

STATE OF CONNECTICUT



*AUDITORS' REPORT
DEPARTMENT OF ECONOMIC AND
COMMUNITY DEVELOPMENT
FISCAL YEARS ENDED JUNE 30, 2017, 2018 AND 2019*

AUDITORS OF PUBLIC ACCOUNTS
JOHN C. GERAGOSIAN ❖ ROBERT J. KANE

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March 31, 2021

EXECUTIVE SUMMARY

In accordance with the provisions of Section 2-90 of the Connecticut General Statutes, we have audited certain operations of the Department of Economic and Community Development (DECD) for the fiscal years ended June 30, 2017, 2018, and 2019. Our audit identified internal control deficiencies; instances of noncompliance with laws, regulations, and policies; and a need for improvement in practices and procedures that warrant the attention of management. The significant findings and recommendations are presented below:

Page 10	DECD issued \$49,410,602 more in film production tax credits to a digital animation company than it would have been entitled to under the digital animation tax credit program. DECD should ensure that digital animation companies do not receive more than \$15 million in tax credits in any one fiscal year as required by Section 12-217ll of the General Statutes. (Recommendation 1.)
Page 11	DECD awarded \$1.5 million excess financial assistance than permitted under the General Statutes. DECD should ensure that the amount of financial assistance it provides to a business is not greater than amounts allowed under the General Statutes without obtaining authorization from the General Assembly. (Recommendation 2.)
Page 16	We reviewed 25 projects for which DECD provided \$129,659,000 in financial assistance and noted that the department did not perform a financial review for 7 projects totaling \$97 million, did not verify whether 4 companies that received \$23.2 million in assistance had pending litigation, and did not determine whether one company that received \$22 million in assistance owed outstanding taxes to the Department of Revenue Services. DECD should conduct financial reviews of its funding in the First Five, Brownfield, and Manufacturing Assistance Act programs. In addition, DECD should clearly document that any financial review concerns have been sufficiently resolved. (Recommendation 4.)
Page 25	During the prior audit, we noted that DECD did not consistently apply relocation requirements to tax credits. Our review of 5 Urban and Industrial Site Reinvestment tax credits disclosed that the department did not require two companies to repay the credits when they relocated out of state. DECD awarded \$2,725,518 of the \$27,255,184 approved tax credits for these projects. DECD should ensure that it requires companies to repay all forms of financial assistance if they relocate out of state within the relocation period, and should implement adequate procedures to determine whether companies have relocated out of state. (Recommendation 9.)
Page 26	DECD did not sufficiently gauge demand for equipment prior to awarding a grant for its purchase, did not require the grantee to use the equipment for a minimum period, and did not sufficiently plan for its use after the expiration of a grant award. DECD paid \$6,533,109 to the grantee under various assistance agreements despite the grantee not fulfilling reporting requirements in a remedy letter. DECD should adequately monitor grant recipients and should ensure that they comply with reporting requirements. In addition, the department should complete its due diligence, and sufficiently gauge the demand for equipment prior to awarding a grant for its purchase and should ensure that the grantee uses the equipment for a sufficient period. (Recommendation 10.)

STATE OF CONNECTICUT



AUDITORS OF PUBLIC ACCOUNTS

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March 31, 2021

AUDITORS' REPORT DEPARTMENT OF ECONOMIC AND COMMUNITY DEVELOPMENT FISCAL YEARS ENDED JUNE 30, 2017, 2018 AND 2019

We have audited certain operations of the Department of Economic and Community Development in fulfillment of our duties under Section 2-90 of the Connecticut General Statutes. The scope of our audit included, but was not necessarily limited to, the years ended June 30, 2017, 2018, and 2019. The objectives of our audit were to:

1. Evaluate the department's internal controls over significant management and financial functions;
2. Evaluate the department's compliance with policies and procedures internal to the department or promulgated by other state agencies, as well as certain legal provisions; and
3. Evaluate the effectiveness, economy, and efficiency of certain management practices and operations, including certain financial transactions.

Our methodology included reviewing written policies and procedures, financial records, minutes of meetings, and other pertinent documents; interviewing various personnel of the department; and testing selected transactions. Our testing is not designed to project to a population unless specifically stated. We obtained an understanding of internal controls that we deemed significant within the context of the audit objectives and assessed whether such controls have been properly designed and placed in operation. We tested certain of those controls to obtain evidence regarding the effectiveness of their design and operation. We also obtained an understanding of legal provisions that are significant within the context of the audit objectives, and we assessed the risk that illegal acts, including fraud, and violations of contracts, grant agreements, or other legal provisions could occur. Based on that risk assessment, we designed and performed procedures to provide reasonable assurance of detecting instances of noncompliance significant to those provisions.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The accompanying Résumé of Operations is presented for informational purposes. This information was obtained from various available sources including, but not limited to, the department's management and the state's information systems, and was not subjected to the procedures applied in our audit of the department. For the areas audited, we:

1. Identified deficiencies in internal controls;
2. Identified apparent non-compliance with laws, regulations, contracts and grant agreements, policies, and procedures; and
3. Identified a need for improvement in management practices and procedures that we deemed to be reportable.

The State Auditors' Findings and Recommendations section of this report presents findings arising from our audit of the Department of Economic and Community Development.

COMMENTS

FOREWORD

The Department of Economic and Community Development (DECD) operates principally under the provisions of Title 32, Chapter 578 and Title 10, Chapter 184b of the General Statutes. DECD administers programs and policies to promote business, community development, brownfield redevelopment, arts, culture and tourism, and is the state agency responsible for promoting economic growth.

The department's mission is to develop and implement strategies to increase the state's economic competitiveness. Specifically, DECD:

- Supports existing businesses and attracts new businesses and jobs with a wide range of programs and services to help companies prosper;
- Promotes Connecticut industries and businesses here at home, throughout the country, and across the globe;
- Strengthens Connecticut communities by providing funding and technical support for local community and economic development projects;
- Works to make tourism a leading economic contributor and a source of pride for Connecticut;
- Develops and strengthens the arts in Connecticut, making artistic experiences widely available to residents and visitors; and
- Helps to eliminate brownfield properties by promoting smart growth principles, strengthening public-private partnerships, and providing a one-stop resource for expertise.

Catherine H. Smith was appointed commissioner of DECD in April 2011 and served in that capacity until January 2019. David Lehman was appointed as commissioner of DECD in February 2019.

Significant Legislation

The following notable legislative changes affecting the department took effect during the audited period:

- **Public Act 16-128**, effective upon passage, established within the Small Business Express program, up to two minority business revolving loan funds to support the growth of small minority-owned businesses. To establish the funds, the act required the DECD commissioner to allocate \$5 million in grants to up to two minority business development entities in each fiscal year from 2016 through 2020.
- **Public Act 16-3 of the May Special Session, Section 15**, effective upon passage, created an incentive for technology-based businesses receiving state economic development loans or other financial assistance to mentor other businesses through CTNext’s mentorship network. The act allowed the DECD commissioner to forgive a portion of that assistance based on the number of hours the business spent mentoring another business.

Section 23, effective upon passage, established a Technology Talent Advisory Committee within DECD to identify shortages of qualified employees in specific technology sectors and develop pilot programs to address those shortages.

- **Public Act 16-1 of the September Special Session**, effective upon passage, established a framework for providing financial incentives to eligible aerospace companies engaging in certain helicopter manufacturing projects. An eligible company may receive up to \$140 million in grants and \$80 million in sales and use tax offsets for the project over a 14-year term. DECD must certify projects and enter into agreements with eligible companies to provide the incentives.

Public Act 17-2 of the June Special Session, Section 168, effective upon passage, established the 7/7 program to provide incentives to businesses for redeveloping and utilizing brownfield and real property that has been abandoned or underutilized for 10 or more years within DECD. Applicants must apply to DECD for these incentives and provide certain information, including a commitment to hire local students to work at the redeveloped property. The incentives are available in two seven-year stages. During the first 7 years after an owner redevelops an approved property, the owner qualifies for corporation business or personal income tax credits, and sales and use tax exemptions. During the next 7 years if the property was a brownfield, the owner qualifies for business or personal income tax deductions.

Section 566, effective upon passage, applied prevailing wage requirements to any construction project with \$1 million or more of DECD financial assistance provided on or after July 1, 2018.

Sections 637 and 639, effective upon passage, established a Tourism Fund and required the Commissioner of Revenue Services to deposit 10% of the amount received from the room occupancy tax into the fund.

Section 701-703, effective upon passage, required DECD to establish and administer a program that allows in-state businesses to use stranded research and development credits in exchange for undertaking eligible in-state capital projects. The act also required the DECD commissioner, in consultation with the Department of Revenue Services commissioner and Connecticut Innovations, to hold tax credit auctions, or enter into agreements, to allow taxpayers holding these credits to use them in exchange for making certain venture capital investments.

- **Public Act 17-162**, effective October 1, 2017, tightened the criterion for determining whether businesses must repay, with a penalty, any state economic development assistance they received if they relocate outside Connecticut within a specified period. Under the act, a business must repay the assistance and a penalty if the company transferred a substantial portion of its operation, or those of any of its divisions, out of state. Under prior law, the business had to repay the assistance plus a penalty only if it transferred its entire operation or any of its divisions out of state.
- **Public Act 17-219, Section 2**, effective October 1, 2017, established a loan guarantee and short-term bridge loan fund developed in consultation with private sector lenders as part of the Small Business Express program.
- **Public Act 18-85**, effective July 1, 2018, extended the maximum period for repaying certain Brownfield loans from 20 to 30 years.

Boards, Commissions, Committees, and Councils

Name	General Statute Section	Statutory Responsibilities
State Historic Preservation Board	§10-321q	Review nominations to the National Register of Historic Places to determine whether the property meets the National Register criteria for evaluation and to make a recommendation that the State Historic Preservation Officer either nominate or reject the proposed nomination.
Culture and Tourism Advisory Committee	§10-393	Provide guidance to DECD with regard to enhancing and promoting culture, history, the arts, and the tourism and digital media and motion picture industries in Connecticut.
Connecticut Arts Council	§10-408a and §10-408b	Foster and support the arts and manage the Connecticut Arts Council Foundation, which was established to raise funds for the purposes of fostering the creation, preservation and expansion of the arts in the state and the dissemination of information related to such activities.

Historic Preservation Council	§10-409	Advise DECD on critical historic preservation functions, review and approve requests to perform rehabilitation work on properties that DECD holds preservation restrictions, prevent the unreasonable destruction of historic properties with the assistance of the Office of the Attorney General, place and maintain suitable markers, memorials or monuments to designate sites or places of historical significance, and develop a model ballot for use by clerks of municipalities considering the establishment of local historic districts.
Sports Advisory Board	§10-425	Advise DECD on the most effective ways to utilize state resources to promote, attract, and market in-state professional and amateur sports and sporting events. In addition, the board coordinates the use of state-owned facilities to enhance sports-related tourism in the state and to develop methods for the dissemination of information concerning in-state professional and amateur sports and sporting events to residents of the state and the northeast.
Committee for the Restoration of Historic Assets in Connecticut	§32-6a	Encourage quality tourism and contribute to the overall historic preservation program. The commissioner of DECD may provide grants or loans as approved by the committee for projects of historic preservation and restoration from the Restoration of Historic Assets in Connecticut Fund.
Manufacturing Innovation Advisory Board	§32-7n	Oversee the Connecticut Manufacturing Innovation Fund, which supports the growth, innovation, and progress of the advanced manufacturing sector. Establish an application and approval process for financial assistance, and approve fund expenditures, budgets, and reports.
Technology Talent Advisory Committee	§32-7p	Identify shortages of qualified employees in specific technology sectors and develop pilot programs to address those shortages.
Small Business Advisory Board	§32-9xx	Provide guidance to DECD with regard to resources available to small businesses.
Commission on Connecticut's Future	§32-245	Advise the General Assembly and DECD on issues related to defense conversion, industrial policy, and the state's business climate; evaluate legislation related to the state's economy, particularly as it affects manufacturers and defense-related businesses; provide a forum for business issues; and stimulate and review public and private assistance to improve the state's economy.

RÉSUMÉ OF OPERATIONS

DECD operations for the fiscal years ended June 30, 2017, 2018, and 2019 were accounted for in the General Fund, special revenue funds, capital and non-capital improvement funds, and a trust fund. The activity of each of the funds is presented in the sections that follow.

General Fund

A summary of General Fund receipts during the audited period follows:

Receipt Description	Fiscal Year Ended June 30,		
	2017	2018	2019
Refunds of Expenditures	\$25,636	\$7	\$10,331
Sales and Use Tax	942	848	1,747
All Other	702	1,233	6,862
Total Receipts	\$27,280	\$2,088	\$18,940

The majority of General Fund revenues are from grant refunds. When a grant recipient does not spend all funds received for project expenditures, the excess disbursement is due to the state.

A summary of General Fund expenditures during the audited period follows:

Expenditure Description	Fiscal Year Ended June 30,		
	2017	2018	2019
Personal Services	\$6,607,388	\$6,728,491	\$6,789,929
Other Expenses	500,153	500,943	500,960
Statewide Marketing	6,435,000	6,435,000	-
Capital Region Development Authority	6,349,121	6,261,621	6,549,121
Arts Commission	1,471,743	1,402,432	-
Arts and Tourism Grants	3,125,908	3,155,491	-
Aquarium/Zoo/Museum Grants	1,606,296	1,429,037	-
Business Development	1,475,704	710,043	-
Main Street Initiatives	95,413	80,000	-
Office of Military Affairs	179,054	117,329	120,859
Total Expenditures	\$27,845,780	\$26,820,386	\$13,960,869

General Fund expenditures decreased by \$1,025,394 and \$12,859,517 during the fiscal years ended June 30, 2018, and 2019, respectively. The decrease in total expenditures during the fiscal year ended June 30, 2019 was primarily due to marketing, arts, culture, and tourism accounts being transferred from the General Fund to the Tourism Fund, established by Public Act 17-2 of the June Special Session.

Special Revenue Funds

DECD uses one of these funds to account for federal and other restricted monies. In addition, DECD utilized 9 other special revenue funds during the audited period. These funds were used primarily for providing financial assistance in the form of grants or loans for economic development.

A summary of receipts from special revenue funds during the audited period follows:

Receipt Description	Fiscal Year Ended June 30,		
	2017	2018	2019
Federal Contributions	\$6,883,123	\$5,293,201	\$4,454,595
Restricted Contributions, Other	26,392,310	24,310,969	32,390,988
Principal and Interest on Loans	27,397,681	57,361,760	39,447,713
All Other	243,606	1,483,892	9,055,510
Total Receipts	\$60,916,720	\$88,449,822	\$85,348,806

Total receipts from special revenue funds increased by \$27,533,102 during the fiscal year ended June 30, 2018 and decreased by \$3,101,016 during the fiscal year ended June 30, 2019. The increase in principal and interest payments during the fiscal year ended June 30, 2018 was primarily due to a company repaying a \$20 million loan including accrued interest and a relocation penalty, when it relocated out of state.

The growth in restricted contributions during the fiscal year ended June 30, 2019 was primarily attributable to an increase in grant transfers for the Small Business Express program. In addition, the increase in other receipts during the fiscal year ended June 30, 2019 was primarily due to amounts transferred to the new Tourism Fund. Public Act 17-2, Section 637 of the June Special Session requires the Commissioner of Revenue Services to deposit 10% of the amount received from the room occupancy tax to the Tourism Fund.

A summary of expenditures from special revenue funds during the audited period follows:

Expenditure Description	Fiscal Year Ended June 30,		
	2017	2018	2019
Loans	\$133,511,834	\$147,026,719	\$116,801,502
Grants	100,501,415	73,307,260	111,586,427
Administration	12,967,381	14,601,334	17,900,381
Total Expenditures	\$246,980,630	\$232,935,313	\$246,288,310

Total expenditures from special revenue funds decreased by \$14,045,317 and increased by \$13,352,997 during the fiscal years ended June 30, 2017, 2018, and 2019, respectively. Changes in loans and grants were mainly in the Manufacturing Assistance Act, Small Business Express, and Brownfield programs. The State Bond Commission authorizes these funds.

Capital and Non-Capital Improvement Funds

Total expenditures from capital and non-capital improvement funds were \$24,850,205, \$19,230,673, and \$22,068,175 for the fiscal years ended June 30, 2017, 2018, and 2019, respectively. The majority of these funds were for the Urban Act program. Urban Act program funds are authorized by the State Bond Commission for the purpose of redirecting, improving, and expanding state activities, which promote conservation and development, and improve the quality of life for urban residents of the state.

Connecticut Arts Endowment Trust Fund

The Connecticut Arts Endowment Fund operates under the provisions of Sections 10-406 through 10-408 of the General Statutes. This fund is financed from the proceeds of state bonds. The interest earnings for the current year become available for state matching grants to eligible arts organizations for the subsequent year. DECD provided arts organizations grants totaling \$377,340, \$792,033, and \$786,106, during the fiscal years ended June 30, 2017, 2018, and 2019, respectively. A summary of financial transactions for the audited period follows:

	As of June 30,		
	2017	2018	2019
Book Value, beginning of year	\$15,820,619	\$15,673,373	\$16,864,080
Shares Purchased	778,021	15,646,298	6,512,574
Shares Redeemed	(1,166,365)	(16,410,091)	(7,293,210)
Gains/(Loss) on Shares Redeemed	241,098	1,954,500	941,559
Net Investment Income Earned	9,011	8,631	5,473
Net Investment Income Distributed	(9,011)	(8,631)	(5,473)
Book Value, end of the year	\$15,673,373	\$16,864,080	\$17,025,003

The fair market value of trust fund assets as of June 30, 2019, was \$20,258,637.

Other Reviews

Section 32-1m of the General Statutes provides that, not later than February 1st annually, the Commissioner of Economic and Community Development shall submit a report that includes information regarding the activities of DECD, and business assistance or incentive programs not administered by the department, during the preceding state fiscal year

Section 2-90c of the General Statutes requires the Auditors of Public Accounts to evaluate DECD annual reports, including:

1. A determination of whether evidence is available to support the accuracy of the data presented in such annual report;
2. An evaluation of management practices and operations regarding the ease or difficulty for taxpayers to comply with the requirements of the incentive programs;

3. Recommendations for improving the administrative efficiency or effectiveness of the incentive programs; and
4. An evaluation of whether such annual reports satisfy the reporting requirements under subsection (a) of Section 32-1m of the General Statutes.

On October 22, 2020, our office completed an [evaluation](#) of the DECD 2018 and 2019 annual reports. Our review focused on determining whether data presented in the annual report appeared accurate and whether the annual report satisfied the reporting requirements under Section 32-1m of the General Statutes. We reviewed the remaining requirements in a separate [performance audit](#), which our office issued on May 21, 2019.

STATE AUDITORS' FINDINGS AND RECOMMENDATIONS

Our examination of the records of the Department of Economic and Community Development disclosed the following 26 recommendations, of which 17 have been repeated from the previous audit:

Excess Film Tax Credits

Criteria: Section 12-217ll of the General Statutes provides that DECD shall administer a system of tax credit vouchers for digital animation companies undertaking digital animation production activity in the state. Any digital animation production company receiving a tax credit pursuant to this section shall not be eligible for or receive a tax credit pursuant to section 12-217jj. Any state-certified digital animation production company incurring production expenses or costs of more than \$1 million shall be eligible for a credit equal to 30 percent of such expenses or costs. The aggregate amount of all tax credits which may be reserved by the department pursuant to this section shall not exceed \$15 million in any one fiscal year.

Section 12-217jj of the General Statutes provides that DECD shall administer a system of tax credit vouchers for eligible film production companies producing a state-certified qualified production in the state. Any eligible film production company incurring production expenses or costs of more than \$1 million shall be eligible for a credit equal to 30 percent of such expenses or costs.

Condition: DECD issued the \$15 million maximum annual tax credits to a company under the digital animation tax credit program through the fiscal year ended June 30, 2016. This company is the only recipient of credits under the program. In July 2016, DECD allowed the company to start receiving film production tax credits rather than digital animation tax credits. Since the General Assembly established a separate program for digital animation companies, it does not appear that it intended for digital animation companies to be eligible for film production tax credits.

Context: DECD issued the company \$94,410,602 of film production tax credits for fiscal years ended June 30, 2016 through 2019.

Effect: DECD issued \$49,410,602 more in film production tax credits to the company through the fiscal year ended June 30, 2019 than it would have been entitled to under the digital animation tax credit program.

Cause: The company requested Urban and Industrial Site Reinvestment (URA) tax credits. Rather than giving the company URA tax credits, DECD allowed it

to participate in the film production tax credit program, which does not have an annual cap.

Prior Audit Finding: This finding has not been previously reported.

Recommendation: The Department of Economic and Community Development should ensure that digital animation companies do not receive more than \$15 million in tax credits in any one fiscal year as required by Section 12-217ll of the General Statutes.

Agency Response: “DECD disagrees with this finding. A digital animation production company is eligible for film production tax credit under Section 12-217jj of the Connecticut general statutes. The company produces motion pictures, which is a statutorily qualified medium, also the company’s productions are further qualified as defined in 12-217jj (3)(A) of the statutes, which includes a, “production via any means and media in any digital media format, film or videotape”. DECD will seek clarification from the State Legislature.”

Auditors’ Concluding Comments:

The General Assembly established the digital animation tax credit program in 2007 by Public Act 07-236, a year after the creation of the film production tax credit program. Therefore, it does not appear that the General Assembly intended for digital animation companies to be eligible for film production tax credits. In addition, if the digital animation company was eligible for film production tax credits, it is unclear why DECD did not award film production tax credits for the first 7 years that the company received credits.

Excess Manufacturing Assistance Act Funding

Criteria: Section 32-462(b)(1) of the General Statutes provides that no agency may award more than a total of \$10 million of financial assistance during any 2-year period to an applicant or for a business project unless such financial assistance is specifically authorized by the General Assembly.

Section 32-4l of the General Statutes provides that DECD establish a First Five Plus program to encourage business expansion and job creation. A business development project eligible for financial assistance shall commit to create not less than 200 new jobs within 24 months or invest at least \$25 million and create not less than 200 new jobs no later than 5 years after the date such application is approved. Financial assistance for the First Five Plus program is exempt from the provisions of Section 32-462 of the General Statutes.

Condition: DECD awarded \$11.5 million in assistance to a First Five Plus company to create 200 jobs in 5 years. Since the company was not required to create the jobs in 24 months, it should have been required to invest at least \$25

million. However, the budget only called for the company to invest \$13.5 million of the total project cost of \$25 million. Without investing at least \$25 million, it appears the company did not qualify as a First Five Plus recipient and should not have been awarded more than \$10 million in assistance.

Context: During the fiscal years ended June 30, 2017, 2018, and 2019, DECD awarded funding for 89 Manufacturing Assistance Act projects consisting of \$96,900,550 in grants and \$295,808,750 in loans.

Effect: DECD awarded \$1,500,000 more in financial assistance than permitted under the General Statutes.

Cause: DECD maintained that since the total project cost was \$25 million that it qualified for First Five Plus.

Prior Audit Finding: This finding has been previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.

Recommendation: The Department of Economic and Community Development should ensure that the amount of financial assistance it provides to a business is not greater than amounts allowed under the General Statutes without obtaining authorization from the General Assembly. (See Recommendation 2.)

Agency Response: “DECD disagrees with this finding based on Section 32-4I of the Connecticut General Statutes. The total project cost of \$25,000,000 (inclusive of the state’s \$11,500,000 investment), meets the second category of eligibility criteria in the First Five statute: “that a business development project eligible for financial assistance shall invest at least \$25,000,000 and create not less than 200 new jobs no later than 5 years from the date the application is approved.” DECD funded this project based on Section 32-4I of the Connecticut General Statutes, however, DECD will seek to obtain additional legal interpretation on whether a company that qualifies for the First Five Plus program and will create not less than 200 new jobs no later than five years after the date the application is approved shall be required to invest at least \$25 million of non-State funds.”

Auditors’ Concluding

Comments: Based on the department’s interpretation, since the First Five Plus program waives the maximum percentage of a project that the department can finance, DECD could fund the entire project and the company would not be required to invest any funds. We note that the DECD First Five Plus Report stated that a company needs to invest \$25 million, not that the total investment must be \$25 million, which contradicts the department’s argument in its response to this finding. DECD should seek a formal opinion

from the Office of the Attorney General on this question, or request that the General Assembly to clarify the statute.

Loans Amended to Change Loan Forgiveness Requirements

Criteria:

Section 32-1c (b) of the General Statutes allows DECD to provide financial assistance to organizations for planning and other functions pertinent to economic development. The commissioner and the organization receiving financial assistance shall enter into a contractual arrangement in accordance with its respective needs.

For projects greater than \$500,000, DECD conducts an economic impact analysis using statistical models to quantify the impact of the proposed project on a city, a region, and the state. The economic impact analysis helps DECD determine the economic development need of a project and its return on investment, to justify the investment of public dollars.

Assistance agreements between DECD and recipients of funding include job creation and retention requirements, the specific period used to determine compliance with the employment obligation, and the deadline for completing and submitting a job audit to the state. In addition, the assistance agreements state whether recipients will be assessed any penalties or awarded loan forgiveness due to the business meeting job creation requirements.

Section 32-701 of the General Statutes provides that if a recipient of state assistance exceeding \$1 million fails to create or retain the number of jobs stipulated in the assistance agreement, due to circumstances within its control, the recipient shall repay an amount in proportion to the number of jobs that it failed to create or retain. This is not required if the awarding authority deems it is in the best interests of the state or the host community to revise such job creation goals. The awarding authority, at its discretion, may modify the terms and conditions of any state assistance, including, but not limited to, forgiveness of a loan repayment, revision of job creation and retention goals, or changes to interest rates, provided the awarding authority notifies the State Bond Commission or the appropriate board of directors of the modification.

While Section 32-701 of the General Statutes only applies to financial assistance over \$1 million, good business practice provides that prior to amending an assistance agreement, DECD should ensure that changes would result in an economic benefit to the state.

Condition:

Our review disclosed that DECD amended the assistance agreements with 4 companies to change the original job creation requirements. DECD did

not document whether changes would result in an economic benefit to the state.

- For one project, the original assistance agreement provided that DECD would forgive \$1 million of a \$2.5 million loan if the company created and retained 63 jobs by December 31, 2015. In addition, if the company created an additional 27 jobs by December 31, 2017, DECD would forgive the remaining \$1.5 million of the loan. However, in 2018 DECD signed an amendment with the company to allow for the inclusion of its parent company's employees. Under the amended agreement, DECD would forgive the remaining \$1.5 million of the loan if they retained 557 jobs. However, DECD could not provide any documentation to show the original number of the parent company's employees. As a result, we could not determine if the amendment still required job creation as a condition of the loan forgiveness. DECD did not conduct an updated economic impact analysis to determine whether it was in the best interests of the state or the host community to revise such job goals. In addition, DECD did not notify the State Bond Commission of the change.
- For one project, the original assistance agreement required the company to retain 17 positions and create 2 and did not include a provision for loan forgiveness. DECD modified the assistance agreement to allow the department to forgive the company's loan if it retained 16 jobs. DECD ultimately forgave \$81,719 of the loan.
- For one project, the original assistance agreement provided that DECD would forgive \$50,000 of the loan if the company created 4 jobs. If less than 4 jobs were created, DECD would apply a 1% interest rate penalty to the loan. DECD modified the assistance agreement to allow prorated forgiveness for the creation of 3 jobs. As a result, DECD forgave \$37,500 of the loan and did not apply the interest rate penalty.
- For one project, the original assistance agreement required the company to retain 20 jobs through 2008 and did not include a loan forgiveness provision. In 2018, DECD modified the assistance agreement to allow the company to receive loan forgiveness if it retained 11 positions. DECD ultimately forgave \$100,000 of the loan.

Context: During the fiscal years ended June 30, 2017, 2018, and 2019, DECD granted \$97,028,668 in loan forgiveness.

Effect: DECD granted \$1,719,219 of loan forgiveness that the companies would not have been entitled to under the original assistance agreements. In 2 cases, the changes allowed the companies to receive loan forgiveness for reducing their workforce.

- Cause:* DECD amended or modified the assistance agreements because the companies could not repay the outstanding loan balances or meet the loan forgiveness requirements.
- Prior audit finding:* This finding has been previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.
- Recommendation:* The Department of Economic and Community Development should ensure that amendments or modifications to assistance agreements would result in an economic benefit to the state and should notify the State Bond Commission of these changes when applicable. In addition, the department should document its reason for amending or modifying assistance agreements. (See Recommendation 3.)
- Agency Response:* “DECD disagrees with the first condition in this finding. The Company created 63 jobs and retained the jobs to earn their first tranche of forgiveness. The Company subsequently merged with another company and proposed to DECD that the 63 jobs should be counted as new jobs, as the resulting entity after the merger was a new entity and the jobs are new to the entity. This request was denied by DECD and DECD proceeded to negotiate a new forgiveness amendment to the contract based on the number of employees the surviving new entity had at the time of the original contract to ensure that the 90 jobs total that were to be created would remain in the amended agreement. DECD agrees that it did not conduct an updated economic impact analysis and did not notify the State Bond Commission of the change.
- DECD disagrees with the second condition in this finding. The Company in question had 2 loans with DECD, one in 1999 and a second one in 2002. The 1999 loan was modified 7 times and the 2002 loan was modified 5 times to help the company survive as a going concern. The Company repaid DECD approximately \$500,000 on the \$350,000 loan and approximately \$214,000 on the \$200,000 loan. Accordingly, DECD made the decision to provide the company with a loan forgiveness conditioned on the company retaining the jobs.
- DECD disagrees with the third condition in this finding. The Company was a financially struggling company and DECD made the decision to grant the company a partial forgiveness of the loan to avoid entering another modification with the company. DECD agrees that an interest rate penalty was not applied, which would have resulted in a repayment plan that the company could not afford.
- DECD disagrees with the fourth condition in this finding. This was a company that had appeared to be close to going out of business, therefore, a \$100,000 loan forgiveness was provided to the company. The Company

is now current with its loan repayments and the interest rate was increased for not creating the original jobs.”

Auditors’ Concluding

Comments:

For the first condition, DECD could not provide any documentation to show the original number of the parent company’s employees. As a result, we could not determine if the amendment still required job creation as a condition of the loan forgiveness.

For the other conditions, in two cases, the changes allowed the companies to receive loan forgiveness despite reducing their workforce. It appears DECD amended or modified these assistance agreements solely to forgive likely uncollectible amounts. This practice may violate Section 3-7(b) of the General Statutes which provides that the Secretary of the Office of Policy and Management must approve the cancellation of any uncollectible claim for an amount greater than \$1,000.

Inadequate Financial Review Process

Criteria:

The DECD Development Manager’s Client Service Manual documents various procedures for the entire business assistance process. This includes identifying information that companies should provide and various forms and guidelines for completion. Prior to approving an application, the Office of Financial Review performs a full review to uncover crucial facts about a company and to assure that DECD makes a knowledgeable financial assistance decision.

Financial reviews may include the following:

- Background investigations of the company, its officers and directors, and affiliated organizations.
- Reviews of legal and functional organization structures.
- Reviews of financial statements, business development plans, projects, and related assumptions.

Condition:

Our examination of financial reviews for 25 projects, for which DECD provided \$129,659,000 in financial economic development assistance, disclosed the following:

- DECD did not perform a financial review for 4 First Five Plus, 2 Brownfield, and one Manufacturing Assistance Act projects totaling \$97 million.
- DECD did not verify whether 4 companies that received \$23.2 million in assistance had pending litigation.

- DECD did not determine whether one company that received \$22 million in assistance owed outstanding taxes to the Department of Revenue Services.

Context: During the fiscal years ended June 30, 2017, 2018, and 2019, DECD awarded funding for 634 Manufacturing Assistance Act (including First Five Plus), Small Business Express, and Brownfield projects consisting of \$563,594,266 in financial assistance.

Effect: Without performing a comprehensive financial review or following up on concerns identified, there is increased risk that a company will default on its loans, improperly use state funds, or will be unable to successfully complete the proposed project and create or retain jobs.

Cause: DECD does not require financial reviews for First Five Plus projects. In addition, DECD relied on the Department of Housing’s review for one Brownfield project but did not obtain a copy of the review. We were unable to determine why DECD did not complete financial reviews for the other projects.

DECD informed us that the project manager addresses concerns noted during the financial review process, or the Letter of Intent (LOI) Committee discusses them when it reviews the proposed financial assistance. Since the LOI Committee does not keep meeting minutes, there is no documentation available to determine whether the committee adequately addressed the concerns.

Prior Audit Finding: This finding has been previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.

Recommendation: The Department of Economic and Community Development should conduct financial reviews for all of its funding in the First Five, Brownfield, and Manufacturing Assistance Act programs. In addition, the department should clearly document that any financial review concerns have been sufficiently resolved. (See Recommendation 4.)

Agency Response: “DECD agrees that a financial review was not conducted for 2 Brownfield projects, 4 First Five projects and 1 Manufacturing Assistance Act project. A financial review for one of the two Brownfield projects was conducted by the Department of Housing (DOH) and DECD included a copy of the review in the file. DECD will conduct a financial review for Brownfield projects and a financial/project review for other financial assistance requests submitted to DECD. For projects that may receive DOH/CHFA funding, DECD will be relying on the underwriting performed by DOH/CHFA and a copy of the financial review will be included in the project file.

DECD agrees with conditions two and three of this finding. DECD will implement the necessary internal control procedures to assure that a tax check and litigation check is performed for companies and entities seeking financial assistance through DECD.”

Inadequate Program Monitoring

Criteria:

The DECD Development Manager’s Client Service Manual documents procedures for the entire business assistance process including construction monitoring. Construction monitoring covers the development phases of projects from pre-bid activities through contract administration. Upon completion of the project, DECD completes a closeout checklist to ensure that the recipient has complied with contract requirements, completed the project, and used funds properly. In the event that these documents demonstrate that the applicant’s actual project expenditures are less than the maximum allowable amounts for state disbursement, any excess disbursement shall become immediately due and payable to the state by the applicant.

The DECD Office of Brownfield Remediation and Development Standard Operating Procedures Manual requires the department to review and score the program’s applications. DECD uses the rating and ranking scores to determine which projects to fund.

For projects greater than \$500,000, DECD conducts an economic impact analysis using statistical models to quantify the impact of the proposed project on the city or town, region, and the state. The economic impact analysis helps DECD determine the economic development need of a project and its return on investment, to justify the spending of public dollars.

DECD and the company enter into an assistance agreement which stipulates the terms and conditions of the assistance including the documents the recipient must submit. They include project administration plans, and periodic reports such as federal and/or state single audits, financial statements, and milestone and progress reports. The documentation varies for each assistance agreement.

Condition:

A review of 9 Manufacturing Assistance Act (MAA), 6 Brownfield, 12 Small Business Express (EXP), and 6 Urban Act project files identified the following deficiencies:

- DECD did not have an application on hand for one Urban Act project.
- DECD did not have a rating and ranking score on file for 3 Brownfield projects.

- DECD did not conduct an economic impact analysis for one \$750,000 Manufacturing Assistance Act project.
- DECD did not include a budget period for one Small Business Express project.
- DECD did not obtain a project administration plan for 2 Urban Act projects.
- DECD did not obtain a state single audit for one Urban Act project.
- DECD did not obtain annual financial statements for one Urban Act project.
- DECD did not obtain semi-annual project financial statements for one Brownfield and one Urban Act project.
- DECD did not obtain project milestone and progress reports for 2 Brownfield projects.
- DECD did not obtain a copy of the report the recipient filed with the federal Security and Exchange Commission and a report on the annual amount of full-time positions created or retained as a result of the project as required by the assistance agreement for one Manufacturing Assistance Act project.
- DECD did not document onsite monitoring for 2 Brownfield projects. In addition, onsite monitoring that was performed for 2 Urban Act projects did not contain sufficient photos to determine whether all aspects of the project were completed.

A review of 20 project closeouts identified the following.

- DECD did not close out 8 projects in a timely manner. It took one to four years for the department to close out the projects.
- DECD lacked supporting documentation for the closeout of 5 projects.
 - The Connecticut Environmental Policy Act compliance document was not on hand for one project.
 - Documentation to support an approved procurement process was not on hand for one project.
 - A final statement of program cost was not on hand for one project.
 - A final construction closeout document was not on hand for 3 projects.
 - A final site visit report was not on hand for 4 projects.
 - A certificate of occupancy was not on hand for one project.

Context:

During the fiscal years ended June 30, 2017, 2018, and 2019, DECD expended \$367,880,372 for MAA projects, \$100,183,914 for Brownfield projects, \$86,139,594 for EXP projects, and \$66,062,598 for Urban Act projects.

Effect:

There is increased risk that DECD may not identify and recover excess disbursements in a timely manner. In addition, DECD may make

inappropriate payments if it does not obtain and review periodic reports when required.

Cause: Administrative controls over the projects were inadequate. DECD informed us that due to staffing constraints and task priorities, it could not complete these tasks in a timely manner. In addition, DECD misfiled or did not receive the required documents. In one case, the department prematurely destroyed the closeout documentation.

Prior Audit Finding: This finding has been previously reported in the last 3 audit reports covering the fiscal years ended June 30, 2011 to 2016.

Recommendation: The Department of Economic and Community Development should ensure that it performs a complete review of all projects from application until financial closeout. (See Recommendation 5.)

Agency Response: “DECD agrees with this finding. DECD has implemented a contract tracking and project management database that will manage all active projects for compliance with applicable regulatory and statutory requirements.”

Improper Project Payment

Criteria: The Department of Economic and Community Development provides funding for Urban Act projects on a reimbursement basis. Recipients submit request for payments, which the department reviews for accuracy. Proper internal controls include ensuring the amount paid agrees with amounts in the payment requisitions and supporting documentation.

Condition: A review of 6 Urban Act project files identified that DECD overpaid a request for payment by \$264,996 for one Urban Act project.

Context: During the fiscal years ended June 30, 2017, 2018, and 2019, DECD expended \$66,062,598 for Urban Act projects.

Effect: DECD improperly advanced \$264,996 for a project.

Cause: Administrative controls over project payments were inadequate. DECD paid the amount on a previous payment request instead of the amount on the current payment request.

Prior Audit Finding: This finding has been previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.

Recommendation: The Department of Economic and Community Development should ensure that it only pays for eligible project costs. (See Recommendation 6.)

Agency Response: “DECD agrees with the finding; The client has agreed to return ineligible expenses and will forward invoices for eligible expenses to be reconciled to the next request for payment.”

Improper Loan Setup

Background: Section 32-1c (b) of the General Statutes allows DECD to provide financial assistance to organizations for planning and other functions pertinent to economic development. The commissioner and the organization receiving financial assistance shall enter a contractual arrangement for this purpose.

DECD assistance agreements and promissory notes with recipients stipulate the terms and conditions of the assistance, including any interest or penalties that could be assessed. The department enters executed loans into its loan management system, which automatically generates monthly invoices detailing principal and interest amounts due.

If a company is delinquent on a loan or is unable to make the required payments, DECD may modify the loan to defer interest or principal payments or extend the terms of the loan to reduce monthly payments. DECD issues the recipient a modification letter, which outlines the terms of the modification.

Criteria: The State Accounting Manual establishes policies and procedures for all state agencies in the management of receivables. Accounts receivable records, including loans receivable, should be accurate, complete, and maintained in a manner to indicate the length of time the debt has been outstanding. Each state agency is responsible to immediately notify the person or entity that money is owed and to collect amounts owed to the state in the most effective and efficient manner.

Good business practice dictates that agencies record loans receivable and bill borrowers in a timely manner in accordance with agreed-upon contractual arrangements.

Condition: Our review of 9 Manufacturing Assistance Act, 4 Brownfield, and 12 Small Business Express loan projects disclosed the following:

- For 6 loans, DECD did not input advances into the loan management system in a timely manner. We noted 7 loan advances that DECD did not input into the system until 1 to 3 months after it made the payments. As the result of the delay, DECD did not promptly bill for principal and interest payments for 2 loans.
- DECD did not input \$5,117,000 of loan forgiveness into the loan management system for one loan.

- The promissory note for a \$3 million loan called for payments for half of the loan to begin in 2019 and end in 2036, and for the other half to be paid on the maturity date in 2036. However, the loan repayment schedule provided for payments beginning in 2031 and continuing until 2056.

We also noted the following errors for loans outside our sample.

- The promissory note for a \$9 million loan called for equal monthly payments with a 20-year amortization schedule and a balloon payment due in 10 years. However, the loan repayment schedule provided for equal monthly payments over 10 years.
- The promissory note for a \$1.75 million loan called for equal monthly payments with a 50-year amortization schedule. The payments would be made for 17 years, after a 3-year deferral period, with a balloon payment due in 20 years. However, the loan repayment schedule provided for equal monthly payments over 17 years.
- One loan modification letter called for reduced payments through September 2018 and required DECD to reevaluate the company's financial position in August 2018. However, DECD deferred loan payments in its loan management system after September 2018 until the September 2023 maturity date. The company should have resumed its regular payments after September 2018.
- One loan modification letter called for reduced payments through September 2018 and required DECD to reevaluate the company's financial position in August 2018. However, DECD deferred payments in its loan management system after September 2018 until the April 2024 maturity date. The company should have resumed regular payments after September 2018.
- One loan modification letter called for reduced payments through February 2019 and required DECD to reevaluate the company's financial position in January 2019. However, DECD deferred payments in its loan management system after February 2019 until the January 2023 maturity date. Regular payments should have resumed after February 2019 barring another loan modification.

Context:

DECD made loan advances to 63 Manufacturing Assistance Act, 35 Brownfield, and 299 Small Business Express loans during the fiscal years ended June 30, 2017, 2018, and 2019. As of January 2020, DECD had modified 104 loans.

Effect:

The department's ability to track and bill for loans is impaired if it does not input advances and forgiveness in its loan system in a timely manner. In some cases, the delay resulted in DECD improperly billing companies for late fees that the department had to reverse. In addition, there is reduced assurance that DECD recorded all loans receivable.

Repayment for 4 loans will start 4 to 12 years later than stipulated in the promissory note or modification letters. As a result, DECD will not collect principal and interest amounts due, which increases the risk that amounts could become uncollectible if the borrower encounters financial difficulties. In addition, DECD overcharged 2 companies for monthly principal payments.

Cause: DECD did not ensure that it input loan advances or forgiveness into its loan system in a timely manner. In addition, errors were due to the incorrect setup of the loan terms. In one case, it appears that DECD inadvertently used a Department of Housing promissory note to setup the loan.

Prior Audit Finding: This finding has been previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.

Recommendation: The Department of Economic and Community Development should enter advances or forgiveness into the loan management system in a timely manner and should ensure that it sets up loans in accordance with the repayment terms of the promissory notes or loan modification letters. (See Recommendation 7.)

Agency Response: “DECD partially agrees with this finding. Most of the loans referenced in the finding were setup timely based on the billing cycle as specified in the promissory notes. In FYE 2018, DECD implemented a loan tracking and reconciliation process that facilitates a timely loan setup and billing functionality. A multi-level loan review process was implemented, which includes a loan review checklist, a supervisory review of the intended interest calculation terms, any modification/forbearances terms of the loan and any forgiveness in accordance with the promissory note of the loan.”

Inadequate Controls over Job Audits

Criteria: Assistance agreements between DECD and recipients of funding include job creation and retention requirements, the specific period used to determine compliance with the employment obligation, and the deadline for completing and submitting a job audit to the state. In addition, the assistance agreement will state whether recipients will be assessed any penalties or awarded loan forgiveness related to job creation requirements. Once DECD completes a job review, it issues a letter to the recipient outlining the results. If a recipient fails to perform any act, duty, or obligation in the assistance agreement, it shall constitute a default of the agreement.

Assistance agreements between DECD and recipients of Small Business Express (EXP) funding state that following the end of the employment

obligation, the applicant will receive a job review package from the state, which must be completed and submitted within 30 days. DECD uses information from the Department of Labor (DOL) to verify the accuracy of information in the job review package.

Most assistance agreements between DECD and recipients of Manufacturing Assistance Act (MAA) funds provide that each applicant shall furnish to DECD by the deadline specified in the assistance agreement, a job audit performed by a certified public accountant (CPA) in accordance with the DECD Audit Guide. If a job audit by a CPA is not required, the recipient will receive a job review package from the state, which must be completed and submitted within 30 days.

Condition: A review of 10 EXP, 9 MAA, and 1 Urban Act job audits identified the following:

- DECD did not promptly review job audits for 10 EXP projects and one MAA project. DECD did not complete the desk reviews until 14 to 56 months after the due dates in the assistance agreements.
- DECD did not receive job review packages for 6 EXP and 2 MAA projects. As a result, DECD used Department of Labor data to approximate the number of the company's jobs. However, DOL data does not indicate how many hours employees work and does not account for turnover.
- DECD did not have the job audit review on file for one MAA project.
- DECD accepted job review packages for 2 projects that used incorrect employment obligation periods.
- DECD incorrectly calculated the number of jobs retained for one EXP and one MAA project.
- As the result of the job review, DECD should have increased the interest rate of the recipient's loan by 1%. However, DECD did not apply the increase in its loan management system.

Context: During the fiscal years ended June 30, 2017, 2018, and 2019, DECD completed 756 EXP and 71 MAA and Urban Act job audits.

Effect: DECD may not be properly calculating or promptly applying employment obligation penalties. Our review noted that DECD did not assess a company a \$21,500 penalty and overcharged another company 0.1% in interest. We also noted that DECD did not charge a company an extra 1% of interest for 3 years because the department did not complete the desk review in a timely manner. In addition, there is reduced assurance that recipients actually complied with their employment obligations.

Cause: Administrative controls over job audits are inadequate. DECD informed us that, due to staffing constraints and other priorities, it could not complete

these tasks in a timely manner. In addition, DECD did not hold companies that failed to submit job review packages in default of their assistance agreements.

Prior Audit Finding: This finding has been previously reported in the last 2 audit reports covering the fiscal years ended June 30, 2013 to 2016.

Recommendation: The Department of Economic and Community Development should ensure that it receives and reviews recipient job audits in a timely manner. In addition, the department should promptly and correctly apply penalties or loan forgiveness that results from those reviews. (See Recommendation 8.)

Agency Response: “DECD agrees that some job audits are not done in a timely manner. DECD has implemented an email notification system to notify companies when their job audit is due and their delinquency if the audits are not submitted. However, not all companies have responded. As an alternative to a company’s nonresponse, DECD will obtain the company’s employee information as reported to the Department of Labor (DOL). This slows the process of a timely job audit review and results in some job audits determined as noncompliant.”

Inadequate Controls over Relocated Businesses

Criteria: Section 32-5a of the General Statutes provides that the DECD commissioner shall require, as a condition of any financial assistance provided, that such business organization shall not relocate out of state for 10 years after receiving such assistance or during the term of a loan or loan guarantee, whichever is longer, unless the full amount of the assistance is repaid to the state and a penalty equal to 5% of the total assistance received is paid to the state.

Condition: During the prior audit, we noted that DECD did not consistently apply relocation requirements to tax credits. Our review of 5 Urban and Industrial Site Reinvestment tax credits disclosed that the department did not require two companies to repay the credits when they relocated out of state. DECD awarded \$2,725,518 of the \$27,255,184 approved tax credits for these projects.

DECD does not adequately track whether companies that received financial assistance remain in the state during the relocation period.

Effect: If the companies left during the relocation period, the state would not be able to recoup the tax credits it provided to the companies. Without adequate tracking procedures, a company could relocate out of state without repaying its financial assistance and paying a penalty.

Cause: DECD does not consistently apply relocation requirements to tax credits. Our review of DECD assistance agreements disclosed that the department required some relocated companies to repay all tax credits and a penalty, only required others to pay a penalty, and did not require others to repay either.

Prior Audit Finding: This finding has been previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.

Recommendation: The Department of Economic and Community Development should ensure that it requires companies to repay all forms of financial assistance if they relocate out of state within the relocation period, and should implement adequate procedures to determine whether companies have relocated out of state. (See Recommendation 9.)

Agency Response: “DECD agrees with this finding. The agency has implemented the necessary internal control procedures to adequately track whether all companies that received financial assistance remain in the State during the relocation period.”

Lack of Monitoring over Grant Awards for Equipment

Background: DECD received a federal Department of Defense grant award through the Office of Economic Adjustment establishing the Regional Aerospace and Defense Exchange Phase 2 (RADE) Program in September 2014. The grant supported activities to strengthen the capability and resilience of the defense supply chain in Connecticut. DECD entered into an assistance agreement with a grantee to administer a portion of the program.

DECD entered into another assistance agreement with the grantee to enhance the state’s manufacturing workforce and industry. The grant recipient used these funds to purchase a milling machine. The grantee would own the equipment and be responsible for marketing to and contracting with Connecticut manufacturers to perform composite projects.

Criteria: The economic adjustment activities approved in the RADE award included the purchase of equipment to provide support exclusively and free of charge to defense industry manufacturing firms. The grant recipient used RADE funds to purchase 3D and X-Ray scanners. The grantee assistance agreement provided that all equipment purchased would be located at and operated by the grantee but would belong to DECD.

Good business practice provides that prior to the end of an assistance agreement with a grant recipient, an agency should establish a sustainability plan that would outline the use or disposal of equipment after the expiration of the agreement.

The RADE program assistance agreement required the recipient to submit monthly reports summarizing program progress and all supplier projects. In addition, the grantee was required to maintain an operation and maintenance log for the equipment.

The assistance agreement for the funds used to purchase the milling machine provided that the grantee shall not relocate any of its operations outside the state for 10 years.

Good business practice provides that prior to awarding a grant to purchase equipment, the department should sufficiently gauge its demand. In addition, the grant award to purchase equipment should specify a minimum length of time the grant recipient must use or retain ownership of the asset.

Condition:

DECD hired a certified public accounting firm to conduct an audit of the grantee's usage of the RADE-funded equipment. The audit found that the grantee used the equipment for unauthorized non-aerospace/defense customers without DECD approval. DECD issued a letter to the grantee ordering it to cease and desist using the equipment. The letter stated that DECD would withhold future funding if the grantee did not meet certain remedy requirements. Among these requirements was the submission of quarterly reports on the machine hours utilized for each project. As of our review in July 2019, the grantee had yet to provide DECD with any quarterly reports. However, DECD continued making payments to the grantee.

Our review of the grantee's monthly reports on the cumulative usage of the RADE-funded equipment disclosed that the reports were inconsistent and unsupported. In addition, the grantee did not maintain an adequate operation and maintenance log for the equipment.

DECD did not establish a sustainability plan for the use of the RADE-funded equipment prior to the expiration of the grantee's assistance agreement. The grantee maintained the equipment at its facilities after the end of the grant award.

As of April 2019, the grantee had only used the milling machine, which was installed in October 2017, for one project. The limited use of the equipment does not appear to justify its cost. In addition, while DECD required the grantee not to relocate its business outside of the state for 10 years, the agreement did not include any restrictions regarding the length of time that the grantee needed to use or retain ownership of the equipment.

- Context:* The grant recipient used \$444,935 of RADE funding to purchase a 3D scanner and \$449,867 to purchase an X-Ray scanner. In addition, DECD awarded \$2.9 million to a grantee to purchase a milling machine.
- Effect:* As of our review, DECD paid \$6,533,109 to the grantee under various assistance agreements despite it not fulfilling the requirements in the remedy letter.
- Without accurate reports, DECD was unable to evaluate the number of hours that the grantee used the RADE-funded equipment. As a result, there is reduced assurance that all hours were for allowable projects.
- The grantee could stop using the milling machine for its intended purpose or sell the equipment without having to reimburse DECD.
- Cause:* DECD did not adequately monitor the grant recipient's usage and reporting of the RADE-funded equipment and did not enforce the requirements of its remedy letter. In addition, DECD did not sufficiently plan for the continued use of the equipment after the expiration of the grant award.
- DECD did not sufficiently gauge demand for the milling machine prior to awarding a grant for its purchase and did not require that the grantee use the equipment for a minimum period.
- Prior Audit Finding:* This finding has not been previously reported.
- Recommendation:* The Department of Economic and Community Development should adequately monitor grant recipients and should ensure that they comply with reporting requirements. In addition, the department should complete its due diligence and sufficiently gauge the demand for equipment prior to awarding a grant for its purchase and should ensure that the grantee uses the equipment for a sufficient period. (See Recommendation 10).
- Agency Response:* **“Reporting:** DECD agrees with this finding. DECD requested and received monthly reports on the usage, operation, and maintenance of the RADE equipment, however, the reports received were incomplete. DECD will implement and create a standard reporting format and review process specific for this program.
- Sustainability:** DECD agrees with this finding. DECD was unable to finalize the agency's draft sustainability plan until the Federal interest period and disposable policy was provided to DECD by the Federal granting agency. This information was not provided to DECD until after the expiration of the State contract with the State grant recipient. DECD will produce a written sustainability plan identifying usage and/or disposal of the RADE equipment.

Due Diligence: DECD agrees with this finding. In the future, DECD will perform additional due diligence to fully gauge demand for the equipment and its technology prior to finalizing assistance agreement and entering the contract phase.”

Inadequate Procedures over Tourism Funding

Background: There are three regional tourism districts in the State of Connecticut. DECD entered into a grant agreement for \$400,000 with each district during the fiscal year ended June 30, 2019.

DECD found that two regional tourism districts did not comply with their grant agreements. The department gave the districts the opportunity to address the issues of noncompliance. The districts failed to comply with their grant agreements because they did not:

- Return unexpended funds before the end date of the agreements.
- Spend funds in accordance with the approved budgets.
- Submit documents required by the grant agreements such as monthly marketing reports, a marketing plan, or a private fundraising plan.

Criteria: DECD’s grant agreements with the tourism districts stipulate the terms and conditions of the funding. The agreements included the following requirements:

- The districts must expend grant funds in accordance with the application budgets and within the period of the agreements, unless DECD approved a written change request before the end date of the agreements. The districts must return unexpended funds to DECD.
- The districts shall partner with a not-for-profit or governmental entity conducting tourism marketing for administrative purposes.
- The districts shall carry and maintain sufficient general liability insurance at all times during the term of the agreements. The policies shall name the state as an additional insured and the districts shall provide copies of the policies to DECD prior to the effective date of the agreements.
- The districts must utilize CTvisit.com as their official website.

Section 1-225 of the General Statutes requires the meetings of all public agencies to be available for public inspection and posted on the public agency’s website no later than 7 days after the meeting.

Condition: DECD did not provide funding to the districts that were in breach of its agreement in a timely manner. DECD funded one district 22 days before the end of the budget period and funded the other district 8 days before the end of the budget period.

Our review of one of the tourism districts disclosed the following:

- The district entered into a partnership agreement with an organization run by its chairman. Prior to entering into the agreement, the district did not have a full board of director's meeting to approve the agreement.
- DECD did not obtain a copy of the district's insurance policy before it disbursed funds. The district's insurance policy was not effective until October 1, 2019, which was after DECD disbursed the funds and the district spent them. In addition, the insurance policy did not list DECD as an additional insured.
- The district did not make the minutes of its board meeting publicly available on CTvisit.com within 7 days of the meeting.

Effect: The tourism districts had minimal time to spend their funds. DECD did not provide these districts with grant funds for the fiscal year ended June 30, 2020 until the districts corrected their compliance issues. As a result, they also had less than a month to spend their 2020 grants. In addition, by not adequately monitoring the tourism districts, DECD has limited assurance that they used funds for their intended purpose and complied with General Statutes and grant agreement requirements.

Cause: The state did not fund the tourism districts during the fiscal years ended June 30, 2017 or 2018. DECD delayed releasing the 2019 funding until after the new administration decided whether to continue funding the districts in future fiscal years.

DECD's monitoring of the tourism districts was limited. In addition, the grant agreements did not require the districts to submit a copy of its partnership agreements to DECD for approval.

Prior Audit Finding: This finding has not been previously reported.

Recommendation: The Department of Economic and Community Development should ensure it gives the regional tourism districts sufficient time to spend grant funds and should ensure that the districts comply with the General Statutes and requirements in grant agreements. In addition, the department should require the tourism districts to submit a copy of their board-approved partner agreements. (See Recommendation 11.)

Agency Response: "DECD partially agrees with this finding. The agency agrees that the events in three of the four conditions stated in this finding did occur, however, the agency offers the following insights on the conditions of the finding:

DECD agrees with the first condition that it did not provide funding to the districts that were in breach of its agreement in a timely manner. The actions were taken to stop/hold funding until the breach was cured. In both cases, that was done, funds were released after the breach was cured.

DECD agrees with the second condition that the district entered into a partnership agreement with an organization run by the district's chairman. The organization referred to in the condition was vetted by DECD and DECD concluded that it was not aware of any conditions or conflicts that would prevent the organization from serving as the Administrative Partner organization.

DECD agrees with the fourth condition in the finding that the district did not make the minutes of its board meeting publicly available and post it on CTvisit.com within 7 days of the meeting. However, the requirement is that the minutes should be sent to each Town and City within the respective districts. The Connecticut Office of Tourism's website; CTvisit.com, referred to, is a tourism marketing website, and has no capacity to accept such minutes and is not aware of any requirement to post the minutes on the website.

DECD disagrees with the stated "cause" of the finding with stated that; "DECD's monitoring of the tourism districts was limited. In addition, the grant agreements did not require the districts to submit a copy of its partnership agreements to DECD for approval." It is DECD's position that all the grant agreements were approved by the DECD Office of Tourism. In addition, DECD conducts monitoring of the tourism districts."

*Auditors' Concluding
Comments:*

The Freedom of Information Act requires public agencies to post meeting minutes to their website no later than seven days after the meeting. DECD's grant agreements with the tourism districts stipulate that the districts must utilize CTvisit.com as their official website. DECD should provide guidance to the tourism districts if they should use an alternate website to post meeting minutes.

While the DECD Office of Tourism approved the grant agreements, the agreements did not require the districts to submit a copy of its partnership agreements to DECD for approval. There was a new requirement for the tourism districts to enter into a tourism marketing partnership agreement with a not-for-profit or governmental entity for administrative purposes. The issue may have been avoided if the department had reviewed and approved these partnership agreements before it disbursed funds.

Additional Funding Provided to Delinquent Company

- Criteria:* The State Accounting Manual establishes policies and procedures for all state agencies in the management and collection of receivables. Accounts receivable records, including loans receivable, should be accurate, complete, and maintained in a manner to indicate the length of time the debt has been outstanding. When an account becomes 60 days past due, further credit should be denied until the account is returned to a current status. Deferred payment terms should be extended on a limited basis, only upon determining that the debtor is unable to pay the balance in full. The agency should not extend payment terms beyond 6 months. However, where large balances are concerned and payment of such balances within 6 months would create a hardship, terms can be extended for a few months more.
- Assistance agreements and promissory notes with recipients stipulate the terms and conditions of assistance provided including job creation and retention requirements. At the completion of the project, DECD performs a financial closeout to ensure that the recipient properly used the financial assistance and a job review to determine whether job requirements were met.
- Before any additional funding is provided to a borrower, the company should be current on payments for previous loans. In addition, DECD should ensure that it has performed all financial closeouts and job reviews on prior projects.
- Condition:* DECD provided a \$150,000 loan to a company that was delinquent on a previous DECD loan. The company never made a payment on its original 2012 loan. DECD modified the agreement in August 2016 to defer payments and forgive part of the loan. The modification also allowed DECD to forgive the remaining balance of the loan following a scheduled January 2018 job review. Prior to the job review, DECD awarded the company the second loan. The financial review performed for the company raised concerns regarding its ability to repay the loan.
- Context:* During the audited period, DECD provided additional assistance to 50 companies that had previously received funding.
- Effect:* There is increased risk that the borrower will default on loans and the state will be unable to recover its resources.
- Cause:* DECD deferred the borrower's original loan through a loan modification at the time it provided the additional assistance. As a result, DECD did not consider the loan delinquent.

Prior Audit Finding: This finding was previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.

Recommendation: The Department of Economic and Community Development should complete its due diligence before providing additional funding to a company, especially if the company is delinquent on past loans or has demonstrated an inability to create and retain jobs. As part of that due diligence, DECD should perform job reviews on older projects before funding new projects. (See Recommendation 12.)

Agency Response: “DECD disagrees with the finding. In 2016, DECD entered into an agreement with the Company in which the company’s performance would be used as a measure to grant the company a loan forgiveness. At the execution of the contract for the new loan in 2018, DECD determined that the Company was no longer delinquent on its loan with DECD and the loan was approved. The loan was provided to the company when the company was no longer delinquent with DECD.”

Auditors’ Concluding Comments:

DECD did not consider the loan delinquent at the time additional assistance was provided because the department modified the company’s original loan. The modification forgave the entire loan despite only requiring the company to retain 30 of its 38 full-time employees. Our last audit (covering the fiscal years ended June 30, 2015 and 2016) reported that DECD would forgive the company’s loan even if it eliminated positions.

Multiple Loan Deferments

Background: Section 32-1c (b) of the General Statutes allows DECD to provide financial assistance to organizations for planning and other functions pertinent to economic development. The commissioner and the organization receiving financial assistance shall enter into a contractual arrangement for this purpose.

In order to support the growth and innovation of Connecticut businesses, DECD administers a number of financing programs to assist businesses. DECD assistance agreements stipulate the terms and conditions of the assistance.

If a company is delinquent on a loan or is unable to make the required payments, DECD may modify the loan to defer interest or principal payments or extend the terms of the loan to reduce monthly payments.

Criteria: The State Accounting Manual establishes policies and procedures for all state agencies in the management and collection of receivables. Each state agency is responsible for the collection of amounts owed to the state in the

most effective and efficient manner. Deferred payment terms should be extended on a limited basis, only upon determining that the debtor is unable to pay the balance in full. Terms should not be extended beyond 6 months. However, terms can be extended an additional few months when large balances are due and payment within 6 months would create a hardship.

Condition: During our review, we noted 21 loans, totaling \$4,888,571, that DECD modified multiple times to defer principal and interest payments. These modifications resulted in DECD deferring principal and interest payments between 2 years and 4 years 8 months.

Context: As of January 2020, DECD had modified 78 loans more than once, 24 of which were modified at least 4 times.

Effect: When payments are deferred for extended periods, there is a reduced chance that loan funds are ever collected.

Cause: DECD has not established clear guidelines for when companies qualify for loan modifications and how long the department defers principal and interest payments.

Prior Audit Finding: This finding was previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.

Recommendation: The Department of Economic and Community Development should limit the time it defers loan payments and should establish clear guidelines for when borrowers should qualify for loan modifications. (See Recommendation 13.)

Agency Response: “DECD agrees with this finding that an increasing number of modifications may result in a diminish likelihood that the loans will be collected. Accordingly, DECD will implement new loan modification and forbearance guidelines that will provide a path to financial stability of companies within DECD’s portfolio and increase the likelihood that the State will collect on the loans in its portfolio.”

Inadequate Controls over URA Tax Credit Fees

Criteria: Section 32-9t creates an Urban and Industrial Site Reinvestment (URA) program under which taxpayers who invest in eligible urban reinvestment projects or eligible industrial site investment projects may be allowed a tax credit in an amount equal to their approved investment. Any taxpayer or fund manager, community development entity, or contractually bound community development entity wishing to make an investment under the provisions of this section shall apply to the commissioner. The commissioner can impose a fee for such application.

Assistance agreements between DECD and recipients of URA tax credits may specify a fee the applicant is required to pay with the submission of its annual certification.

Condition: A review of 5 companies that received URA tax credits disclosed the following:

- DECD did not collect a \$10,000 application fee before issuing a \$2 million tax credit to a company.
- DECD overcharged a company an \$18,000 application fee and a \$3,000 annual fee.

Context: During the fiscal years ended June 30, 2017, 2018, and 2019, DECD issued \$124,125,518 in URA tax credits.

Effect: DECD did not collect the proper amount of fees from recipients of URA tax credits.

Cause: DECD does not have an adequate process to track whether it has collected all fees prior to issuing tax credits. In addition, DECD required a company that previously applied for the program and paid the application fee to reapply and pay an additional fee. DECD's 2008 assistance agreement with the company stated that URA tax credits would not be available until the company delivered DECD written notice that legislation repealed or reduced the Digital Animation Production tax credit. In 2015, the company notified DECD that this legislative action occurred and requested URA tax credits. Since URA tax credits were included in the original assistance agreement, the company should not have had to reapply for the program and pay an additional application fee. In addition, under the original assistance agreement, the company was not required to pay an annual fee, but the second application required a \$3,000 annual fee.

Prior Audit Finding: This finding has not been previously reported.

Recommendation: The Department of Economic and Community Department should ensure that it collects the proper amount of application and annual fees for Urban and Industrial Site Reinvestment tax credits prior to their issuance. (See Recommendation 14.)

Agency Response: "DECD agrees with this finding. The agency will implement the appropriate corrective measures to provide reasonable assurance that the proper amount of fees will be collected from recipients of the URA tax credits."

Erroneous Loans Receivable Balances

- Criteria:* The State Accounting Manual establishes policies and procedures for all state agencies in the management and collection of receivables. Accounts receivable records, including loans receivable, should be accurate, complete, and maintained in a manner to indicate the length of time the debt has been outstanding.
- The Office of the State Comptroller requires all state agencies to report accurate accounts receivable balances as of June 30th including the amount of receivables that are estimated to be uncollectible. The State Comptroller includes reported amounts in the state's Comprehensive Annual Financial Report.
- Condition:* Our testing of DECD's reported receivable balances disclosed that the department overstated loans receivable by \$3,052,378 and \$4,167,873 for the fiscal years ended June 30, 2017 and 2018, respectively.
- In addition, DECD has not developed a sufficient method to estimate the amount of uncollectible receivables. DECD only reports receivables as uncollectible for borrowers that are out of business. We reviewed receivables as of June 30, 2019 and noted DECD did not include \$10.7 million of receivables that were delinquent over 2 years, and are likely uncollectible, in its estimate of uncollectible receivables.
- Context:* DECD reported loans receivable of \$552,185,716, \$623,647,809, and \$661,440,571 for the fiscal years ended June 30, 2017, 2018, and 2019, respectively.
- Effect:* DECD reported inaccurate amounts of loans receivable to the Office of the State Comptroller, and included receivables that are likely uncollectible.
- Cause:* Errors were due to clerical mistakes and oversights. In addition, DECD did not develop a sufficient method to estimate the amount of uncollectible receivables, and did not include receivables that their lending partners previously determined to be uncollectible.
- Prior Audit Finding:* This finding has been previously reported in the last 4 audit reports covering the fiscal years ended June 30, 2009 to 2016.
- Recommendation:* The Department of Economic and Community Development should strengthen its internal controls to ensure that the amount of loans receivable reported to the Office of the State Comptroller is accurate and includes estimated uncollectible receivables. (See Recommendation 15.)

Agency Response: “DECD agrees with this finding. For FY 19-20 the agency has implemented a process in which loan receivable amounts identified as doubtful collections are reported as uncollectible on loan receivable and GAAP reports to the Office of the State Comptroller.”

Incorrect Interest Calculation Method

Background: Section 32-1c (b) of the General Statutes allows DECD to provide financial assistance to organizations for planning and other functions pertinent to economic development. Financial assistance shall be rendered upon such contractual arrangements as may be agreed upon by the commissioner and any such organization for this purpose.

DECD assistance agreements and promissory notes with recipients stipulate the terms and conditions of the assistance, including any interest or penalties that could be assessed. The department enters executed loans into its loan management system, which automatically generates monthly invoices detailing principal and interest amounts due.

Each year, DECD reports its June 30th receivable balances to the State Comptroller, including loan interest and late fee receivables, based on reports from its loan management system. The State Comptroller includes reported amounts in the state’s Comprehensive Annual Financial Report.

Criteria: The State Accounting Manual establishes policies and procedures for all state agencies in the management and collection of receivables. Accounts receivable records, including records related to interest and penalties assessed against individuals and organizations, should be accurate, complete, and properly maintained.

Good business practice dictates that agencies accrue and bill interest to borrowers properly and in accordance with agreed-upon contractual arrangements.

Condition: During our previous audit, we noted that 68 loans were set up in the loan management system using an incorrect interest calculation method. We reviewed these loans as of January 9, 2020 and determined that 5 loans were still incorrect. The 5 loans that are still using the wrong interest calculation method total \$5 million.

In addition, we reviewed 10 reported receivables and noted that DECD incorrectly calculated the interest billed or capitalized for 3 loans during the tested fiscal year. DECD understated the interest billed or capitalized for 2 loans totaling \$228 and overstated one \$4,125 loan.

- Context:* DECD reported receivables for interest and late fees of \$5,589,171, \$7,348,753, and \$9,152,151, for the fiscal years ended June 30, 2017, 2018, and 2019, respectively.
- Effect:* DECD did not always calculate interest accruals in accordance with the terms of the assistance agreements. In addition, DECD reported inaccurate interest receivable amounts to the State Comptroller.
- Cause:* The differences noted were due to DECD incorrectly setting up the interest calculation terms in the loan management system.
- Prior Audit Finding:* This finding has been previously reported in the last 2 audit reports covering the fiscal years ended June 30, 2013 to 2016.
- Recommendation:* The Department of Economic and Community Development should ensure that loan interest is calculated and billed or capitalized in accordance with financial assistance agreements. (See Recommendation 16.)
- Agency Response:* “DECD agrees with the findings. The identified loans have been corrected. During 2018-19 DECD implemented measures to ensure accurate loans setups including a review checklist that ensures compliance with the terms of the promissory note and financial assistance agreement, supervisory review of setup and staff training.”

Untimely Recording of Bank Deposits

- Criteria:* The State Accounting Manual provides that agencies should complete the confirmation and journalizing of bank deposits by the end of the day that agencies receive the deposit information through the Core-CT system. Each agency is required to post deposits in Core-CT as soon as the confirmation process is complete or no later than four business days from the accounting date of the deposit. The four-day extension is intended solely for problematic deposits with bank issues that must be resolved. If there is not a bank issue, agencies should record deposits the same day that the deposit appears on its pick list.
- The State Accounting Manual provides that any receipt of money that cannot be posted to the correct funding source must be posted to funds awaiting distribution until the final disposition is determined. This fund allows agencies to comply with statutory depositing requirements.
- Condition:* Our review of 15 cash receipt transactions, totaling \$975,206, disclosed that DECD did not post 2 deposits, totaling \$606,676, in a timely manner. DECD posted the deposits 2 days late.

- Context:* DECD recorded \$53,827,959, \$86,728,002, and \$64,477,021 of deposits during the fiscal years ended June 30, 2017, 2018, and 2019, respectively.
- Effect:* DECD did not comply with requirements concerning the prompt posting of bank deposit information. This could have delayed the detection of bank deposit recording errors.
- Cause:* Administrative controls over deposits were inadequate. DECD could not determine the correct funding for the deposits and delayed posting them rather than posting them to funds awaiting distribution.
- Prior Audit Finding:* This finding has not been previously reported.
- Recommendation:* The Department of Economic and Community Development should post deposits in a timely manner. (See Recommendation 17.)
- Agency Response:* “DECD agrees with this finding. Based on the volume and complexities of the transactions that DECD processes, the agency will seek a waiver from the Office of State comptroller (OSC) regarding the State Accounting Manual requirement that agencies are required to post deposits in Core-CT as soon as the confirmation process is complete or no later than four business days from the accounting date of the deposit.”

Inadequate Cash Receipts Reconciliations

- Criteria:* Proper internal controls include performing monthly reconciliations to compare the amount recorded to the funds the agency should have accounted for. The agency should promptly identify and resolve any variances.
- Condition:* DECD did not properly reconcile total cash receipts to the amounts entered into Core-CT.
- Context:* DECD recorded \$53,827,959, \$86,728,002, and \$64,477,021 of deposits during the fiscal years ended June 30, 2017, 2018, and 2019, respectively.
- Effect:* There is increased risk that errors or irregularities may go undetected.
- Cause:* DECD only performs reconciliations for its loan programs. The department does not perform reconciliations for other types of cash receipts.
- Prior Audit Finding:* This finding has not been previously reported.
- Recommendation:* The Department of Economic and Community Development should prepare monthly reconciliations of all cash receipts. (See Recommendation 18.)

Agency Response: “DECD agrees with the recommendation. DECD has taken measures to improve the cash receipts reconciliation including running Core-CT deposit reports daily and updating the cash receipt log. Currently, the agency performs a monthly detailed reconciliation of cash receipts for large volume accounts and reconciles small volume accounts but will enhance this process to include the attaching of Core-CT back-up reports for these accounts in support of monthly reconciliations.”

Lack of Monitoring of Lending Partners

Background: Section 32-9yy of the General Statutes provides that the commissioner of DECD shall establish the Connecticut Credit Consortium, which shall be a small business assistance revolving loan program to provide direct loans and lines of credit to qualified businesses. A separate, non-lapsing small business assistance account (SBAA) was established for the purpose of funding the small business assistance revolving loan program.

Section 32-7g of the General Statutes established the Small Business Express program (EXP) within DECD to provide small businesses with various forms of financial assistance, including revolving loans to support growth, deferrable or forgivable job creation incentive loans, and matching grants. DECD may partner with lenders of the Connecticut Credit Consortium, established under Section 32-9yy of the General Statutes, to fulfill the requirements of the program.

The amount of loans receivable balances for the lending partners per DECD’s loans system is included on the state’s Comprehensive Annual Financial Report (CAFR).

Criteria: Adequate internal controls would include properly monitoring that service providers are using state funds for their intended purpose and ensuring that financial amounts provided by the service provider are accurate.

The DECD agreements with Small Business Assistance Account and Small Business Express lending partners require them to submit semi-annual reports on all loans (due within 45 days after June 30 and December 31).

Condition: DECD has not established adequate procedures to monitor the lending partners responsible for administering, servicing, and monitoring financial assistance provided under EXP and SBAA. Our review disclosed the following:

- DECD has not implemented procedures to ensure that lending partners are using funds in accordance with the lending agreements.

- DECD does not reconcile EXP and SBAA lending partner loans reported in semi-annual reports to amounts in its loan system. Reports from the lending partners indicate that some loans were written off, paid off, or forgiven, but the loans still have outstanding balances in DECD’s loan system. In addition, we noted SBAA loan payments that were posted to EXP loans in DECD’s loan system. The unreconciled loan balance reported by DECD as of June 30, 2019 was \$3,586,271 for SBAA and \$13,614,065 for EXP.

Context: DECD entered into lending agreements with 7 SBAA lending partners and 6 EXP lending partners to administer, service, and monitor the financial assistance. As of June 30, 2019, DECD provided SBAA lending partners with \$8,790,406 and EXP lending partners with \$31,985,000 to administer the programs.

Effect: By not adequately monitoring the lending partners, DECD has limited assurance that funds were used for the intended purposes and that the lending partner controls are properly designed and operating effectively. Furthermore, DECD recorded inaccurate loans receivable balances in the state’s Comprehensive Annual Financial Report (CAFR).

Cause: DECD has developed procedures to conduct onsite reviews of its lending partners. However, DECD did not implement these procedures during the audited period.

Prior Audit Finding: This finding has been previously reported in the last 2 audit reports covering the fiscal years ended June 30, 2013 to 2016.

Recommendation: The Department of Economic and Community Development should implement procedures to monitor the activities of its lending partners that administer, service, and monitor financial assistance provided under the Small Business Assistance Account and Small Business Express programs. In addition, the department should ensure that lending partner loans receivable balances are accurately and properly recorded in the state’s financial statements. (See Recommendation 19.)

Agency Response: “DECD agrees with the first condition in this finding. DECD had begun the process of onsite reviews of the lending partners in early 2020 and was scheduled to conduct the first review in March of 2020, however, because of the COVID-19 pandemic the review was cancelled. Future reviews will be scheduled and coordinated based on the lending partners availability.

DECD agrees with the second condition in this finding. Balances have been updated in the loan system and ongoing measures have been taken to enhance performance in this area.”

Terminated Lending Partners – Unassigned Loans

Background: Section 32-7g of the General Statutes established the Small Business Express program (EXP) within DECD to provide small businesses with various forms of financial assistance, including revolving loans to support growth, deferrable or forgivable job creation incentive loans, and matching grants. DECD may partner with lenders of the Connecticut Credit Consortium, established under Section 32-9yy of the General Statutes, to fulfill the requirements of the program.

Effective April 2012, DECD entered into lending agreements with 6 lending partners to administer, service, and monitor the financial assistance provided under the program and to provide ongoing technical assistance. In accordance with the terms of the agreements, DECD would annually provide the lending partners \$3,500 technical assistance services fees for each borrower and servicing fees equal to 3% of the outstanding principal balance of all of its loans. In addition, the lending partners could retain 50 percent of the interest received on loan portfolios.

DECD offered to provide each lending partner with \$1 million in new program funding if it accepted an amendment to the terms of the original agreement. Under the amended agreement, lending partners would no longer receive technical assistance service fees and would only receive annual service fees equal to 1.5% of the outstanding principal balance of all of its loans. In addition, the partners would return all interest they received on their loan portfolios to DECD. Effective June 30, 2015, DECD terminated agreements with two lending partners that did not agree to the proposed modifications.

Criteria: DECD's termination letter to the lending partners provides that they should assign all active loans to DECD and return any remaining funds.

Condition: One terminated lending partner did not assign its active loans to DECD.

Context: Outstanding loan balances for the terminated lending partner totaled \$1,399,853 as of June 30, 2019.

Effect: While DECD no longer paid the lending partner technical assistance and servicing fees, it continued to retain 50 percent of the interest collected on the loans. This resulted in DECD not receiving \$127,165 of interest payments.

Cause: DECD did not require the lending partner to assign its loans to the department.

Prior Audit Finding: This finding has not been previously reported.

Recommendation: The Department of Economic and Community Development should require terminated lending partners to transfer active loans to the department or sign an amended lending agreement. (See Recommendation 20.)

Agency Response: “DECD partially agrees with this finding. A termination letter was issued to the lending partner on June 26, 2015 in which DECD attempted to terminate its existing agreement with the lending partner. A modified agreement was sent to the lending partner stating the terms of a modified agreement in which the lending partner would assign all its active Small Business Express (EXP) loans and charge-offs to DECD. The lending partner declined to sign the modification agreement and is still actively managing the EXP loans in its portfolio. DECD has requested legal assistance to pursue the enforcement of the modification agreement with the lending partner.”

Inadequate Controls over Time and Attendance

Criteria: Section 5-245 of the General Statutes provides that employees can receive overtime pay when authorized by the employee’s appointing authority.

Collective bargaining agreements permit agency employees to earn compensatory time with prior supervisory approval. The P-5 bargaining unit agreement allows employees to bank up to 100 hours of compensatory time. If, at any time an employees’ compensatory time bank exceeds the 100-hour maximum, the employee shall be paid for the excess time as soon as practicable.

DECD policies and procedures require that the office/unit administrator and commissioner authorize compensatory time and overtime at least 24 hours in advance using the appropriate request form.

Some collective bargaining agreements require that employees charge leave time at a minimum increment. The NP-2 bargaining unit agreement requires all paid leave be taken in half-hour increments and charged against the employee’s leave records. The NP-3 bargaining unit agreement provides that employees are encouraged to use vacation credits in full days, but may use them in minimum increments of one hour.

Section 5-247-11 of the State Regulations requires the submission of an acceptable medical certificate signed by a licensed physician or other practitioner whose method of healing is recognized by the state to substantiate the use of sick leave for a period of more than five consecutive working days.

Condition: Our review of time and attendance during the fiscal years ended June 30, 2017, 2018, and 2019 disclosed the following:

- A review of 201 instances of overtime paid to 5 employees disclosed the following:
 - Request forms were not on hand in 5 instances.
 - DECD did not approve overtime in advance in 3 instances.
 - DECD paid more overtime than was approved on the request forms in 23 instances.
- A review of 196 instances of compensatory time for 5 employees disclosed the following:
 - Request forms were not on hand in 16 instances.
 - DECD did not preapprove compensatory time in 11 instances.
 - DECD had 3 of the 5 employees reviewed enrolled in the wrong compensatory time plan in Core-CT. The 3 employees were in the P-5 bargaining unit. As a result, they could bank more than 100 hours of compensatory time in violation of the bargaining unit contract.
- Our review disclosed that 11 NP-2 and NP-3 bargaining unit employees charged leave time 67 times in increments less than allowed by their contracts during the audited period.
- Our review of 3 employees that took more than 5 consecutive sick days disclosed that DECD did not have a medical certificate on file for one employee.

Context: During the audited period, DECD paid 21 employees \$73,162 in overtime, 39 employees earned 2,248 hours of compensatory time, and 10 employees took more than 5 consecutive sick days.

Effect: There is reduced assurance that DECD properly authorized all earned compensatory time and overtime and complied with the time and attendance requirements in collective bargaining agreements. Our review disclosed that DECD supervisors did not preapprove \$2,345 of overtime and 78 hours of compensatory time. In addition, without obtaining medical certificates for employees with more than 5 consecutive sick days, there is an increased risk that sick leave abuse may go undetected.

Cause: Controls over time and attendance are inadequate.

Prior Audit Finding: This finding has been previously reported in the last 6 audit reports covering the fiscal years ended June 30, 2005 to 2016.

Recommendation: The Department of Economic and Community Development should ensure that it follows time and attendance requirements as promulgated in the General Statutes, state regulations, collective bargaining agreements, and department policies. (See Recommendation 21.)

Agency Response: “DECD agrees with condition one of the finding. The agency has implemented the appropriate measures for the approval and usage of compensatory/overtime.

DECD agrees with condition two of the finding. An updated process has been implemented to facilitate efficient approvals of over/comp time. As of 5/24/19, these three employees were enrolled in the correct Comp time plan.

DECD agrees with condition three of the finding. All NP-2 and NP-3 employees and their supervisors have been reminded of the requirement to charge leave time in minimum increments.

DECD agrees with condition four of the finding. This finding relates to an employee who reports directly to the Governor’s Office and is assigned to DECD for administrative support purposes exclusively. DECD has communicated this finding to the individual responsible for approving the employee’s timesheet for the appropriate corrective action(s).”

Circumvention of Hiring Procedures

Background: DECD entered into a memorandum of understanding (MOU) with Connecticut Innovations (CI) for a CI employee’s consulting services. The CI employee worked in the DECD Office of Brownfield Remediation and Development from June 1, 2014 until March 29, 2019.

Criteria: Chapter 67 of the General Statutes known as the State Personnel Act contains the state’s hiring policies.

The P-4 bargaining unit agreement provides that in order to limit long-term reliance on consultants that an agency may hire due to a lack of in-house knowledge or skill, any such consultant contract shall contain a provision that provides for training the agency employees.

Condition: DECD circumvented hiring procedures by relying on the work of a consultant for almost five years rather than hiring a bargaining unit employee. For much of this time, it appears that the consultant was performing similar work to the bargaining unit employees in the Brownfield unit. In addition, the memorandum of understanding did not have a training provision for agency employees.

Context: DECD reimbursed Connecticut Innovations \$793,009 for the employee's salary, fringe benefits, travel and other out-of-pocket expenses.

Effect: DECD did not comply with the State Personnel Act and requirements included in the P-4 bargaining unit agreement. In addition, it appears DECD reimbursed CI more than it would have paid a bargaining unit employee.

Cause: DECD initially hired the consultant as a subject area expert when the department's Brownfield program began to experience considerable activity. It is unclear why the department continued using the consultant's services for so long.

Prior Audit Finding: This finding has not been previously reported.

Recommendation: The Department of Economic and Community Development should comply with the State Personnel Act and bargaining unit agreements by not relying on consultants' work for extended periods for tasks that department employees can perform. (See Recommendation 22.)

Agency Response: "DECD disagrees with the finding. The individual who provided the services was an employee of CT Innovations (CI), a State of CT quasi-public agency, and DECD entered into a memorandum of agreement (MOA) with CI addressing the provision of the services. Conn. Gen. Stat. sec. 32-11(4) states that the commissioner of DECD shall have the power "To enter into such agreements with CI as may be appropriate for the purpose of performing its duties which agreements may include, but shall not be limited to, provisions for the delivery of services by CI to third parties, provisions for payment by the department to CI for the delivery of such services, provisions for advances and reimbursements to the department for any expenses incurred or to be incurred by it in delivery of any services, assistance, revenues, rights, assets and interests and provisions for the sharing with CI of assistants, agents and other consultants, professionals and employees, and facilities and other real and personal property used in the conduct of the department's affairs". In addition, CGS sec. 32-35(f) states the following: (f) The corporation shall have the authority to contract with the Department of Economic and Community Development for administrative or other services."

*Auditors' Concluding
Comments:*

While DECD is permitted to enter into an agreement with Connecticut Innovations for consulting services, DECD circumvented hiring procedures by relying on the work of the consultant for almost five years rather than hiring a bargaining unit employee. The CI employee performed similar work to bargaining unit employees and likely cost the department more.

Missing and Incorrect Reports

Criteria: DECD is required to comply with numerous reporting requirements set forth by the General Statutes and public and special acts. These reports are due at different times throughout the year. An adequate system of internal control should include a method for management to track and monitor the submission of mandated reports.

The Office of the State Comptroller requires state agencies to annually prepare and submit Generally Accepted Accounting Principles (GAAP) closing packages. Agency submissions contain financial information not available on the state's Core-CT accounting system. The Office of the State Comptroller uses this information in preparation of the state's financial statements. The State Accounting Manual and the State Comptroller's GAAP closing and reporting instructions stipulate the procedures for completing GAAP reporting forms.

Condition: DECD did not submit the following reports:

- Annual report on the registry of small businesses owned by veterans required by Section 32-1t of the General Statutes
- Biennial report of the strategic plan for culture and tourism required by Section 10-392 of the General Statutes
- Annual report of job skills required by Section 31-362b of the General Statutes
- Report on the Stranded Research and Development Tax Credit Program required by Special Act 16-21, due on January 1, 2017
- Study of certain employment transitions in eastern Connecticut required by Special Act 16-12, due January 1, 2017

DECD overstated contractual obligations reported in the GAAP closing package for the fiscal year ended June 30, 2018 by \$8,980,443, overstated interest and late fees receivable by \$612,737, understated receivables estimated to be uncollectible by \$1,242,914, and overstated the amount of receivables collected through August 31st by \$405,877. In addition, DECD understated contractual obligations by \$21,630,403 and interest and late fee receivables estimated to be uncollectible by \$901,958 for the fiscal year ended June 30, 2019.

Effect: DECD did not comply with reporting requirements established by the General Statutes, public and special Acts, and the Office of the State Comptroller.

Cause: Section 32-1t of the General Statutes provided that DECD establish the registry of small businesses owned by veterans within available resources. Due to a lack of appropriations, the department did not create the registry.

As a result, there was no data to report. In addition, DECD did not think the annual report of job skills was necessary since it duplicates reports prepared by the Office of Workforce Competitiveness. Other reports were not prepared due to a lack of administrative oversight.

Errors noted in the GAAP closing packages were due to clerical mistakes and the department's misunderstanding of the Office of the State Comptroller's reporting instructions. In addition, DECD did not develop a sufficient method to estimate the amount of uncollectible receivables.

Prior Audit Finding: This finding has not been previously reported.

Recommendation: The Department of Economic and Community Development should ensure all required reports are complete and accurate. In addition, the department should pursue the repeal of statutes requiring reports that are duplicative or are no longer necessary. (See Recommendation 23.)

Agency Response: "DECD agrees with the first condition in this finding. The agency will seek a repeal of the statutes establishing some of these reports, as some of the reports are a duplication of other reports that DECD prepares and others are no longer necessary.

DECD agrees with the second condition in this finding. In FY 19-20 DECD performed a GAAP reporting LEAN from which corrective and performance enhancement measures were implemented. Individual staff has received training where appropriate."

Asset Management Not in Accordance with Prescribed Procedures

Criteria: Section 4-36 of the General Statutes requires that each state agency establish and maintain an inventory account in the form prescribed by the State Comptroller, and shall annually, on or before October 1st, transmit a detailed inventory as of June 30th of all real property and personal property to the Comptroller.

The State of Connecticut Property Control Manual provides the following standards and procedures for maintaining a property control system.

- Agencies should report the value of all capitalized real and personal property on the CO-59 Asset Management/Inventory Report/GAAP Reporting Form.
- Property records should be complete and accurate and should contain sufficient information to adequately track and report items. At a minimum, this information should include item description, cost, tag number, and location.

- Agencies should tag all personal property unless tagging the item would be impractical or would otherwise alter the item's usefulness. The tag should provide a unique number and the property owner's name.
- Agencies should continuously survey property to determine which assets are no longer needed, reassign property among its activities when it is no longer required for its current use, and report personal property that become surplus to an agency's needs, is unserviceable, obsolete, or otherwise unusable to the State Property Distribution Center.
- Appraisals for works of art and historical treasures are no longer a mandatory, but are highly recommended when resources are available.

Condition:

Our review of DECD's property control system disclosed the following.

- We selected 30 items from DECD inventory records and 25 items during a physical inspection of DECD assets to verify that the department properly included the items in its inventory records. Our review disclosed the following:
 - We could not locate one item in the inventory records.
 - We found one item in a different location than DECD indicated in its inventory records.
- We noted that DECD purchased 7 iPads 5 years ago that were not regularly used. DECD never used 3 of the iPads and had not used the other 4 for over 4 years.
- We noted that DECD used an incomplete appraisal list of art and historical treasures to prepare the CO-59 Asset Management/Inventory Report/GAAP Reporting Form. DECD's inventory records for one of its museums included over 1,200 items that were not on the appraisal list. DECD did not record values in the inventory records for these items.

Context:

DECD reported \$6,607,128, \$5,909,068, and \$7,407,515 in real and personal property for the fiscal year ended June 30, 2017, 2018, and 2019, respectively.

Effect:

If DECD does not maintain accurate inventory records, there is an increased risk that inventory can be lost or stolen and a decreased possibility of detecting such activity. In addition, unused equipment could become obsolete. Inventory amounts reported on the state's Comprehensive Annual Financial Report are inaccurate.

Cause: DECD has not made a sufficient effort to maintain accurate inventory records in accordance with the State of Connecticut Property Control Manual. In addition, DECD purchased the iPads for the state's welcome centers, which closed shortly after the purchase.

Prior Audit Finding: This finding has been previously reported in the last 3 audit reports covering the fiscal years ended June 30, 2011 to 2016.

Recommendation: The Department of Economic and Community Development should improve internal controls and should maintain its property control system in accordance with the State of Connecticut Property Control Manual. In addition, the department should reassign unused equipment or report it to the State Property Distribution Center. (See Recommendation 24.)

Agency Response: "The agency partially disagrees with the finding and has made consistent efforts to address the management of its physical assets. For condition number one, the agency is not clear which item could not be located, as the POS port Tag # 11612 is not required to be part of the inventory.

The agency partially disagrees with second condition in this finding. The IPADS in question were purchased for the Welcome Centers which were closed prior to the units being utilized for their intended purpose. The units were deployed intermittently as appropriate including to the museums. After the closing of the Welcome Centers ongoing dialogue regarding re-opening and the low residual value of the units made it inappropriate to dispose of them. When the Welcome Centers were re-opened, the units were updated and deployed as appropriate.

The agency agrees with this finding and has made extensive effort to catalogue a collection of tens of thousands of historic artifacts. These artifacts are extremely difficult to value accurately and we have had ongoing discussions with the Comptroller's office regarding the handling of this matter. Efforts to address this matter will continue as resources allow."

Auditors' Concluding Comments:

DECD tagged the POS Port but did not include it in its inventory records. The department did not provide documentation to support that the item was not required to be included in its inventory records.

Failure to Delete Core-CT Access for Separated Employees

Criteria: Core-CT is the state's integrated human resources, payroll, and financial system. The Core-CT Security Liaison Guide states that each agency is responsible for assigning one or more Core-CT Security Liaisons to be the point of contact for security related requests, issues, and communications.

The agency liaison is responsible for locking out functional Core-CT users immediately upon an employee's termination.

Condition: Our review disclosed that DECD did not immediately deactivate Core-CT access to 9 employees, 5 of whom accessed the system after their termination dates.

Context: During the fiscal years ended June 30, 2017, 2018, and 2019, 16 functional Core-CT users retired, transferred to another agency, or terminated their employment.

Effect: DECD did not promptly terminate former employees' access to Core-CT, which resulted in an increased risk of unauthorized access to the system and possible manipulation of data.

Cause: DECD has not established appropriate controls to deactivate the Core-CT access of separated employees.

Prior Audit Finding: This finding has been previously reported in the last audit report covering the fiscal years ended June 30, 2015 and 2016.

Recommendation: The Department of Economic and Community Development should immediately deactivate the Core-CT access of separated employees. (See Recommendation 25.)

Agency Response: "DECD agrees with this finding. All accesses were reviewed and have been terminated when this finding was originally identified in the prior audit report. Internal control procedures have been implemented to ensure that former employees that have been separated from State service will no longer have access to Core-CT."

Review of Boards, Councils, Committees, and Commissions

Background: The General Statutes relating to the Department of Economic and Community Development provide for the following boards, councils, committees, and commissions, which we will collectively refer to as boards.

- Commission on Connecticut's Future
- Committee for the Restoration of Historic Assets in Connecticut
- Connecticut Arts Council
- Culture and Tourism Advisory Committee
- Historic Preservation Council
- Manufacturing Innovation Advisory Board
- Small Business Advisory Board
- Sports Advisory Board
- State Historic Preservation Board

- Technology Talent Advisory Committee

Criteria:

Section 1-225 of the General Statutes requires the meetings of all state agencies to be available for public inspection and posted to the agency's website no later than 7 days after the meeting. Public agencies must file their schedule of regular meetings for the ensuing year with the Secretary of the State no later than January 31st of each year and post the schedule on their website. In addition, public agencies must file the agenda of meetings with the Secretary of State not less than 24 hours before a meeting and post such agenda on the agency's website.

Section 10-408a of the General Statutes provides that any member of the Connecticut Arts Council who fails to attend three consecutive meetings or who fails to attend 50 percent of all meetings held during a calendar year shall be deemed to have resigned. Seven voting members of the council shall constitute a quorum for the transaction of any business for the exercise of any power of the council.

Section 10-409 of the General Statutes provides that any member of the Historic Preservation Council who fails to attend three consecutive meetings or who fails to attend 50 percent of all meetings held during a calendar year shall be deemed to have resigned.

Section 10-393 of the General Statutes established the Culture and Tourism Advisory Committee to provide guidance to DECD with regard to enhancing and promoting culture, history, the arts, and the tourism and digital media and motion picture industries in Connecticut.

Section 32-6a of the General Statutes established the Committee for the Restoration of Historic Assets in Connecticut for the purposes of encouraging quality tourism and contributing to an overall historic preservation program.

Section 32-9xx of the General Statutes established the Small Business Advisory Board to provide guidance to DECD regarding resources available to small businesses, and requires that the board meet on or before December 31, 2010, and at least annually thereafter.

Section 32-245 of the General Statutes established the Commission on Connecticut's Future, and required the commission to submit a report concerning the economic renewal of Connecticut to the Governor and the General Assembly on or before December 1, 2014. In addition, the statute required the chairperson to call a meeting not later than October 1, 2013 and at other times as deemed necessary.

Section 10-425 of the General Statutes established a Sports Advisory Board to advise the commissioner of DECD on the most effective ways to utilize state resources to promote, attract, and market in-state professional and amateur sports and sporting events.

Condition:

Our review of the DECD boards disclosed the following:

- DECD did not post approved meeting minutes for 3 Connecticut Arts Council and 6 Historic Preservation Council meetings on its website during the audited period.
- DECD did not file the 2020 schedule of meetings for the State Historic Preservation Board, Historic Preservation Council, and Sports Advisory Board with the Secretary of the State by the January 31st deadline. In addition, the Connecticut Arts Council, Culture and Tourism Advisory Committee, State Historic Preservation Board, and Sports Advisory Board did not have their 2020 schedules of meetings posted to the DECD website by the January 31st deadline.
- DECD did not post the most recent meeting agendas for the State Historic Preservation Board and Sports Advisory Board.
- A review of board meeting attendance disclosed that 2 members of the Connecticut Arts Council and one member of the Historic Preservation Council missed three consecutive meetings and/or failed to attend fifty percent of all the meetings in a calendar year. These board members continued to serve, despite being deemed to have resigned.
- The Connecticut Arts Council failed to have a quorum in 5 of 16 meetings during the audited period but still conducted votes for the approval of business transactions.
- DECD informed us that the Commission on Connecticut's Future, the Committee for the Restoration of Historic Assets in Connecticut, and the Small Business Advisory Board are not active and the Culture and Tourism Advisory Committee is no longer necessary due to the creation of the Connecticut Tourism Council in Public Act 19-178. In addition, the Sports Advisory Board did not meet regularly during the audited period and only a quarter of the members attended the meetings.

Effect:

Some of the boards did not comply with freedom of information requirements. As a result, the public was not able to review board activities. In addition, some boards did not actively meet in accordance with the General Statutes, and members failed to regularly attend meetings. Failure to have a quorum can delay the boards' work. In addition, certain

Connecticut Arts Council votes may not be valid due to the lack of a quorum.

Cause: A lack of administrative oversight and resources contributed to these conditions.

During the 2018 legislative session, DECD submitted a proposal to eliminate the Sports Advisory Board. In addition, during the 2020 session, DECD submitted a proposal to eliminate the Commission on Connecticut's Future, the Committee for the Restoration of Historic Assets in Connecticut, the Culture and Tourism Advisory Committee, and the Small Business Advisory Board. These proposals did not pass.

Prior Audit Finding: This finding has been previously reported in the last 2 audit reports covering the fiscal years ended June 30, 2013 to 2016.

Recommendation: The Department of Economic and Community Development should work with its boards to ensure that they comply with the Freedom of Information Act and applicable General Statutes. Boards with attendance issues should notify their appointing authorities to ensure adequate representation at all meetings.

In addition, the department should pursue the repeal of the statutes establishing the Commission on Connecticut's Future, the Committee for the Restoration of Historic Assets in Connecticut, the Small Business Advisory Board, the Culture and Tourism Advisory Committee, and the Sports Advisory Board if they are no longer active or necessary. (See Recommendation 26.)

Agency Response: "DECD agrees with conditions one, two and three in this finding that the CT Office of the Arts (COA) and CT State Historic Preservation Board (SHPO) did not post 3 CT Arts Council and 6 Historic Preservation Council meeting minutes on their website during the period of audit, that the 2020 schedule of meetings for the CT Arts Council, State Historic Preservation Board and Historic Preservation Council were not posted to the Secretary of State by the January 31 deadline; and that the most recent meeting agendas for the SHPO were not posted. COA administrative staff and SHPO administrative staff will add notes to their calendars to ensure that all meetings, agendas, and minutes are posted as defined in statute. The Director of Arts, Preservation and Museums and the Director of Operations for SHPO will monitor oversight and ensure the adoption of policies and procedures to rectify these errors.

DECD agrees with condition four and five in this finding regarding required attendance for Council members at CT Arts Council meetings that 2 members of the CT Arts Council and 1 member of the Historic Preservation

Council (HPC) missed three consecutive meetings and/or failed to attend fifty percent of all the meetings held in a calendar year, and continued to serve, despite being deemed to have resigned. COA and SHPO staff will create a document that will be read at the beginning of each council meeting to remind the board chair and council members of the quorum for meetings, and requirements for attendance. COA and HPC administrative staff will create a spreadsheet to document attendance at Council meetings. Council members who are in danger of being noncompliant will be notified.

DECD agrees with condition six in this finding regarding the need to decommission the old Committee for the Restoration of Historic Assets in Connecticut and will support the Agency in legislative work to repeal the statutes that created the Restoration of Historic Assets in Connecticut, as it has not been active.”

RECOMMENDATIONS

Status of Prior Audit Recommendations:

Our prior audit report on the Department of Economic and Community Development contained 20 recommendations. 3 have been implemented or otherwise resolved and 17 have been repeated or restated with modifications during the current audit.

- The Department of Economic and Community Development should ensure that the amount of financial assistance it provides to a business is not greater than amounts allowed under the General Statutes without obtaining authorization from the General Assembly. **This recommendation is being repeated. (See Recommendation 2.)**
- Prior to amending an assistance agreement, the Department of Economic and Community Development should notify the State Bond Commission and should ensure that changes would result in an economic benefit to the state. In addition, DECD should document the reason for amending assistance agreements. **This recommendation is being repeated. (See Recommendation 3.)**
- The Department of Economic and Community Development should conduct financial reviews for all financial assistance provided, including assistance provided under the First Five Plus program. In addition, DECD should clearly document that any financial review concerns have been sufficiently resolved. **This recommendation is being repeated. (See Recommendation 4.)**
- The Department of Economic and Community Development should ensure that it requires companies to repay all forms of financial assistance if they relocate out of state within the relocation period, and should implement adequate procedures to determine whether companies have relocated out of state. In addition, DECD should seek clarification whether Section 32-5a of the General Statutes applies to tax credits and should establish policies to apply consistent relocation requirements to tax credits. **This recommendation is being repeated. (See Recommendation 9.)**
- The Department of Economic and Community Development should ensure that it only reimburses eligible project costs and that recipients meet assistance agreement payment requirements before disbursing funds. **This recommendation is being restated. (See Recommendation 6.)**
- The Department of Economic and Community Development should ensure that it performs a complete review of all projects from application until financial closeout. In addition, the department should ensure that assistance agreement requirements are followed. **This recommendation is being repeated. (See Recommendation 5.)**

- The Department of Economic and Community Development should ensure that job audits are properly prepared and reviewed in a timely manner. In addition, DECD should ensure that companies meet job creation and retention requirements prior to granting loan forgiveness. **This recommendation is being repeated. (See Recommendation 8.)**
- The Department of Economic and Community Development should ensure that financial assistance is properly documented using an assistance agreement that stipulates the terms and conditions of the assistance. **This recommendation has been resolved.**
- The Department of Economic and Community Development should complete its due diligence before providing additional funding to a company, especially if the company is delinquent on past loans or has demonstrated an inability to create and retain jobs. As part of that due diligence, DECD should perform closeouts and job reviews on older projects before funding new projects. **This recommendation is being repeated. (See Recommendation 12.)**
- The Department of Economic and Community Development should limit the time it defers loan payments and should establish clear guidelines for when borrowers should qualify for loan modifications. **This recommendation is being repeated. (See Recommendation 13.)**
- The Department of Economic and Community Development should enter advances into the loan management system in a timely manner and should ensure that it sets up loans in accordance with the repayment terms of the promissory notes. **This recommendation is being repeated. (See Recommendation 7.)**
- The Department of Economic and Community Development should ensure that loan interest is calculated and billed or capitalized in accordance with financial assistance agreements. **This recommendation is being repeated. (See Recommendation 16.)**
- The Department of Economic and Community Development should strengthen its internal controls to ensure that the amount of loan receivables reported to the Office of the State Comptroller is accurate and includes estimated uncollectible receivables. **This recommendation is being repeated. (See Recommendation 15.)**
- The Department of Economic and Community Development should establish and implement procedures to monitor the activities of its lending partners that administer, service, and monitor financial assistance provided under the Small Business Assistance Account and Small Business Express programs. In addition, the department should ensure that lending partner loan receivable balances are accurately and properly recorded in the state's financial statements. **This recommendation is being repeated. (See Recommendation 19.)**

- The Department of Economic and Community Development should ensure that all travel expenses are necessary and reasonable and that any unused airline tickets are credited or reused. In addition, employees should reimburse the department for any travel costs incurred for their personal convenience. **This recommendation has been resolved.**
- The Department of Economic and Community Development should ensure that it follows time and attendance requirements in the General Statutes, collective bargaining agreements, and DECD policies. **This recommendation is being repeated. (See Recommendation 21.)**
- The Department of Economic and Community Development should strengthen its internal controls to ensure that funds are committed prior to purchasing goods and services. **This recommendation has been resolved.**
- The Department of Economic and Community Development should improve internal controls and should maintain its property control system in accordance with the State of Connecticut Property Control Manual. **This recommendation is being repeated. (See Recommendation 24.)**
- The Department of Economic and Community Development should immediately deactivate the Core-CT access of separated employees. **This recommendation is being repeated. (See Recommendation 25.)**
- The Department of Economic and Community Development should work with its boards to ensure that they comply with the Freedom of Information Act and applicable General Statutes. Boards with attendance issues should notify their appointing authorities to ensure adequate representation at all meetings.

In addition, the department should either pursue the repeal of the statutes establishing the Commission on Connecticut's Future, the Committee for the Restoration of Historic Assets in Connecticut, and the Small Business Advisory Board if they are no longer active or necessary. **This recommendation is being repeated. (See Recommendation 26.)**

Current Audit Recommendations:

- 1. The Department of Economic and Community Development should ensure that digital animation companies do not receive more than \$15 million in tax credits in any one fiscal year as required by Section 12-217ll of the General Statutes.**

Comment:

DECD issued a digital animation company \$49,410,602 more in film production tax credits than it would have been entitled to under the digital animation tax credit program.

- 2. The Department of Economic and Community Development should ensure that the amount of financial assistance it provides to a business is not greater than amounts allowed under the General Statutes without obtaining authorization from the General Assembly.**

Comment:

DECD awarded \$1,500,000 more in financial assistance than permitted under the General Statutes.

- 3. The Department of Economic and Community Development should ensure that amendments or modifications to assistance agreements would result in an economic benefit to the state and should notify the State Bond Commission of these changes when applicable. In addition, the department should document its reason for amending or modifying assistance agreements.**

Comment:

Our review disclosed that DECD amended the assistance agreements for 4 companies, which resulted in the companies receiving \$1,719,219 of loan forgiveness that they would not have been entitled to under the original agreements. DECD did not document whether changes would result in an economic benefit to the state. In one case, DECD did not notify the State Bond Commission of the changes and did not perform an updated economic impact analysis.

- 4. The Department of Economic and Community Development should conduct financial reviews for all of its funding in the First Five, Brownfield, and Manufacturing Assistance Act programs. In addition, the department should clearly document that any financial review concerns have been sufficiently resolved.**

Comment:

Our review of 25 projects, for which DECD provided \$129,659,000 in financial assistance, disclosed that the department did not perform a financial review for 7 projects totaling \$97

million, did not verify whether 4 companies that received \$23.2 million in assistance had pending litigation, and did not determine whether one company that received \$22 million in assistance owed outstanding taxes to the Department of Revenue Services.

- 5. The Department of Economic and Community Development should ensure that it performs a complete review of all projects from application until financial closeout.**

Comment:

Our review of 33 project files identified that DECD was missing an application for one project and rating and ranking scores for 3 projects, did not conduct an economic impact analysis for one project, did not include a budget period for one project, and did not sufficiently document that onsite monitoring was performed for 4 projects. In addition, in 9 cases, DECD did not obtain required project administration plans or periodic reports such as state single audits, financial statements, and milestone and progress reports.

A review of 20 project closeouts identified that DECD did not close out 8 projects for 1 to 4 years. In addition, DECD was missing supporting documentation for the closeout of 5 projects.

- 6. The Department of Economic and Community Development should ensure that it only pays for eligible project costs.**

Comment:

DECD improperly advanced \$264,996 for an Urban Act project.

- 7. The Department of Economic and Community Development should enter advances or forgiveness into the loan management system in a timely manner and should ensure that it sets up loans in accordance with the repayment terms of the promissory notes or loan modification letters.**

Comment:

Our review of 9 Manufacturing Assistance Act, 4 Brownfield, and 12 Small Business Express loan projects disclosed that DECD did not input loan advances for 6 loans into the loan management system in a timely manner, did not input loan forgiveness for one loan, and improperly setup one loan. In addition, the department did not properly set up 5 other loans in its loan management system.

- 8. The Department of Economic and Community Development should ensure that it receives and reviews recipient job audits in a timely manner. In addition, the department should promptly and correctly apply penalties or loan forgiveness that results from those reviews.**

Comment:

Our review disclosed that DECD did not receive job audits for all projects, accepted improperly prepared audits, and did not always promptly review them. In addition, DECD incorrectly calculated the amount of jobs retained for some projects and did not properly apply a penalty that resulted from a review.

- 9. The Department of Economic and Community Development should ensure that it requires companies to repay all forms of financial assistance if they relocate out of state within the relocation period, and should implement adequate procedures to determine whether companies have relocated out of state.**

Comment:

During the prior audit, we noted that DECD did not consistently apply relocation requirements to tax credits. Our review of 5 Urban and Industrial Site Reinvestment tax credits disclosed that the department did not require two companies to repay the credits when they relocated out of state. DECD awarded \$2,725,518 of the \$27,255,184 approved tax credits for these projects.

- 10. The Department of Economic and Community Development should adequately monitor grant recipients and should ensure that they comply with reporting requirements. In addition, the department should complete its due diligence and sufficiently gauge the demand for equipment prior to awarding a grant for its purchase and should ensure that the grantee uses the equipment for a sufficient period.**

Comment:

DECD did not sufficiently gauge demand for equipment prior to awarding a grant for its purchase, did not require the grantee to use the equipment for a minimum period, and did not sufficiently plan for its use after the expiration of a grant award.

DECD issued a letter to the grantee ordering it to cease and desist using the equipment. DECD paid \$6,533,109 to the grantee under various assistance agreements despite the grantee not fulfilling reporting requirements in the letter. The grantee did not submit quarterly reports on how many hours it used the equipment, and provided other reports that were inconsistent and unsupported.

- 11. The Department of Economic and Community Development should ensure it gives the regional tourism districts sufficient time to spend grant funds and should ensure that the districts comply with the General Statutes and requirements in grant agreements. In addition, the department should require the tourism districts to submit a copy of their board-approved partner agreements.**

Comment:

DECD did not provide funding to the tourism districts in a timely manner. DECD funded one district 22 days before the end of the budget period and funded the other district 8 days before the end of the budget period. In addition, our review of one tourism district disclosed the district entered into a partnership agreement run by its chairman; the district's insurance policy was not effective until after DECD disbursed the funds and the district spent them; and the district did not make the minutes of its board meeting publicly available and post it on CTvisit.com within 7 days of the meeting.

- 12. The Department of Economic and Community Development should complete its due diligence before providing additional funding to a company, especially if the company is delinquent on past loans or has demonstrated an inability to create and retain jobs. As part of that due diligence, DECD should perform job reviews on older projects before funding new projects.**

Comment:

DECD provided a \$150,000 loan to a company that was delinquent on a previous DECD loan. The company never made a payment on its original loan. In addition, DECD did not complete a job review on prior financial assistance before awarding the company the second loan.

- 13. The Department of Economic and Community Development should limit the time it defers loan payments and should establish clear guidelines for when borrowers should qualify for loan modifications.**

Comment:

We noted 21 loans totaling \$4,888,571 that DECD modified multiple times to defer principal and interest payments. These modifications resulted in DECD deferring principal and interest payments between 2 years and 4 years 8 months.

- 14. The Department of Economic and Community Department should ensure that it collects the proper amount of application and annual fees for Urban and Industrial Site Reinvestment tax credits prior to their issuance.**

Comment:

DECD did not collect a \$10,000 application fee before issuing a \$2 million tax credit to a company and overcharged a company an \$18,000 application fee and a \$3,000 annual fee.

- 15. The Department of Economic and Community Development should strengthen its internal controls to ensure that the amount of loans receivable reported to the Office of the State Comptroller is accurate and includes estimated uncollectible receivables.**

Comment:

DECD overstated reported receivable balances by \$3,052,378 and \$4,167,873 for the fiscal years ended June 30, 2017 and 2018, respectively. In addition, DECD has not developed a sufficient method to estimate the amount of uncollectible receivables.

- 16. The Department of Economic and Community Development should ensure that loan interest is calculated and billed or capitalized in accordance with financial assistance agreements.**

Comment:

Our review disclosed that DECD incorrectly set up 5 loans, totaling \$5 million, by using the wrong interest calculation method. In addition, we reviewed 10 receivables and noted that DECD incorrectly calculated the interest billed or capitalized for 3 loans.

- 17. The Department of Economic and Community Development should post deposits in a timely manner.**

Comment:

DECD did not post 2 deposits, totaling \$606,676, in a timely manner. DECD posted the deposits 2 days late.

- 18. The Department of Economic and Community Development should prepare monthly reconciliations of all cash receipts.**

Comment:

DECD did not properly reconcile total cash receipts to the amounts entered into Core-CT.

- 19. The Department of Economic and Community Development should implement procedures to monitor the activities of its lending partners that administer, service, and monitor financial assistance provided under the Small Business Assistance Account and Small Business Express programs. In addition, the department should ensure that lending partner loans receivable balances are accurately and properly recorded in the state's financial statements.**

Comment:

DECD has not established adequate procedures to monitor the lending partners responsible for administering, servicing, and monitoring financial assistance provided under the Small Business Express (EXP) and Small Business Assistance Account (SBAA) programs. The department has not implemented procedures to ensure that lending partners are using funds in accordance with their lending agreements and does not reconcile EXP and SBAA lending partner loans as reported in semi-annual reports to amounts in its loan system.

- 20. The Department of Economic and Community Development should require terminated lending partners to transfer active loans to the department or sign an amended lending agreement.**

Comment:

One terminated Small Business Express lending partner did not assign its active loans to DECD.

- 21. The Department of Economic and Community Development should ensure that it follows time and attendance requirements as promulgated in the General Statutes, state regulations, collective bargaining agreements, and department policies.**

Comment:

Our review disclosed that DECD did not properly authorize all compensatory and overtime and did not comply with the time and attendance requirements in collective bargaining agreements. In addition, DECD did not obtain a medical certificate for an employee that took more than 5 consecutive sick days.

- 22. The Department of Economic and Community Development should comply with the State Personnel Act and bargaining unit agreements by not relying on consultants' work for extended periods for tasks that department employees can perform.**

Comment:

DECD circumvented hiring procedures by relying on the work of a consultant for almost five years rather than hiring a bargaining unit employee.

- 23. The Department of Economic and Community Development should ensure all required reports are complete and accurate. In addition, the department should pursue the repeal of statutes requiring reports that are duplicative or are no longer necessary.**

Comment:

DECD did not submit five reports required by the General Statutes and public and special acts. In addition, the department reported incorrect amounts to the Office of the State Comptroller.

- 24. The Department of Economic and Community Development should improve internal controls and should maintain its property control system in accordance with the State of Connecticut Property Control Manual. In addition, the department should reassign unused equipment or report it to the State Property Distribution Center.**

Comment:

The DECD inventory records did not reflect the actual assets on hand. We could not locate an item listed in the inventory records and found one item in a different location. Our review also noted inventory items that the department was not regularly using.

DECD used an incomplete appraisal list of art and historical treasures for one of its museums to prepare the CO-59 Asset Management/Inventory Report/GAAP Reporting Form. The list was missing over 1,200 items.

- 25. The Department of Economic and Community Development should immediately deactivate the Core-CT access of separated employees.**

Comment:

Our review disclosed that the department did not immediately deactivate Core-CT access to 9 employees that had retired, transferred to another agency, or terminated their employment, 5 of whom accessed the system after their termination dates.

- 26. The Department of Economic and Community Development should work with its boards to ensure that they comply with the Freedom of Information Act and applicable General Statutes. Boards with attendance issues should notify their appointing authorities to ensure adequate representation at all meetings.**

In addition, the department should pursue the repeal of the statutes establishing the Commission on Connecticut's Future, the Committee for the Restoration of Historic Assets in Connecticut, the Small Business Advisory Board, the Culture and Tourism Advisory Committee, and the Sports Advisory Board if they are no longer active or necessary.

Comment:

Our review disclosed that some DECD boards did not comply with freedom of information requirements. In addition, some boards did not actively meet in accordance with the General Statutes, and members failed to regularly attend meetings.

ACKNOWLEDGMENTS

The Auditors of Public Accounts wish to express our appreciation for the courtesies and cooperation extended to our representatives by the personnel of the Department of Economic and Community Development during the course of our examination.

The Auditors of Public Accounts also would like to acknowledge the auditors who contributed to this report:

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