STATE OF CONNECTICUT

AUDITORS' REPORT
CONNECTICUT HEALTH AND EDUCATIONAL FACILIIITIES AUTHORITY
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

AUDITORS OF PUBLIC ACCOUNTS
KEVIN P. JOHNSTON ❖ ROBERT G. JAEKLE

Table of Contents

INTRODUCTION..1
SCOPE OF AUDIT..1

COMMENTS..2
FOREWORD 2
Board of Directors and Administrative Officials..3
Significant State Legislation..3
Accounting Policies 3
RÉSUMÉ OF OPERATIONS 5

CONDITION OF RECORDS..8
Written Policies..8
Contracted Professional Services...9
Penalty of False Statement..10
Grants 11
Annual Report..12
Segregation of Duties..13

RECOMMENDATIONS..15

CERTIFICATION 17

CONCLUSION 20

August 26, 2009

AUDITORS' REPORT
CONNECTICUT HEALTH AND EDUCATIONAL FACILIITIES AUTHORITY
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

We have examined the books, records and accounts of the Connecticut Health and Educational Facilities Authority (the Authority), as provided in Section 2-90 and Section 1-122 of the General Statutes, for the fiscal year ended June 30, 2007.

SCOPE OF AUDIT:

This audit was primarily limited to performing tests of the Authority's compliance with certain provisions of laws, regulations, contracts and grants, including but not limited to, a determination of whether the Authority has complied with its written operating procedures, that are required per Section 10a-179(h) of the General Statutes, concerning the following areas:

- Affirmative action
- Personnel practices
- Purchase of goods and services
- Use of surplus funds
- Distribution of loans, grants and other financial resources.

We also considered the Authority's internal control over its financial operations and its compliance with requirements that could have a material or significant effect on the Authority's financial operations in order to determine our auditing procedures for the purpose of evaluating the Authority's financial operations and compliance with certain provisions of laws, regulations, contracts and grants, and not to provide assurance on the internal control over those control objectives. Our consideration of internal control included the five areas identified above.

Our audit included a review of a representative sample of the Authority's activities during the fiscal year in the five areas identified above and a review of such other areas as we considered necessary. The financial statement audit of the Authority, for the fiscal year indicated above, was conducted by the Authority's independent public accountants.

This report on our examination consists of the Comments, Condition of Records, Recommendations, and Certification that follow.

COMMENTS

FOREWORD:

The State of Connecticut Health and Educational Facilities Authority (hereafter CHEFA or the Authority) operates under the provisions of Title 10a, Chapter 187, of the General Statutes. The Authority is a public instrumentality and political subdivision of the State whose Board of Directors is appointed by the Governor. Pursuant to Chapter 12 of the General Statutes, CHEFA is classified as a quasi-public agency. As a quasi-public agency, the Authority's financial information is included as a component unit in the State of Connecticut's Comprehensive Annual Financial Report (CAFR).

The purpose of the Authority is to assist certain health care institutions, institutions of higher education, and qualified not-for-profit institutions in the financing and refinancing of projects to be undertaken in relation to programs for these institutions. The Authority is empowered to issue its own bonds, bond anticipation notes and any other obligations for any of its corporate purposes and to fund and refund the same. As of June 30, 2007, CHEFA has issued $9,872,785,000 in bonds, of which $5,610,859,000 are outstanding. The Authority issued general obligation bonds through June 1979, for which the Authority is ultimately responsible for the payment of principle and interest when due. Subsequent to July 1, 1979, the Authority has issued only special obligation bonds for which principle and interest is solely payable from the revenues of the institutions and is not a debt of the Authority or the State of Connecticut. As of June 30, 2007, there were no general obligation bonds outstanding. The State is not obligated for the debt, except for debt that is issued under the Child Care Facilities Loan Program and the Special Capital Reserve Program.

Under the Child Care Facilities Loan Program, the State of Connecticut is responsible for paying a portion of the debt service on bonds issued under the program as specified in Section 17b-749i of the General Statutes. Under the Special Capital Reserve Program, debt is guaranteed by the State under Section 10a-186a of the General Statutes. Section 10a-186a of the General Statutes provides for the maintenance of a Special Capital Reserve Fund to be used for the payment of principal and interest on Authority bonds to finance projects at participating nursing homes and public institutions of higher education. The State is contingently liable to provide annual debt service requirements for such bonds if the Authority's funds are not sufficient to meet minimum reserve requirements for the Special Capital Reserve Fund.

The Authority's operations do not rely upon any State appropriation either from the General Fund or from bond funds. CHEFA generates revenue from fees on its portfolio of bonds and investment income.

The Authority provides grants to non-profit organizations that provide essential health, educational, culture, and childcare services to Connecticut residents in targeted geographic areas of Connecticut. During the fiscal year ended June 30, 2007, CHEFA administered four grant programs, the Client Grant Program, the Open Grant Program, the Focused Investment Grant Program, and the Medical Malpractice Grant Program.

Board of Directors and Administrative Officials:

Pursuant to Section 10a-179(a) of the General Statutes, the Authority operates under a ten person Board of Directors. The Board of Directors includes the State Treasurer and the Secretary of the Office of Policy and Management as ex-officio members and eight residents of the State who are appointed by the Governor. Not more than four of the eight members appointed by the Governor can be of the same political party. In addition, three appointed members shall be trustees, directors, officers or employees of institutions for higher education, two appointed members shall be trustees, directors, officers or employees of health care institutions and one shall be a person having a favorable reputation for skill, knowledge, and experience in State and municipal finance. Members of the Board of Directors as of June 30, 2007, were as follows:

Ex-Officio:
Denise L. Nappier, State Treasurer
Robert L. Genuario, Office of Policy and Management

Appointed by the Governor:
Barbara Rubin, Chairperson
Patrick A. Colangelo, Vice Chairperson
John M. Biancamano
Steven P. Blackburn, Ph.D.
William J. Cibes, Jr., Ph.D.
Benson R. Cohn
Bryan K. Pollard, Esq.
Dori T. Sullivan, Ph.D.

The Executive Director of the Authority is appointed by the Board of Directors. Richard D. Gray served in that capacity throughout the audited period.

Significant State Legislation:

There was no legislation enacted during the audited period that significantly impacted the Authority.

Accounting Policies:

The Authority maintains books of accounts for its own operations and for each of the issues of debt outstanding. In accordance with the requirements of bond issue documents, separate funds are maintained for each issue. A brief description of the various types of funds maintained by the Authority and their purpose follows.

***General Fund* –** This fund accounts for the revenues and expenses applicable to the operations of the Authority.

***Construction and Project Funds* –** These funds reflect the receipt of bond proceeds, costs of issuance and disbursement of moneys for the payment of construction or renovation projects and equipment for the institutions.

***Debt Service and Bond Funds* –** These funds account for the receipt of payments from the institutions and disbursement of monies for the payment of bond interest and principal.

***Debt Service Reserve Funds* –** These funds record the receipt of a portion of the bond proceeds held in reserve to comply with the various bond resolutions. The balances are generally required to be maintained at an amount equal to the greatest amount of principal and interest payable in the current or any future bond year.

***Loan Reserve Funds* –** These funds are used to repay the principal and interest of the institutions' repayment schedule.

***Project Reserve Funds* –** These funds account for the receipt and disbursement of assets that are held for major repairs. The establishment of these funds is required by some bond issue documents.

***Rebate Funds* –** These funds account for the accumulation of assets used to make arbitrage rebate payments to the Federal government under the Internal Revenue Code. The Federal government requires the rebate of amounts earned on the investment of tax-exempt bond proceeds in excess of the yield on the bonds.

***Redemption Funds* –** These funds account for the accumulation of assets not required by other funds for the eventual redemption or purchase of bonds.

***Renewal and Replacement Funds* –** These funds account for moneys that are deposited to cover anticipated expenses for major repairs of the project whose revenues are pledged to the bonds or for repair and replacement of related equipment.

***Special Capital Reserve Funds* –** These funds are maintained to ensure compliance with minimum capital reserve requirements of bond issues. Any deficiencies in the reserves are required to be funded by the institution after notification by the trustee. If the bond was issued under Section 10a-186a of the General Statutes, the State is obligated to replenish the fund if the institution does not.

***Working Capital Reserve Funds* –** These funds are used if an institution fails to make its principal or interest payments on its loan. These funds are used before any withdrawals from the Special Capital Reserve Fund are made.

The assets of the Debt Service and Bond Funds, Debt Service Reserve Funds, Loan Reserve Funds, Project Reserve Funds, Rebate Funds, Redemption Funds, Renewal and Replacement Funds, Special Capital Reserve Funds, and Working Capital Reserve Funds are held by trustees in accordance with the bond resolutions. The funds of the Construction and Project Funds are controlled by CHEFA, which has a fiduciary responsibility for them.

RÉSUMÉ OF OPERATIONS:

The financial position of the Authority as of June 30, 2006 and 2007, per its audited financial statements, is presented below.

	As of June 30,	
	2007	2006
Assets		
Current Assets		
Unrestricted Assets:		
Cash	$ 180,000	$ 101,000
Accounts Receivable, Net of Allowance for Bad Debt	256,000	252,000
Investments	21,386,000	20,425,000
Prepaid Expenses and Other	121,000	120,000
Total Unrestricted Assets	21,943,000	20,898,000
Restricted Assets:		
Cash	162,000	129,000
Fund Investments	536,437,000	468,240,000
Other Investments	4,708,000	3,185,000
Other Receivables	90,000	59,000
Total Unrestricted Assets	541,397,000	471,613,000
Total Current Assets	563,340,000	492,511,000
Noncurrent Assets		
Investments (Restricted)	2,247,000	2,247,000
Capital Asset, Net of Depreciation	254,000	275,000
Total Noncurrent assets	2,501,000	2,522,000
Total Assets	**$ 565,841,000**	**$ 495,033,000**
Liabilities and Net Assets		
Current Liabilities		
Accounts Payable and Accrued Expenses	$ 1,799,000	$ 2,230,000
Amounts Held for Institutions	541,335,000	471,585,000
Total Current Liabilities	543,134,000	473,815,000

Noncurrent Liabilities		
Amount Held on Behalf of State of CT	2,247,000	2,247,000
Total Liabilities	545,381,000	476,062,000
Net Assets		
Invested in Capital Assets	254,000	275,000
Unrestricted	20,206,000	18,696,000
Total Net Assets	20,460,000	18,971,000
Total Liabilities and Net Assets	**$ 565,841,000**	**$ 495,033,000**

The Authority invests any excess funds in short-term investments and marketable securities, including the State Treasurer's Short Term Investment Fund (STIF) to earn investment income. Increases in the Authority's investments during the fiscal year ended June 30, 2007, are primarily from the recovery of $1.28 million in legal expenses incurred during the workout and sale of a skilled nursing home that had gone into bankruptcy during the fiscal year ended June 30, 2006.

The Authority holds $2,247,000 on behalf of the State of Connecticut to guarantee loans pursuant to Sections 17b-749g and 17b-749h of the General Statutes. Section 17b-749g established the Guaranteed Loan Fund Program and Section 17b-749h established the Small Direct Revolving Loan Program. The State provided $1.5 million and $750,000, respectively, to fund loan guarantees made under the programs. To date there has been one call on a loan guaranteed under the Small Direct Revolving Loan Program for a loss of $3,000. Funds held on behalf of the State of Connecticut are invested in the State Treasurer's Short Term Investment Fund (STIF).

Fund investments are investments associated with construction and project funds that are managed and held by the Authority on behalf of client institutions. Increases in fund investments during the fiscal year ended June 30, 2007, are due to proceeds of the bonds that were issued during the fiscal year.

A statement of revenues, expenses and changes in net assets for the fiscal years ended June 30, 2006 and 2007, follows. The information was obtained from the Authority's audited financial statements.

	As of June 30,	
	2007	**2006**
Operating Revenues		
Revenues from Institutions:		
Administrative Fees	$ 4,871,000	$ 4,542,000
Bond Issuance Fees	138,000	87,000
Miscellaneous Revenues	1,284,000	26,000
Total Operating Revenues	6,293,000	4,655,000

Operating Expenses		
Salaries and Related Expenses	2,297,000	1,915,000
Grant Expenses	2,083,000	2,216,000
Other Operating Expenses	1,452,000	1,924,000
Total Operating Expenses	5,832,000	6,055,000
Operating Gain (Loss)	461,000	(1,400,000)
Non-Operating Revenues		
Income from Investments	1,028,000	844,000
Change in Net Assets	1,489,000	(556,000)
Net Assets, Beginning of Year	18,971,000	19,527,000
Net Assets, End of Year	**$ 20,460,000**	**$ 18,971,000**

Total revenues for the fiscal year ended June 30, 2007, were $7,321,000, a $1,822,000 increase over the fiscal year ended June 30, 2006. The Authority charges an annual administrative fee to institutions with outstanding bond issues to cover operating expenses of the Authority. All issues other than those under the Special Capital Reserve Program are charged an annual fee of nine basis points on the outstanding par amount of the bonds. Bonds issued under the Special Capital Reserve Program are charged an annual fee of fourteen basis points. The increase in administrative fees was caused by the additional fee generated by new bonds that were issued during the fiscal year. The Authority also charges a bond issuance fee of $5,000 for each bond issue. The $1.284 million in miscellaneous revenues reflects moneys recovered for legal expenses incurred during the workout and sale of a skilled nursing home that had gone into bankruptcy during the fiscal year ended June 30, 2006. Income from investments increased during the fiscal year ended June 30, 2007, because of an increase in the amount invested and a higher average yield for investments. The average yield during fiscal year 2007 was 5.518 percent as compared to 4.404 percent for fiscal year 2006.

Operating expenses of the Authority totaled $5,832,000 during the fiscal year ended June 30, 2007, a $223,000 decrease from fiscal year ended June 30, 2006. The Authority's operating expenses consists of salary expenses, grant expenses, and other operating expenses. Salary expenses increased during the fiscal year by $382,000. The increase was caused by the addition of two new positions and labor grade adjustments for employees. The labor grade adjustments were in response to the Governor's request for quasi-public agencies to review and alter its compensation policies. The Authority engaged an outside consultant firm to complete a compensation study and to make recommendations for changes in compensation. Grant expenses decreased by $133,000 from the fiscal year ended June 30, 2006. The amount of grants awarded during a fiscal year depends on the availability of funding. Other operating expenses decreased by $472,000 from fiscal year ended June 30, 2006. This decrease is primarily to a decrease in legal expenses associated with the workout and sale of a skilled nursing home that went into bankruptcy during the fiscal year ended June 30, 2006.

CONDITION OF RECORDS

Our review of the records of the Connecticut Health and Educational Facilities Authority revealed the following areas that warrant comment.

Written Policies:

Criteria: Section 10a-179(h) of the General Statutes provides that the Board of Directors of the Authority shall adopt written procedures for various administrative areas.

Condition: It appears that the Authority was not aware that some of its written procedures existed because these procedures were not provided to us until after the audit fieldwork was completed even though we requested all of the written procedures at the start of the audit. Due to not getting these procedures in a timely manner, we were unable to test whether the Authority followed all of these procedures. At the start of the audit the Authority did provide us with some procedures that we were able to test.

We noted that the Authority did not follow at least two of its written procedures. These areas were as follows.

- Obtaining approval by the Board of Directors prior to filling vacant staff positions.
- Having checks signed by employees that were not included as positions authorized to sign checks in the Authority's written procedures.

Effect: By not following its written procedures, the Authority could have weakened internal controls. Strong internal controls are necessary to ensure the safeguarding of assets, the reliability of financial records, and compliance with laws and regulations.

Cause: The Authority did not consider the need to update written procedures for all of its policies to reflect the Authority's current practices.

Recommendation: The Connecticut Health and Educational Facilities Authority should update all written procedures as required by Section 10a-179(h) of the General Statutes as necessary and should adhere to its written procedures. (See Recommendation 1.)

Agency Response: "Written procedures were adopted by the Authority's Board in December 1988 and said procedures took effect on January 1, 1989. The Authority hereby agrees to update said written procedures as necessary."

Contracted Professional Services:

Criteria: Section 10a-179(h)(4) of the General Statutes provides that the Board of Directors of the Authority shall adopt written procedures for contracting for financial, legal, bond underwriting and other professional services, including a requirement that the Authority solicit proposals at least once every three years for each such service which it uses.

Condition: We noted that the Authority did not solicit proposals at least once every three years for some contracted professional services.

Effect: The Authority is not in compliance with Section 10a-179(h)(4) of the General Statutes.

Cause: The Authority considered some of the contractors to be sole source providers. However, it does not appear that the providers are the only contractors who could provide the applicable services.

Recommendation: The Connecticut Health and Educational Facilities Authority should solicit proposals at least once every three years for all contracted professional services as required under Section 10a-179(h)(4) of the General Statutes. (See Recommendation 2.)

Agency Response: "The Authority hereby acknowledges that it has not solicited proposals every three years for four of its contracted professionals including those for payroll processing services, information technology programming services, and loan origination/servicing for the Child Care Facilities Loan Fund (CCFLF) Guaranteed Loan Fund Program and Small Direct Loan Fund. The Authority does not believe it can or should be required to solicit proposals in the future for the aforementioned services due to the unique nature of the services required and the limited availability of contractors for said services. The following further explains the Authority's position:

1. Payroll Processing Services – the annual cost for these services to date has approximated $5,100 or below. ADP [Automatic Data Processing, Inc.] has provided these services to the Authority for many years, with a very low margin of error, and in a manner that meets its needs. We do not believe that it would be economically or operationally prudent to move these services to another provider.

2. Information Technology Programming Services – the current contractor Aniello Associates has provided these services for over twenty years. This contractor is a sole source provider that developed a customized system for the Authority's bond issue trust and investment accounting system, they have maintained the system for the Authority, and they make modifications to the customized system as necessary.

3. CCFLF Guaranteed Loan Fund – when this program was established pursuant to PA 97-259, it was structured to have participation by seven lending institutions that agreed to share equally in the loan risk which was supported by a State and Authority loan guaranty. Only one of the seven banks offered to assume the role of the loan originator/servicer, Peoples United Bank. Since the other Banks were not willing to serve as loan originator/servicer, we don't believe that we have any other option and therefore we will continue to use Peoples United Bank.

4. CCFLF Small Direct Loan Fund – CTCIC [Connecticut Community Investment Corporation] is a Federally funded Statewide Small Business Administration (SBA) lender. The loans made under this program, subject to a maximum loan of $25,000, are made in conjunction with much larger SBA loans. The loan structure is somewhat unique, CTCIC has agreed to function as the loan originator and servicer, CTCIC has agreed to provide these services with a management fee that is based on the investment earnings of the Small Direct Loan Fund Protection Account which has an approximate balance of $750,000. Our options are limited and therefore we will continue to use CTCIC."

Auditors' Concluding Comment: Section 10a-179(h)(4) of the General Statutes does not provide any exceptions to the requirement to solicit proposals at least once every three years for all contracted professional services.

Penalty of False Statement:

Criteria: Section 1-126 of the General Statutes provides that any quasi-public agency shall require any application, agreement, or other writing submitted to it with respect to any loan, mortgage, guarantee, investment, grant, lease, tax relief, bond financing or other extension of credit or financial assistance, that provides information on which the decision of such quasi-public agency was based, to be signed under penalty of false statement as provided in Section 53a-157b of the General Statutes.

Section 53a-157b of the General Statutes provides that a person is guilty of false statement in the second degree when the person intentionally makes a false written statement pursuant to a form bearing notice of such punishment.

Condition: Some of the Authority's financial assistance applications and agreements do not contain the required false statement provisions. The Authority provides financial assistance in the form of grants, loans, and bonds.

Effect: The Authority is not in compliance with Section 1-126 of the General Statutes.

Cause: The Authority neglected to include a false statement provision in all of its financial assistance applications and agreements.

Recommendation: The Connecticut Health and Educational Facilities Authority should include a penalty for false statement provision in all of its financial assistance applications and agreements as required under Section 1-126 of the General Statutes. (See Recommendation 3.)

Agency Response: "Management agrees with this comment and has already taken steps to correct this non-compliance.

1. The Child Care Pooled Bond Issue Series F documents will be amended to include the requirements of Section 1-126.

2. All grant applications and agreements from this point forward will include the requirements of Section 1-126.

3. The EasyLease and EasyLoan applications and documents from this point forward will include the requirements of Section 1-126."

Grants:

Criteria: Section 10a-180(u) of the General Statutes authorizes the Authority to make grants or provide other forms of financial assistance to any institution for higher education, to any health care institution, to any nursing home, to any child care or child development facility and to any qualified nonprofit organization in such amounts, for such purposes and subject to such eligibility and other requirements as are established pursuant to written procedures adopted by the Board of Directors pursuant to subsection (h) of Section 10a-179.

Condition: Grant awards for the acquisition of assets do not specify a minimum amount of time the grant recipient must use or obtain ownership of the asset. The Authority verifies that grant funds are used to purchase the asset as required in the grant agreement. However, it does not verify that the asset is used for its intended purpose for a reasonable period of time.

Effect: Without having a set time frame, grant recipients are not discouraged from using the asset for something other than it was intended or from disposing of the asset prematurely.

Cause: The Authority did not consider the need to include a minimum time period in the grant agreement in which assets purchased with grant funds should be used.

Recommendation: The Connecticut Health and Educational Facilities Authority should specify a minimum time period for which capital assets purchased with grant funds should be used. In addition, the Authority should monitor whether the asset is being used for its intended purpose for the specified time. (See Recommendation 4.)

Agency Response: "Management agrees with this comment and will implement the recommendation as part of the approval process for the current grant cycle, which has an application deadline of October 15, 2008."

Annual Report:

Criteria: Section 1-123 of the General Statutes provides that the Board of Directors shall annually submit a report to the Governor and the Auditors of Public Accounts and two copies of such report to the Legislative Program Review and Investigations Committee. Such report should include the following:

1. A list of all bond issues for the preceding fiscal year, including, for each such issue, the financial advisor and underwriters, whether the issue was competitive, negotiated or privately placed, and the issue's face value and net proceeds;

2. A list of all projects, other than those pertaining to owner-occupied housing or student loans, receiving financial assistance during the preceding fiscal year, including each project's purpose, location, and the amount of funds provided by the agency; and

3. A list of all outside individuals and firms receiving in excess of five thousand dollars in the form of loans, grants or payments for services, except for individuals receiving loans for owner-occupied housing and education.

Condition: Our review of the Authority's annual report for the fiscal year ended June 30, 2007, disclosed the following:

1. The list of bond issues did not provide whether the issues were competitive or negotiated.

2. The list of projects receiving financial assistance did not include each project's purpose, location, and the amount of funds provided by the

Authority for funds disbursed under two grant programs. Total payments made under these two grant programs totaled $764,909.

3. The list of outside individuals and firms receiving in excess of five thousand dollars excluded one vendor that was paid $11,781. In addition, although the amount paid to each vendor is not required to be included, we noted that the amounts listed for three vendors were incorrect.

Effect: Some information contained in CHEFA's annual report was incomplete.

Cause: The first condition was caused because the Authority was not aware that it needed to indicate whether the bond issue was competitive or negotiated. The Authority merely thought that it needed to indicate whether it was a public or private issue. The second and third conditions appear to have been oversights.

Recommendation: The Connecticut Health and Educational Facilities Authority should ensure that its annual report contains all information required under Section 1-123 of the General Statutes. (See Recommendation 5.)

Agency Response: "Management agrees with this comment and will implement the recommendation in conjunction with the filing of the annual report required under C.G.S. Section 1-123."

Segregation of Duties:

Criteria: Good internal control includes a plan of organization, procedures, and records designed to safeguard assets and provide reliable financial records. A system of internal control should include proper segregation of duties so that no one individual is capable of handling all phases of a transaction from beginning to end.

Condition: We found that the same employee who enters payroll amounts in the Authority's payroll system also authorizes the processing of the payroll checks. In addition, there is no regular review of the amounts being paid to employees.

Effect: The lack of segregation of duties increases the risk that errors or irregularities may go undetected.

Cause: The Authority did not consider the need to separate the function of processing payroll with authorizing the processing of payroll checks.

Recommendation: The Connecticut Health and Educational Facilities Authority should either segregate the duties of entering payroll amounts and authorizing payroll processing or should implement a review of the payroll process. (See Recommendation 6.)

Agency Response: "Management agrees with this comment and has already implemented the recommendation. There is now an appropriate segregation of duties whereby the Controller prepares the payroll, enters the data into the payroll system and prints out a payroll preview which is then reviewed by the Chief Financial Officer (CFO). The CFO reviews the payroll to ensure that the proper hours and pay rates are utilized. The CFO then signs and dates the report authorizing the Controller to transmit the payroll information. Once the actual payroll is received the CFO reviews the actual payroll to ensure that there have been no changes made without proper authorization between the payroll preview and the actual payroll."

RECOMMENDATIONS

Status of Prior Audit Recommendations:

There were no recommendations developed for the prior report that covered the fiscal year ended June 30, 2006.

Current Audit Recommendations:

1. **The Connecticut Health and Educational Facilities Authority should update all written procedures as required by Section 10a-179(h) of the General Statutes as necessary and should adhere to its written procedures.**

   Comment:

   Our review disclosed that the Authority does not follow all of its written procedures. In addition, it appears that the Authority was not aware that some of its written procedures existed.

2. **The Connecticut Health and Educational Facilities Authority should solicit proposals at least once every three years for all contracted professional services as required under Section 10a-179(h)(4) of the General Statutes.**

   Comment:

   The Authority did not solicit proposals at least once every three years for some contracted professional services.

3. **The Connecticut Health and Educational Facilities Authority should include a penalty for false statement provision in all of its financial assistance applications and agreements as required under Section 1-126 of the General Statutes.**

   Comment:

   Our review disclosed that some of the Authority's financial assistance applications and agreements do not contain the required false statement provisions. The Authority provides financial assistance in the form of grants, loans, and bonds.

4. **The Connecticut Health and Educational Facilities Authority should specify a minimum time period for which capital assets purchased with grant funds should be used. In addition, the Authority should monitor whether the asset is being used for its intended purpose for the specified time.**

   Comment:

   Grant awards for the acquisition of assets do not specify a minimum amount of time the grant recipient must use or obtain ownership of the asset. The Authority verifies that grant funds are used to purchase the asset as required in the grant agreement. However, it does not verify that the asset is used for its intended purpose for a reasonable period of time.

5. **The Connecticut Health and Educational Facilities Authority should ensure that its annual report contains all information required under Section 1-123 of the General Statutes.**

   Comment:

   Our review of the Authority's annual report for the fiscal year ended June 30, 2007, disclosed that it does not contain all information required under Section 1-123 of the General Statutes.

6. **The Connecticut Health and Educational Facilities Authority should either segregate the duties of entering payroll amounts and authorizing payroll processing or should implement a review of the payroll process.**

   Comment:

   Our review disclosed that the same employee who enters payroll amounts in the Authority's payroll system also authorizes the processing of the payroll checks. In addition, there is no regular review of the amounts being paid to employees. The lack of segregation of duties increases the risk that errors or irregularities may go undetected.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 and Section 1-122 of the General Statutes, we have conducted an audit of the State of Connecticut Health and Educational Facilities Authority's activities for the fiscal year ended June 30, 2007. This audit was primarily limited to performing tests of the Authority's compliance with certain provisions of laws, regulations, contracts and grant agreements, including but not limited to a determination of whether the Authority has complied with its regulations concerning affirmative action, personnel practices, the purchase of goods and services, the use of surplus funds and the distribution of loans, grant agreements and other financial resources, and to understanding and evaluating the effectiveness of the Authority's internal control policies and procedures for ensuring that the provisions of certain laws, regulations, contracts and grant agreements applicable to the Authority are complied with. The financial statement audit of the Authority, for the fiscal year indicated above, was conducted by the Authority's independent public accountants.

We conducted our audit in accordance with the requirements of Section 2-90 and Section 1-122 of the General Statutes. In doing so, we planned and performed the audit to obtain reasonable assurance about whether the Authority complied in all material respects with the provisions of certain laws, regulations, contracts and grant agreements and to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing and extent of tests to be performed during the conduct of the audit.

Internal Control over Financial Operations and Compliance:

In planning and performing our audit, we considered the Connecticut Health and Educational Facilities Authority's internal control over its financial operations and its compliance with requirements as a basis for designing our auditing procedures for the purpose of evaluating the Authority's financial operations and compliance with certain provisions of laws, regulations, contracts and grant agreements, but not for the purpose of providing assurance on the effectiveness of the Authority's internal control over those control objectives. Our consideration of internal control included, but was not limited to, the following areas:

- Affirmative action
- Personnel practices
- Purchase of goods and services
- Use of surplus funds
- Distribution of loans, grants and other financial resources.

Our consideration of the internal control over the Authority's financial operations and over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial operations and compliance with requirements that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial operations and compliance with requirements that we consider to be significant deficiencies.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect on a timely basis unauthorized, illegal, or irregular transactions. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the Authority's ability to properly initiate, authorize, record, process, or report financial data reliably consistent with management's direction, and/or comply with certain provisions of laws, regulations, contracts, and grant agreements such that there is more than a remote likelihood that noncompliance with laws, regulations, contracts and grant agreements that is more than inconsequential will not be prevented or detected by the Authority's internal control. We consider the following deficiencies, described in detail in the accompanying "Condition of Records" and "Recommendations" sections of this report, to be significant deficiencies in internal control over financial operations and compliance with requirements: Recommendation 1 – Written policies and Recommendation 6 – Segregation of duties over the payroll function.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that noncompliance which could result in significant unauthorized, illegal, irregular or unsafe transactions and/or material noncompliance with certain provisions of laws, regulations, contracts, and grant agreements that would be material in relation to the Authority's financial operations will not be prevented or detected by the Authority's internal control.

Our consideration of the internal control over the Authority's financial operations and compliance with requirements was for the limited purpose described in the first paragraph of this section and would not necessarily disclose all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that neither of the significant deficiencies described above is a material weakness.

Compliance and Other Matters:

As part of obtaining reasonable assurance about whether the Connecticut Health and Educational Facilities Authority complied with laws, regulations, contracts and grant agreements, noncompliance with which could result in significant unauthorized, illegal, irregular or unsafe transactions or could have a direct and material effect on the results of the Authority's financial operations for the fiscal year ended June 30, 2007, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, including but not limited to the following areas:

- Affirmative action
- Personnel practices
- Purchase of goods and services
- Use of surplus funds
- Distribution of loans, grants and other financial resources.

Our examination included reviewing all or a representative sample of the Authority's activities in those areas and performing such other procedures as we considered necessary in the circumstances.

The results of our tests disclosed no material or significant instances of noncompliance. However, we noted certain matters which we reported to Authority management in the accompanying "Condition of Records" and "Recommendations" sections of this report.

This report is intended for the information of the Governor, the State Comptroller, the Appropriations Committee of the General Assembly and the Legislative Committee on Program Review and Investigations. However, this report is a matter of public record and its distribution is not limited. Users of this report should be aware that our audit does not provide a legal determination of the Authority's compliance with the provisions of the laws, regulations, contracts and grant agreements included within the scope of this audit.

CONCLUSION

We wish to express our appreciation for the cooperation and courtesies extended to our representatives by the personnel of the Connecticut Health and Educational Facilities Authority during our examination.

Catherine L. Dunne
Auditor 2

Approved:

Kevin P. Johnston
Auditor of Public Accounts

Robert G. Jaekle
Auditor of Public Accounts