and investments held by a trustee for debt service payments on bonds issued to finance the state's infrastructure program.

CAPITAL PROJECTS FUNDS:

This category of funds was established to group those funds that account for financial resources used to acquire or construct major capital facilities, including highways and bridges. Included in this category are additional funds authorized for capital improvements and non-capital improvements or other purposes by specific fiscal year. The most significant of these funds is the Infrastructure Improvement Fund, which is used to account for highway and transit construction project expenditures at the Department of Transportation. The major source of financing for Capital Projects Funds is the proceeds of various state bond issues. Other sources include federal aid and other restricted contributions receivable to meet a portion of the capital outlay costs.

The financial positions of the combined Capital Projects Funds at June 30, 2012, and the cash transactions of the 2011-2012 fiscal year, on a budgetary basis, are set forth in Exhibit E and Schedule E-1, respectively, of the Comptroller's 2012 Annual Report. As of June 30, 2012, there were 39 active funds within the Capital Projects Funds category.

The total unreserved fund balances of the Capital Projects Funds decreased by $628,190,188 during the 2011-2012 fiscal year to a deficit balance of $4,997,224,205, as of June 30, 2012. It should be noted that the issuance of bonds already authorized, as shown in Schedule E-5, as well as the collection of those receivables fully reserved in Exhibit A and Exhibit E, will eliminate this deficit balance.

INTERNAL SERVICE FUNDS:

This category of funds was established to group those funds accounting for the costs and billings for goods and services provided by state agencies to other agencies or governmental units. These costs are recovered by transfer charges to user agencies so that authorized working capital of the funds is kept intact.

The financial position of the combined Internal Service Funds at June 30, 2012, together with the cash transactions for the fiscal year then ended, on a budgetary basis, are shown in Exhibit F and Schedule F-1, respectively, of the Comptroller's 2012 Annual Report. As of June 30, 2012, there were three active funds within the Internal Service Funds category.

Exhibit A of the Comptroller's 2012 Annual Report recognizes, as reserved within fund balances and related reserves, $10,058,405 in allotment and appropriation balances in force as of June 30, 2012, and which have been carried forward to the 2012-2013 fiscal year on the records of the Office of the State Comptroller. This has resulted in additional deficit unreserved fund balances being reported in Exhibit A and Exhibit F of the Comptroller's 2012 Annual Report because the assets and resources to meet these allotment balances are already reserved or, more likely, are not recorded by the Comptroller. Those assets and resources not recorded include inventories and receivables reported only by the agencies administering the funds involved.

Additional comments concerning the operations of each individual internal service fund will be contained in audit reports covering the various state agencies administering such funds.

ENTERPRISE FUNDS:

This category of funds was established to group those proprietary funds that provide for the financing of goods and services to the public and recover costs by user charges.

The financial position and fiscal year cash transactions of the combined Enterprise Funds, as accounted for in the records of the Office of the State Comptroller, on a budgetary basis, are shown in Exhibit G and Schedule G-1, respectively, of the Comptroller's 2012 Annual Report. As of June 30, 2012, there were 18 active funds within the Enterprise Funds category.

Additional comments concerning the operations of each individual enterprise fund will be contained in audit reports covering the various state agencies administering such funds.

FIDUCIARY FUNDS:

The financial position of the combined Fiduciary Funds at June 30, 2012, and the cash transactions for the year then ended, on a budgetary basis, is shown in Exhibit H and Schedule H-1, respectively of the Comptroller's 2012 Annual Report. The funds included under this caption may be classified into three types:

- Receipts held pending distribution to state funds, municipalities, private companies or individuals.
- Deposits held by the state for security, guarantees, awards, endowments or distributions.
- Retirement and post employment benefit funds for state and municipal employees held in trust by the State Treasurer.

As of June 30, 2012, there were 26 active funds within the Fiduciary Funds category. The total liabilities, reserves and fund balances of the fiduciary funds increased by $3,717,752,422 during the 2011-2012 fiscal year to a balance of $42,217,345,110, as of June 30, 2012. The increase was the result of a $3,678,582,000 increase in the amount of resources to be provided in future years for state employee's and teacher's retirements. The amounts reported as resources to be provided in future years for retirement funds were as of June 30, 2012, and were based on the currently available actuary reports. The fiduciary funds financial statements did not report actuarially determined resources to be provided in future years for other post employment benefits.

Additional comments concerning the operations of each individual fiduciary fund will be contained in audit reports covering the various state agencies administering or using such funds.

STATE BOND AND NOTE INDEBTEDNESS:

The state's bond and note indebtedness at June 30, 2012, payable from future revenue of state funds is shown in Exhibit A of the Comptroller's 2012 Annual Report. A summary of bonds and notes outstanding and maturity schedules, detailing the funding requirements of specific bond and note issues, are presented in Schedule E-3 and Schedule E-4, respectively, of the Comptroller's 2012 Annual Report.

The state's bond and note indebtedness, redeemable from General and Transportation Fund revenues, aggregated $19,043,148,000 as of June 30, 2012, a decrease of $199,492,000 over the total of $19,242,640,000 at June 30, 2011. This was the net result of the issuance during the 2011-2012 fiscal year of new bonds in the amount of $2,774,615,000, while scheduled principal payments and refunded and defeased bonds and notes during the period amounted to $2,974,107,000. Scheduled interest costs through maturity on the aforementioned bond and note indebtedness, as shown in Schedule E-4 of the Comptroller's 2012 Annual Report, totaled $8,266,781,000. Accordingly, as of June 30, 2012, the state was committed to future debt service on bonds and notes outstanding in the aggregate of $27,309,929,000. This total represented a decrease of $472,338,000 over the corresponding amount as of June 30, 2011.

Included in the totals of bond and note indebtedness are revenue and refunding bonds outstanding in the amount of $195,185,000 for improvements to Bradley International Airport. The proceeds of such bonds are being held and disbursed by a trustee and all revenue of the airport's operations is being deposited with the trustee. Principal and interest payments on such bonds are being met from funds held by the trustee. Similarly, included in the totals of bond and note indebtedness are the revenue bonds outstanding of $3,287,340,000 for the state's Transportation Infrastructure Program. While the proceeds of such bonds are held and accounted for in the usual manner, debt service reserve amounts and principal and interest payments on such bonds are being handled by a trustee.

Partially offsetting the aforementioned indebtedness were unreserved fund balances of $766,982,762 within the debt service fund group, which were available for debt service at June 30, 2012, and which are detailed in Exhibit D of the Comptroller's 2012 Annual Report.

In addition to the foregoing bond indebtedness at June 30, 2012, there was in force as of that date unused borrowing authorizations totaling $5,137,927,000 and prospective authorizations, subject to Bond Commission approval, totaling $2,148,716,000. These authorization balances, which are detailed in Schedule E-5 of the Comptroller's 2012 Annual Report, may be summarized as follows:

Purpose or Agency	**In Force**	**Prospective Authorizations**
Municipal and Economic Development	$ 216,105,000	$ 127,364,000
Capital Improvements and Other Purposes	317,088,000	527,437,000
Transportation Infrastructure Improvement	2,557,769,000	444,576,000
Elimination of Water Pollution	816,953,000	18,420,000
Housing Programs	103,648,000	44,645,000
University and State University Facilities	192,891,000	191,000,000
Student Loan Foundation	5,000,000	0
Local Capital Improvements	0	20,000,000
State Equipment Purchases	35,195,000	8,732,000
Grants to Local Governments and Others	300,003,000	440,342,000
Contaminated Property Remediation	1,000,000	1,000,000
Connecticut Bioscience Collaboration	14,162,000	0
Magnet Schools	5,000	323,000,000
Highway and Bridge Construction	1,452,000	0
Preservation of Agricultural Lands	25,751,000	0
Connecticut Innovations Incorporated	500,000	0
Bradley Parking Garage	0	1,200,000

Industrial Building Mortgage Insurance	19,450,000	1,000,000
Connecticut Housing Finance Authority	1,460,000	0
Connecticut Development Authority	3,595,000	0
Second Injury Fund	525,900,000	0
Total Authorizations	**$5,137,927,000**	**$2,148,716,000**

It should be noted that, in accordance with the debt limitation provisions contained in Section 3-21 of the General Statutes, no bonds, notes, or other evidences of indebtedness for borrowed money payable from General Fund tax receipts of the state shall be authorized by the General Assembly except as shall not cause the aggregate amount of (1) the total amount of such indebtedness authorized by the General Assembly but not yet issued and (2) the total amount of such indebtedness which has been issued but remains outstanding, to exceed 1.6 times the total estimated General Fund tax receipts of the state for the fiscal year in which any such authorization will become effective, as estimated by the joint standing committee of the General Assembly having cognizance of finance, revenue and bonding. Such tax receipts for the fiscal year ended June 30, 2013 were estimated, as of February 1, 2013, to total $14,408,165,000. As of February 1, 2013, the State Treasurer determined that authorizations for bonds, notes, and other obligations subject to such limit, net of debt retirement fund resources related to certain self-liquidating bond issues, totaled $16,685,270,202. Accordingly, as of this date, the state's debt-incurring margin totaled $6,367,793,798.

In addition to the indebtedness previously mentioned, there were other obligations that, although not in the form of state bonds or notes, constituted long-term indebtedness or the guarantee of existing indebtedness. Such obligations included:

1. Obligations of the state to towns for participation in the construction and alteration of school buildings, under Section 10-287 of the General Statutes (installment payments) in the amount of some $174,000,000, and Sections 10-287g and 10-287h (interest subsidy) in the amount of some $23,000,000, as of June 30, 2012. It should be noted that Sections 10-287g and 10-287h were repealed by Public Act 97-11 (June Special Session) for construction projects approved subsequent to July 1, 1997. With regard to projects approved after July 1, 1997, this same public act established a new financing method, which provides for the state to pay for its share of school construction costs on a "progress payment" basis (Section 10-287i of the General Statutes). As of June 30, 2012, the State Board of Education estimates that current grant obligations under this latter program will total some $2,508,000,000.

2. The obligation of Section 5-156a of the General Statutes to fund the State Employees Retirement System on an actuarial reserve basis. The unfunded actuarial liability is amortized as a level percent of payroll over a declining period of years, starting with 40 years as of July 1, 1991. A full actuarial survey of the system was performed as of June 30, 2012, and showed an unfunded accrued liability of $13,273,766,185.

3. The obligation of Section 51-49d of the General Statutes to fund the Judges, Family Support Magistrates and Compensation Commissioners Retirement System on an actuarial reserve basis over a 40-year period commencing July 1, 1991. The last

actuarial survey of the system was performed as of June 30, 2012, and showed an unfunded accrued liability of $144,847,720.

4. The obligation of Section 10-183z of the General Statutes to fund the Teachers' Retirement System on an actuarial reserve basis over a 40-year period commencing July 1, 1992. The last actuarial survey of the system was performed as of June 30, 2012, and showed an unfunded accrued liability of $11,127,400,000.

5. Loans under the Insurance program, insured by the state ($25,000,000 maximum limit) through the Connecticut Development Authority, which totaled $3,803,749 as of June 30, 2012. In accordance with Section 32-17a of the General Statutes, these are contingent indebtedness of the state; however, actual indebtedness would result only in the event of a loan default or the inability of the authority to make the payment of bonds and notes. Effective July 1, 2012 the Connecticut Development Authority was merged into Connecticut Innovations Incorporated.

6. Loan guarantees under the Connecticut Works Fund, insured by the state through the Connecticut Development Authority, as provided for in Section 32-23ii of the General Statutes. The state has authorized the issuance of up to $95,000,000 in bonds allocated to the fund, of which $82,485,000 has been distributed as of June 30, 2012. Loan guarantees were also extended under the Connecticut Works Guarantee Fund, as provided for in Section 32-261 of the General Statutes. The state has authorized the issuance of up to $30,000,000 in bonds allocated to the funds, of which $18,900,000 has been distributed as of June 30, 2012. The Connecticut Development Authority also provided portfolio insurance to participating financial institutions under the Connecticut Capital Access Fund, as provided for in Section 32-265 of the General Statutes. The state has authorized the issuance of $5,000,000 in bonds allocated for the purpose, of which $2,000,000 has been distributed as of June 30, 2012. Any losses on guarantees made by the authority under any of these funds are reimbursable by the state until the remaining bond allocation has been utilized.

7. Under the General Obligation Bond program, bonds secured by a special capital reserve fund were issued by the Connecticut Development Authority to finance economic development projects. As of February 1, 2013, $1,500,000 of such bonds remained outstanding.

8. The State of Connecticut is contingently liable to the Connecticut Housing Finance Authority, the Connecticut Resources Recovery Authority and the Connecticut Higher Education Supplemental Loan Authority for amounts needed annually to maintain debt service reserves for one year's principal and interest on certain authority bonds in the event authority funds are insufficient to do so, as provided for in Sections 8-252a(b), 22a-272(b) and 10a-232(b), respectively, of the General Statutes. As of February 1, 2013, the principal amount of outstanding bonds, secured by special capital reserve funds, for the Connecticut Housing Finance Authority, the Connecticut Resources Recovery Authority, and the Connecticut Higher Education Supplemental Loan Authority totaled $3,547,900,000, $17,100,000, and

$150,900,000, respectively.

9. The State of Connecticut is contingently liable to the Connecticut Health and Educational Facilities Authority for amounts needed annually to maintain debt service reserves for one year's principal and interest on those authority bonds used to finance projects at participating nursing homes or to finance dormitories or facilities for the provision of student housing at public and private institutions of higher education, in the event authority funds are insufficient to do so, as provided for in Section 10a-186a of the General Statutes. As of February 1, 2013, the principal amount of outstanding bonds secured by special capital reserve funds totaled some $292,000,000.

10. The Connecticut Health and Educational Facilities Authority has issued child care facilities bonds and has loaned the proceeds to various entities for child care facilities. The State Department of Education has entered into commitments to pay the debt service on the loans by annual appropriations, with the remainder paid from the intercept of revenues from providers. As of February 1, 2013 there was $61,200,000 in child care facilities bonds outstanding with annual debt service of $4,600,000, of which $4,200,000 is a commitment paid by annual appropriations.

11. The Capital City Economic Development Authority, predecessor to the Capital Region Development Authority, has issued revenue bonds backed by the state's contract assistance agreement for the Hartford convention center project. As of February 1, 2013 there was $97,540,000 in bonds outstanding. The state's obligation under this agreement is limited to $9,000,000 per year.

12. Public Act 11-84, effective July 1, 2011, established the Connecticut Airport Authority as a quasi-public agency to manage the operation of Bradley International Airport and the state's general aviation airports. The Connecticut Airport Authority is authorized to issue revenue bonds which may be backed by a special capital reserve fund. Funds shall be appropriated from the General Fund to pay any amount needed to maintain the special capital reserve at the required minimum level.

13. Public Act 12-84, June Special Session established the Clean Energy Finance and Investment Authority, effective October 1, 2012, as a successor agency to Connecticut Innovations Incorporated for administering the Clean Energy Fund. The Clean Energy Finance and Investment Authority is authorized to issue bonds which may be backed by a special capital reserve fund contributed to by the state.

14. In accordance with the provisions of Special Act 67-381, as subsequently amended by Special Acts 73-95 and 90-28, $1,300,000 in bonds of the Southeastern Connecticut Water Authority are guaranteed by the state, as of February 1, 2013.

CONDITION OF RECORDS

Our review of statewide financial reporting identified internal control weaknesses as defined by the standards of the American Institute of Certified Public Accountants (AICPA). Although they are not deemed significant deficiencies or material weaknesses per the AICPA standard, they are areas that require corrective action. These areas are detailed in the following pages:

State Accounting Manual Update to Reflect the Core-CT Environment:

Criteria: Section 3-112 of the General Statutes provides that the Comptroller shall "establish and maintain the accounts of the state government…prescribe the mode of keeping and rendering all public accounts of departments or agencies of the state and of institutions supported by the state or receiving state aid by appropriation from the General Assembly… prepare and issue effective accounting and payroll manuals for use by the various agencies of the state."

The State Accounting Manual, issued by the Office of the State Comptroller, originally provided a formal set of accounting policies and procedures, and established the definitions of authority and responsibility between state departments and agencies, and the Office of the State Comptroller.

Condition: Our audits of state financial operations for the fiscal years ended June 30, 2004, 2005, 2006, 2007, 2009, 2010, 2011 and 2012 have noted that the Office of the State Comptroller has not provided user agencies with an updated version of its State Accounting Manual. At the time of our review (May 2013), we noted that the following sections of the State Accounting Manual were not available to users and were listed as currently under review:

1. General State Accounting Policies and Procedures
2. Funds
3. GAAP Acceptance in Connecticut
4. Inter & Intra State Transfers and Adjustments
5. Management of Receivables
6. Year End

Effect: Financial guidance is communicated to agencies in the form of online job aids within each Core-CT accounting application, Comptroller's numbered memoranda, various Core-CT communications and access to a help desk. The lack of a systematized accounting manual requires users to sort through numerous resources to obtain desired information.

Cause: The Budget and Financial Analysis Division of the State Comptroller has indicated that time and resources were still a consideration.

Recommendation: The Office of the State Comptroller should promptly complete the remaining portions of its revision to the State Accounting Manual (See Recommendation 1.)

Agency Response: "I am pleased to report that as of May 2013, the State Accounting Manual (SAM) has been fully updated to integrate Core-CT applications. The manual is on-line and has links to Core-CT and other source documentation to assist users. The SAM will be updated to reflect any changes as required."

Revolving Fund Accounting - Department of Administrative Services:

Background: The Department of Administrative Services (DAS) submits financial statements for the General Services Revolving Fund to the Office of the State Comptroller to be included in the CAFR, and to document indirect costs for the Statewide Cost Allocation Plan.

Criteria: OMB Circular A-87, Appendix C, Section E(3)(b)(1) requires the inclusion of financial statements for proprietary funds within the Statewide Cost Allocation Plan.

Governmental Accounting Standards Board Statement No. 34 (GASB 34) specifies that financial statements compiled for governmental proprietary funds include a statement of cash flows. GASB 34 further requires that internal service funds, such as the General Services Revolving Fund, use the current economic resources measurement focus and the full accrual basis of accounting. In a memorandum dated August 2007, the Office of the State Comptroller mandated that the Department of Administrative Services comply with GASB 34.

Condition: An audit of the records maintained by the Department of Administrative Services found that the department reported significant additions in land and buildings. Upon our inquiry regarding such additions, we found the amounts provided by DAS for fixed assets on its balance sheet were not accurate. DAS is currently in communication with other agencies to determine what the proper inventory amounts should be. It was indicated that the property inventory record had not been reconciled in over two years. For certain properties, DAS were unsure whether they should be accounted for in the Revolving Fund or the General Fund.

We also found that DAS reported an opening balance equity amount of $33,632,889 on its balance sheet in its QuickBooks records. This amount dates from 2008 and, upon our inquiry, DAS indicated that it has not communicated to the Office of the State Comptroller regarding the nature of this amount. We note that DAS obtains financial data from Core-CT, the state's main financial system, loads it into its QuickBooks accounting records, then uses QuickBooks to prepare its financial statements. These statements are manually forwarded to the State Comptroller to enable statewide financial reporting on the Core-CT system. While the use of the QuickBooks system is not prohibited by state statute or regulation, it is noted that the use of such a system could introduce the opportunity for additional error through incomplete or inaccurate data transfer to or from the Core-CT system.

Effect: The errors in presentation indicate that the information presented in the financial statements, which are used to compile billing rates for services, is unreliable.

Cause: The Department of Administrative Services did not appear to complete its implementation of controls over the preparation of the financial statements for the fund. It did not allocate sufficient resources to the tasks associated with the preparation of the financial statements for the fund. DAS should consider using the Core-CT financial system as its sole financial system to increase efficiency in the reporting process and to eliminate the likelihood of errors in the data transmission process.

Recommendation: The Office of the State Comptroller and the Department of Administrative Services should continue to work together to ensure that the General Services Revolving Fund financial statements are accurately presented. (See Recommendation 2.)

Agency Response: "We are in agreement with this finding. As you state, this office mandated compliance with GASB Statement 34 by revolving fund agencies. For the reasons you outline, the Department of Administrative Services (DAS) was not compliant with these requirements.

As recommended, this office assisted DAS in the proper preparation of GASB compliant statements and made the necessary fund balance adjustments to the State's fiscal year 2012 financial statements. The validation of balances to Core-CT will continue in future fiscal years. In addition, we have encouraged DAS to transition from QuickBooks to Core-CT as it will provide greater transparency and consistency in transaction processing. But as you note, the revolving fund is not statutorily compelled to use Core-CT."

Cross Check and Validation of Central Accounting Journal Entries:

Criteria: Proper internal controls require all journal entries, including those considered nonstandard or nonroutine, have adequate supporting documentation and are reviewed and approved independently prior to posting. There should be appropriate segregation of duties among those who initiate journal entries, approve journal entries and post journal entries to the Core-CT general ledger.

Condition: The central accounting function within the Budget and Financial Analysis Division of the State Comptroller prepares and posts journal entries to the Core-CT general ledger for statewide budgetary and GAAP accounting, fiscal year-end close and financial statement preparation. A single individual is frequently preparing and posting journal entries of significant amounts without a second person to review and approve the journal prior to posting it to the general ledger.

In our examination of 147 journal lines from the General Fund budgetary basis general ledger, we found 107, or 73 percent, that were prepared and reviewed by the same individual. We noted a similar condition with other fund groups.

In our examination of the GAAP basis general ledger, we found that journal entries were not always or consistently reviewed by a second individual for certain special revenue, debt service, enterprise and fiduciary funds.

There were no compensating controls to ensure that errors and omissions in the journal entries would be detected and corrected.

Effect: Our annual audits of the financial statements have identified errors in journal entries posted to the Core-CT system. Errors not identified and corrected by the audit process can result in a material misstatement in the financial statements.

Cause: Statewide central accounting is performed by a small staff that does not readily lend itself to the establishment of segregated duties and the cross checking of work. In response to our previous audit, the Budget and Financial Analysis Division stated that it had implemented corrective action to require the validation of GAAP journal entries by the division director prior to posting. Our current audit found complete corrective action had not been implemented. As described above, we found numerous GAAP journal entries entered from November 2012 through the completion of the CAFR in February 2013 that were not reviewed by a second individual.

Recommendation: The Budget and Financial Analysis Division of the Office of the State Comptroller should ensure that all centrally posted journal entries have adequate supporting documentation and are reviewed and approved independently prior to posting. (See Recommendation 3.)

Agency Response: "We are in full agreement with this finding, and as you have noted in May 2012 corrective action was implemented. In fiscal year 2013 all journal entries will be cross checked."

RECOMMENDATIONS

Status of Prior Audit Recommendations:

Office of the State Comptroller - State Financial Operations Audit Report -

Two recommendations were presented in our prior report. Both of these recommendations are being restated in our current report. A list of the previous recommendations and their resolution are as follows:

1. The Office of the State Comptroller should promptly complete the remaining portions of its revision to the State Accounting Manual. Our previous examination found partial corrective action made with the revision of major portions of the manual effective October 17, 2011. However, we again note that significant portions are still not completed. We again recommend that the Office of the State Comptroller promptly update and complete the remaining portions of the State Accounting Manual. (See Recommendation 1.)

2. The Office of the State Comptroller and the Department of Administrative Services, working together, should ensure that the General Services Revolving Fund financial statements are prepared in a manner compliant with state and federal regulations, and accounting standards and pronouncements and resolve the disparities in reported financial position of the fund. Our current audit found corrective action had not been implemented. (See Recommendation 2.)

Current Audit Recommendations:

1. **The Office of the State Comptroller should promptly complete the remaining portions of its revision to the State Accounting Manual.**

   Comment:

   We found that the task of revising the documentation of state accounting policies and procedures was still incomplete.

2. **The Office of the State Comptroller and the Department of Administrative Services should continue to work together to ensure that the General Services Revolving Fund financial statements are accurately presented.**

   Comment:

   As a result of the failure to establish proper accounting policies and procedures, the financial statements of the General Services Revolving Fund required significant reworking to make them acceptable for the state's CAFR.

3. **The Budget and Financial Analysis Division of the Office of the State Comptroller should ensure that all centrally posted journal entries are reviewed and approved independently prior to posting.**

   Comment:

   Our examination found journal entries posted to the budgetary and GAAP basis general ledgers that were not reviewed and approved by a second individual.

CONCLUSION

In conclusion, we wish to express our appreciation of the courtesies shown to our representatives during the course of our audit. The assistance and cooperation extended to them by the personnel of the Office of the State Comptroller in making records readily available and in explaining transactions as required greatly facilitated the conduct of this examination.

Matthew Rugens
Administrative Auditor

Approved:

John C. Geragosian
Auditor of Public Accounts

Robert M. Ward
Auditor of Public Accounts