STATE OF CONNECTICUT

AUDITORS' REPORT
CONNECTICUT HIGHER EDUCATION
SUPPLEMENTAL LOAN AUTHORITY
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

AUDITORS OF PUBLIC ACCOUNTS

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October 18, 2006

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FOR THE FISCAL YEAR ENDED JUNE 30, 2005

We have examined the books, records, and accounts of the Connecticut Higher Education Supplemental Loan Authority, as provided in Section 2-90 and Section 1-122 of the General Statutes, for the fiscal year ended June 30, 2005.

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 regulations 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 its 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 objects. 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 other such areas as we considered necessary. The financial statement audit of the Connecticut Higher Education Supplemental

Loan Authority, for the fiscal year ended June 30, 2005, was conducted by the Authority's independent public accountants.

COMMENTS

FOREWORD:

The Connecticut Higher Education Supplemental Loan Authority (hereafter referred to as CHESLA) operates primarily under the provisions of Title 10a, Chapter 187b, Sections 10a-221 through 10a-246 of the Connecticut General Statutes.

Effective October 1, 1985, Section 10a-232 permits CHESLA to create and establish one or more Special Capital Reserve Funds for which the State of Connecticut has a contingent liability.

CHESLA is a quasi-public agency and political subdivision of the State. CHESLA's purpose is to assist borrowers (students, their parents or others responsible for paying the costs of education) and institutions of higher education in the financing and refinancing of the costs of higher education through its Bond Funds. During the audited period, CHESLA reported no loans to institutions.

Under CHESLA's Connecticut Family Education Loan Program, qualifying applicants can receive an Education Loan for each academic year in an amount that does not exceed the student's cost of education for the year. The cost of education is determined by the college or university in which the student is enrolled and is reduced by all other financial assistance received by the student.

CHESLA is defined by the General Statutes as a Quasi-Public Agency. Provisions for Quasi-Public Agencies are codified primarily in Sections 1-120 through 1-127 of Chapter 12 of the General Statutes. The provisions require that an annual compliance audit be performed addressing CHESLA's compliance with its regulations concerning affirmative action, personnel practices, the purchase of goods and services, the use of surplus funds, and the distribution of loans, grants and other financial assistance. Effective July 1, 2004, Public Act 03-133, as codified in Section 1-122 of the General Statutes, required that the Auditors of Public Accounts perform or contract out such audits. This is our report on our audit of CHESLA's compliance with these requirements during the audited period.

Board Members:

As authorized under Section 10a-224 of the General Statutes, the powers of CHESLA are vested in an eight member board of directors, consisting of the State Treasurer, the Secretary of the Office of Policy and Management, and the Commissioner of Higher Education, all serving as ex-officio directors, and five directors appointed by the Governor.

As of June 30, 2005, CHESLA's board of directors was as follows:

Ex-Officio:

Denise L. Nappier, State Treasurer
Robert L. Genuario, Secretary of the Office of Policy and Management
Valerie F. Lewis, Commissioner of Higher Education

Appointed by the Governor:	Term Expires July 1,
Michael E.McKeeman, Chairman	2008
Frank R. A. Resnick	2005
Julie B. Savino	2005
William J. Pizzuto	2006
Delores P. Graham	2009

Gloria F. Ragosta was appointed the Executive Director of CHESLA on May 19, 1998, and has served in that position throughout the audited period.

Accounting Policies:

CHESLA maintains financial records for its own operation and for the debt issue outstanding in accordance with the requirements of bond issue documents. Assets of the Bond Issue Funds are held by a trustee. A brief description of each fund follows:

Authority Operating Fund – Revenues and expenses applicable to the Authority's operations are accounted for within this fund. Revenues are generated from interest income and administrative fees.

Bond Funds – CHESLA issues revenue bonds whose proceeds are used to provide loans directly to students and others to finance the cost of higher education. Bond Fund revenue is generated from interest earned on investments and loans outstanding.

Bond Issue Funds Outstanding as of June 30, 2005, included:

2005 Series A and B, 2003 Series A and B, 2001 Series A, 2000 Series A and B, 1999 Series A and B, 1998 Series A and B, and 1996 Series A.

During the period under review, CHESLA issued in total $37,355,000 in 2005 Series A and B Bonds, consisting of $31,455,000 in 2005 Series A Revenue Bonds and $5,900,000 in 2005 Series B Revenue Refunding Bonds. Refunding bonds are new bonds issued to retire an already outstanding bond issue. The refunding of bonds is most frequently done to take advantage of more favorable interest rates and to escape from less favorable bond covenants. By this and other measures, such as restricting its administrative fees and covering bond issuance costs from its operating fund, CHESLA seeks to achieve a competitive advantage in the market place for its student loans.

As of June 30, 2005, CHESLA had issued $300,580,000 in Revenue Bonds and Revenue Refunding Bonds with $130,645,000 outstanding. During the audited period, the aggregate amount of Special Capital Reserve Fund-backed (to be discussed below) bonds outstanding at any given time was limited by statute to $170,000,000.

With respect to bond issues outstanding as of June 30, 2005, the 1996, 1998, 1999, 2000, 2001, 2003, and 2005 Series loans may be made to finance educational needs, under the Connecticut Family Educational Loan Program (CT FELP), in principal amounts from $2,000 up to the costs of education for eligible students. Cumulative loan amounts are capped at $125,000 for each eligible student over the life of the CT FELP program.

CHESLA contracts for the following services, among others, to help it achieve its accounting objectives:

- Loan Servicer: Originates and services student loans.
- Accountant: Produces financial statements and supporting ledgers.
- Investors services: Invests and accounts for bond proceeds, payments.
- Financial Advisors: Performs underwriting, cash flow analyses, arbitrage calculations.
- Collection Agency: Pursues non-performing student loans.

Other Audit Examinations:

An independent certified public accountant audited the books and accounts of CHESLA for the fiscal year under review.

The independent public accountant's report to CHESLA for the fiscal year ended June 30, 2005, expressed an unqualified opinion on CHESLA's financial statements and reported no material weaknesses in internal control.

Section 1-122 of the Connecticut General Statutes requires that quasi-public agencies such as CHESLA have a compliance audit performed annually. Such audits should determine whether these agencies comply with their own regulations concerning affirmative action, personnel practices, the purchase of goods and services, the use of surplus funds, and the distribution of loans, grants and other financial assistance. In accordance with this statute, we performed the compliance audit of CHESLA covering the 2004-2005 fiscal year. We did not note any weaknesses in compliance or internal control.

RÉSUMÉ OF OPERATIONS:

CHESLA had issued 21 series of bonds as of June 30, 2005. The 1983 Series A Revenue Bonds were issued for the purpose of financing loans to Yale University, Wesleyan University, and Connecticut College in order to fund education loans to students, and parents of students, and to finance the students' attendance at such institutions. The 1985, 1990, 1991, 1993, 1994, 1996, 1998, 1999, 2000, 2001, 2003, and 2005 Series A Revenue Bonds and the 1998, 1999, and 2000 Series B Revenue Bonds were issued for the purpose of providing financial assistance directly to students in or from the State, their parents and others responsible for the costs of students attending eligible institutions for higher education under the Family Education Loan Program (FELP). The 1990, 1991, 2000, 2003, and 2005 Series B and 1992 Series A issues were Revenue Refunding Bonds.

The 2005 Series A Revenue Bonds and Series B Revenue Refunding Bonds, issued during the audited period, amounted to $31,455,000 and $5,900,000, respectively.

The bonds are special obligations of CHESLA, which has no taxing power. The bonds shall not be deemed to constitute a debt or liability to the State or any of its political subdivisions, but shall be payable solely from the revenues and other receipts, funds or moneys pledged therefore. However, effective October 1, 1985, the State became contingently liable in that it must provide annual debt service requirements if not met by CHESLA's funds. The State's contingent liability in connection with the various Series A and B Bonds is the Special Capital Reserve Fund requirement for such Bonds, funded as of June 30, 2005, in the aggregate amount of $9,050,000. As of June 30, 2005, the State has not made nor was it required to make any such deposit.

The Vice President of the Connecticut Conference of Independent Colleges (CCIC), Gloria F. Ragosta, served as the Executive Director of CHESLA. The Executive Director was compensated by CCIC. The CCIC charged CHESLA for services provided by the Executive Director, pursuant to a written agreement for services with the CCIC. Such fees totaled $102,000 for the fiscal year ended June 30, 2005.

CHESLA also entered into a sublease agreement with the CCIC for the use of office space in connection with CHESLA's operation. Under the agreement, CCIC charged CHESLA a monthly fee for the use of such space.

Revenues credited to Bond Funds totaled $9,402,852 for the fiscal year ended June 30, 2005. This amount consisted primarily of interest income derived from investments and loans to individuals.

Expenditures for the Bond Funds totaled $ 7,133,834 for the fiscal year ended June 30, 2005. This amount consisted primarily of debt service (interest). The Bond Funds balance of $3,458,215 as of June 30, 2004, increased to $5,727,233 as of June 30, 2005.

Revenues credited to the Authority Operating Fund for the fiscal year ended June 30, 2005, totaled $736,093 and consisted of administrative fees and investment income. Operating expenses paid from the Operating Fund during the same fiscal year totaled $781,412 and consisted primarily of professional and administrative expenses, and bond issuance costs. The Authority Operating Fund fund balance decreased from $3,069,250 at June 30, 2004, to $3,023,931 at June 30, 2005.

The cumulative number of loans made to students by CHESLA for all Bond Funds as of June 30, 2005, totaled 22,189, compared to 21,083 as of June 30, 2004, amounting to 1,106 additional loans over the audited period. The average of the cumulative dollar amount loaned to each student as of June 30, 2005, totaled $9,385.

CONDITION OF RECORDS

There were no recommendations developed as a result of this examination.

RECOMMENDATIONS

Status of Prior Audit Recommendations:

- The Authority should improve its internal control over purchasing and accounts payable operations by taking the following steps. The Board's Chairperson should provide written approval for the Executive Director's expense reimbursements. An employee, rather than the Executive Director, should reconcile Authority bank statements. The Executive Director should inform the Chairman of the Board Directors in writing when making non-budgeted expenditures below $2,000. The Authority should also take steps to ensure that its credit card purchases preclude any transactions that could be perceived to be unrelated to Authority business. In the current audit, we reviewed each of the four items included in this finding, and determined that the Authority has implemented procedures over these areas in order to improve internal control over purchasing and accounts payable. The Authority has taken corrective action on each of the four items included in this finding; therefore, the finding is not being repeated.

- The Authority should implement and adhere to a written policy limiting the hiring of relatives and other business dealings with relatives of Authority employees, board members, or the Executive Director. The Authority should either follow its own written vacation policies with respect to the carry over of vacation leave days from one year to the next or update these policies to reflect the Authority's actual practices. Further, Authority personnel policies should be updated to clearly and completely specify the number of vacation, sick and personal leave days granted to employees. In addition, the Authority should implement an employee time sheet system to document and support time worked and leave time used for each pay period. The Authority has reasonably addressed each matter included in this finding, so the finding is not being repeated.

Current Audit Recommendations:

There were no recommendations developed as a result of this examination.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 and Section 1-122 of the General Statutes, we have conducted an audit of the Connecticut Higher Education Supplemental Loan Authority's activities for the fiscal year ended June 30, 2005. 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 regulations concerning affirmative action, personnel practices, the purchase of goods and services, the use of surplus funds and the distribution of loans, grants 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 grants applicable to the Authority are complied with. The financial statement audit of the Connecticut Higher Education Supplemental Loan Authority, for the fiscal year indicated above, was conducted by the Authority's independent public accountants.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Connecticut Higher Education Supplemental Loan Authority complied in all material respects with the provisions of certain laws, regulations, contracts and grants and to obtain a sufficient understanding of the internal control to plan the audit and determine the nature, timing and extent of tests to be performed during the conduct of the audit.

Compliance:

Compliance with the requirements of laws, regulations, contracts and grants applicable to the Connecticut Higher Education Supplemental Loan Authority is the responsibility of the Authority's management.

As part of obtaining reasonable assurance about whether the Connecticut Higher Education Supplemental Loan Authority complied with laws, regulations, contracts and grants, 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, 2005, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 instances of noncompliance.

Internal Control

The management of the Connecticut Higher Education Supplemental Loan Authority is responsible for establishing and maintaining effective internal control over its financial operations and compliance with the requirements of laws, regulations, contracts and grants applicable to the Authority. In planning and performing our audit, we 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, 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 would not necessarily disclose all matters in the internal control that might be material or significant weaknesses. A material or significant weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with certain provisions of laws, regulations, contracts, and grants that would be material in relation to the Authority's financial operations or noncompliance which could result in significant unauthorized, illegal, irregular or unsafe transactions at the Authority may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control that we consider to be material or significant weaknesses.

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 Connecticut Higher Education Supplemental Loan Authority's compliance with the provisions of the laws, regulations, contracts and grants included within the scope of this audit.

CONCLUSION

We wish to express our appreciation for the courtesies and cooperation extended to our representatives by the personnel of the Connecticut Higher Education Supplemental Loan Authority during the course of our examination.

Timothy M. LePore
Principal Auditor

Approved:

Kevin P. Johnston
Auditor of Public Accounts

Robert G. Jaekle
Auditor of Public Accounts